

## § 26.2654-1 Certain trusts treated as separate trusts.

### (a) *Single trust treated as separate trusts* —

#### (1) *Substantially separate and independent shares* —

- (i) *In general.* If a single trust consists solely of substantially separate and independent shares for different beneficiaries, the share attributable to each beneficiary (or group of beneficiaries) is treated as a separate trust for purposes of Chapter 13. The phrase “substantially separate and independent shares” generally has the same meaning as provided in § 1.663(c)-3. However, except as provided in paragraph (a)(1)(iii) of this section, a portion of a trust is not a separate share unless such share exists from and at all times after the creation of the trust. For purposes of this paragraph (a)(1), a trust is treated as created at the date of death of the grantor if the trust is includible in its entirety in the grantor's gross estate for Federal estate tax purposes. Further, except with respect to shares or trusts that are treated as separate trusts under local law, treatment of a single trust as separate trusts under this paragraph (a)(1) does not permit treatment of those portions as separate trusts for purposes of filing returns and payment of tax or for purposes of computing any other tax imposed under the Internal Revenue Code. Also, additions to, and distributions from, such trusts are allocated pro rata among the separate trusts, unless the governing instrument expressly provides otherwise. See § 26.2642-6 and paragraph (b) of this section regarding the treatment, for purposes of Chapter 13, of separate trusts resulting from the discretionary severance of a single trust.
- (ii) *Certain pecuniary amounts.* For purposes of this section, if a person holds the current right to receive a mandatory (i.e., nondiscretionary and noncontingent) payment of a pecuniary amount at the death of the transferor from an inter vivos trust that is includible in the transferor's gross estate, or a testamentary trust, the pecuniary amount is a separate and independent share if—
  - (A) The trustee is required to pay appropriate interest (as defined in § 26.2642-2(b)(4)(i) and (ii)) to the person; and
  - (B) If the pecuniary amount is payable in kind on the basis of value other than the date of distribution value of the assets, the trustee is required to allocate assets to the pecuniary payment in a manner that fairly reflects net appreciation or depreciation in the value of the assets in the fund available to pay the pecuniary amount measured from the valuation date to the date of payment.
- (iii) *Mandatory severances.* For purposes of this section, if the governing instrument of a trust requires the division or severance of a single trust into separate trusts upon the future occurrence of a particular event not within the discretion of the trustee or any other person, and if the trusts resulting from such a division or severance are recognized as separate trusts under applicable state law, then each resulting trust is treated as a separate trust for purposes of Chapter 13. For this purpose, the

rules of [paragraph \(b\)\(1\)\(ii\)\(C\)](#) of this section apply with respect to the severance and funding of the trusts. Similarly, if the governing instrument requires the division of a single trust into separate shares under the circumstances described in this paragraph, each such share is treated as a separate trust for purposes of Chapter 13. The post-severance treatment of the resulting shares or trusts as separate trusts for GST tax purposes generally permits the allocation of GST tax exemption, the making of various elections permitted for GST tax purposes, and the occurrence of a taxable distribution or termination with regard to a particular resulting share or trust, with no GST tax impact on any other trust or share resulting from that severance. The treatment of a single trust as separate trusts under this [paragraph \(a\)\(1\)](#), however, does not permit treatment of those portions as separate trusts for purposes of filing returns and payment of tax or for purposes of computing any other tax imposed under the Internal Revenue Code, if those portions are not treated as separate trusts under local law. Also, additions to, and distributions from, such trusts are allocated pro rata among the separate trusts, unless the governing instrument expressly provides otherwise. Each separate share and each trust resulting from a mandatory division or severance described in this paragraph will have the same inclusion ratio immediately after the severance as that of the original trust immediately before the division or severance.

(2) *Multiple transferors with respect to single trust –*

- (i) *In general.* If there is more than one transferor with respect to a trust, the portions of the trust attributable to the different transferors are treated as separate trusts for purposes of chapter 13. Treatment of a single trust as separate trusts under this [paragraph \(a\)\(2\)](#) does not permit treatment of those portions as separate trusts for purposes of filing returns and payment of tax or for purposes of computing any other tax imposed under the Internal Revenue Code. Also, additions to, and distributions from, such trusts are allocated pro rata among the separate trusts unless otherwise expressly provided in the governing instrument.
- (ii) *Addition by a transferor.* If an individual makes an addition to a trust of which the individual is not the sole transferor, the portion of the single trust attributable to each separate trust is determined by multiplying the fair market value of the single trust immediately after the contribution by a fraction. The numerator of the fraction is the value of the separate trust immediately after the contribution. The denominator of the fraction is the fair market value of all the property in the single trust immediately after the transfer.

(3) *Severance of a single trust.* A single trust treated as separate trusts under [paragraphs \(a\)\(1\) or \(2\)](#) of this section may be divided at any time into separate trusts to reflect that treatment. For this purpose, the rules of [paragraph \(b\)\(1\)\(ii\)\(C\)](#) of this section apply with respect to the severance and funding of the severed trusts.

(4) *Allocation of exemption –*

- (i) *In general.* With respect to a separate share treated as a separate trust under [paragraph \(a\)\(1\) or \(2\)](#) of this section, an individual's GST exemption is

allocated to the separate trust. See § 26.2632-1 for rules concerning the allocation of GST exemption.

- (ii) *Automatic allocation to direct skips.* If the transfer is a direct skip to a trust that occurs during the transferor's lifetime and is treated as a transfer to separate trusts under paragraphs (a)(1) or (a)(2) of this section, the transferor's GST exemption not previously allocated is automatically allocated on a pro rata basis among the separate trusts. The transferor may prevent an automatic allocation of GST exemption to a separate share of a single trust by describing on a timely-filed United States Gift (and Generation-Skipping Transfer) Tax Return (Form 709) the transfer and the extent to which the automatic allocation is not to apply to a particular share. See § 26.2632-1(b) for rules for avoiding the automatic allocation of GST exemption.

- (5) *Examples.* The following examples illustrate the principles of this section (a):

*Example 1. Separate shares as separate trusts.* T transfers \$100,000 to a trust under which income is to be paid in equal shares for 10 years to T's child, C, and T's grandchild, GC (or their respective estates). The trust does not permit distributions of principal during the term of the trust. At the end of the 10-year term, the trust principal is to be distributed to C and GC in equal shares. The shares of C and GC in the trust are separate and independent and, therefore, are treated as separate trusts. The result would not be the same if the trust permitted distributions of principal unless the distributions could only be made from a one-half separate share of the initial trust principal and the distributee's future rights with respect to the trust are correspondingly reduced. T may allocate part of T's GST exemption under section 2632(a) to the share held for the benefit of GC.

*Example 2. Separate share rule inapplicable.* The facts are the same as in *Example 1*, except the trustee holds the discretionary power to distribute the income in any proportion between C and GC during the last year of the trust. The shares of C and GC in the trust are not separate and independent shares throughout the entire term of the trust and, therefore, are not treated as separate trusts for purposes of chapter 13.

*Example 3. Pecuniary payment as separate share.* T creates a lifetime revocable trust providing that on T's death \$500,000 is payable to T's spouse, S, with the balance of the principal to be held for the benefit of T's grandchildren. The value of the trust is includible in T's gross estate upon T's death. Under the terms of the trust, the payment to S is required to be made in cash, and under local law S is entitled to receive interest on the payment at an annual rate of 6 percent, commencing immediately upon T's death. For purposes of chapter 13, the trust is treated as created at T's death, and the \$500,000 payable to S from the trust is treated as a separate share. The result would be the same if the payment to S could be satisfied using noncash assets at their value on the date of distribution. Further, the result would be the same if the decedent's probate estate poured over to the revocable trust on the decedent's death and was then distributed in accordance with the terms of the trust.

*Example 4. Pecuniary payment not treated as separate share.* The facts are the same as in *Example 3*, except the bequest to S is to be paid in noncash assets valued at their values as

finally determined for Federal estate tax purposes. Neither the trust instrument nor local law requires that the assets distributed in satisfaction of the bequest fairly reflect net appreciation or depreciation in all the assets from which the bequest may be funded. S's \$500,000 bequest is not treated as a separate share and the trust is treated as a single trust for purposes of chapter 13.

*Example 5. Multiple transferors to single trust.* A transfers \$100,000 to an irrevocable generation-skipping trust; B simultaneously transfers \$50,000 to the same trust. As of the time of the transfers, the single trust is treated as two trusts for purposes of chapter 13. Because A contributed  $\frac{2}{3}$  of the value of the initial corpus,  $\frac{2}{3}$  of the single trust principal is treated as a separate trust created by A. Similarly, because B contributed  $\frac{1}{3}$  of the value of the initial corpus,  $\frac{1}{3}$  of the single trust is treated as a separate trust created by B. A or B may allocate their GST exemption under section 2632(a) to the respective separate trusts.

*Example 6. Additional contributions.* A transfers \$100,000 to an irrevocable generation-skipping trust; B simultaneously transfers \$50,000 to the same trust. When the value of the single trust has increased to \$180,000, A contributes an additional \$60,000 to the trust. At the time of the additional contribution, the portion of the single trust attributable to each grantor's separate trust must be redetermined. The portion of the single trust attributable to A's separate trust immediately after the contribution is  $\frac{3}{4}$  ( $((\frac{2}{3} \times \$180,000) + \$60,000) / \$240,000$ ). The portion attributable to B's separate trust after A's addition is  $\frac{1}{4}$ .

*Example 7. Distributions from a separate share.* The facts are the same as in *Example 6*, except that, after A's second contribution, \$50,000 is distributed to a beneficiary of the trust. Absent a provision in the trust instrument that charges the distribution against the contribution of either A or B,  $\frac{3}{4}$  of the distribution is treated as made from the separate trust of which A is the transferor and  $\frac{1}{4}$  from the separate trust of which B is the transferor.

*Example 8. Subsequent mandatory division into separate trusts.* T creates an irrevocable trust that provides the trustee with the discretionary power to distribute income or corpus to T's children and grandchildren. The trust provides that, when T's youngest child reaches age 21, the trust will be divided into separate shares, one share for each child of T. The income from a respective child's share will be paid to the child during the child's life, with the remainder passing on the child's death to such child's children (grandchildren of T). The separate shares that come into existence when the youngest child reaches age 21 will be recognized as of that date as separate trusts for purposes of Chapter 13. The inclusion ratio of the separate trusts will be identical to the inclusion ratio of the trust before the severance. Any allocation of GST tax exemption to the trust after T's youngest child reaches age 21 may be made to any one or more of the separate shares. The result would be the same if the trust instrument provided that the trust was to be divided into separate trusts when T's youngest child reached age 21, provided that the severance and funding of the separate trusts meets the requirements of this section.

**(b)** *Division of a trust included in the gross estate –*

- (1)** *In general.* The severance of a trust that is included in the transferor's gross estate (or created under the transferor's will) into two or more trusts is recognized for purposes of chapter 13 if—
  - (i)** The trust is severed pursuant to a direction in the governing instrument providing that the trust is to be divided upon the death of the transferor; or
  - (ii)** The governing instrument does not require or otherwise direct severance but the trust is severed pursuant to discretionary authority granted either under the governing instrument or under local law; and
    - (A)** The terms of the new trusts provide in the aggregate for the same succession of interests and beneficiaries as are provided in the original trust;
    - (B)** The severance occurs (or a reformation proceeding, if required, is commenced) prior to the date prescribed for filing the Federal estate tax return (including extensions actually granted) for the estate of the transferor; and
    - (C)** Either—
      - (1)** The new trusts are severed on a fractional basis. If severed on a fractional basis, the separate trusts need not be funded with a pro rata portion of each asset held by the undivided trust. The trusts may be funded on a nonpro rata basis provided funding is based on either the fair market value of the assets on the date of funding or in a manner that fairly reflects the net appreciation or depreciation in the value of the assets measured from the valuation date to the date of funding; or
      - (2)** If the severance is required (by the terms of the governing instrument) to be made on the basis of a pecuniary amount, the pecuniary payment is satisfied in a manner that would meet the requirements of [paragraph \(a\)\(1\)\(ii\)](#) of this section if it were paid to an individual.
- (2)** *Special rule.* If a court order severing the trust has not been issued at the time the Federal estate tax return is filed, the executor must indicate on a statement attached to the return that a proceeding has been commenced to sever the trust and describe the manner in which the trust is proposed to be severed. A copy of the petition or other instrument used to commence the proceeding must also be attached to the return. If the governing instrument of a trust or local law authorizes the severance of the trust, a severance pursuant to that authorization is treated as meeting the requirement of [paragraph \(b\)\(1\)\(ii\)\(B\)](#) of this section if the executor indicates on the Federal estate tax return that separate trusts will be created (or funded) and clearly sets forth the manner in which the trust is to be severed and the separate trusts funded.
- (3)** *Allocation of exemption.* An individual's GST exemption under § 2632 may be allocated to the separate trusts created pursuant to this section at the discretion of the executor or trustee.
- (4)** *Examples.* The following examples illustrate the provisions of this section (b):

*Example 1. Severance of single trust.* T's will establishes a testamentary trust providing that income is to be paid to T's spouse for life. At the spouse's death, one-half of the corpus is to be paid to T's child, C, or C's estate (if C fails to survive the spouse) and one-half of the corpus is to be paid to T's grandchild, GC, or GC's estate (if GC fails to survive the spouse). If the requirements of [paragraph \(b\)](#) of this section are otherwise satisfied, T's executor may divide the testamentary trust equally into two separate trusts, one trust providing an income interest to spouse for life with remainder to C, and the other trust with an income interest to spouse for life with remainder to GC. Furthermore, if the requirements of [paragraph \(b\)](#) of this section are satisfied, the executor or trustee may further divide the trust for the benefit of GC. GST exemption may be allocated to any of the divided trusts.

*Example 2. Severance of revocable trust.* T creates an inter vivos revocable trust providing that, at T's death and after payment of all taxes and administration expenses, the remaining corpus will be divided into two trusts. One trust, for the benefit of T's spouse, is to be funded with the smallest amount that, if qualifying for the marital deduction, will reduce the estate tax to zero. The other trust, for the benefit of T's descendants, is to be funded with the balance of the revocable trust corpus. The trust corpus is includible in T's gross estate. Each trust is recognized as a separate trust for purposes of chapter 13.

*Example 3. Formula severance.* T's will establishes a testamentary marital trust (Trust) that meets the requirements of qualified terminable interest property (QTIP) if an election under section 2056(b)(7) is made. Trust provides that all trust income is to be paid to T's spouse for life. On the spouse's death, the trust corpus is to be held in further trust for the benefit of T's then-living descendants. On T's date of death in January of 2004, T's unused GST tax exemption is \$1,200,000, and T's will includes \$200,000 of bequests to T's grandchildren. Prior to the due date for filing the Form 706, "United States Estate (and Generation-Skipping Transfer) Tax Return," for T's estate, T's executor, pursuant to applicable state law, divides Trust into two separate trusts, Trust 1 and Trust 2. Trust 1 is to be funded with that fraction of the Trust assets, the numerator of which is \$1,000,000, and the denominator of which is the value of the Trust assets as finally determined for federal estate tax purposes. Trust 2 is to be funded with that fraction of the Trust assets, the numerator of which is the excess of the Trust assets over \$1,000,000, and the denominator of which is the value of the Trust assets as finally determined for federal estate tax purposes. On the Form 706 filed for the estate, T's executor makes a QTIP election under section 2056(b)(7) with respect to Trust 1 and Trust 2 and a "reverse" QTIP election under section 2652(a)(3) with respect to Trust 1. Further, T's executor allocates \$200,000 of T's available GST tax exemption to the bequests to T's grandchildren, and the balance of T's exemption (\$1,000,000) to Trust 1. If the requirements of [paragraph \(b\)](#) of this section are otherwise satisfied, Trust 1 and Trust 2 are recognized as separate trusts for GST tax purposes. Accordingly, the "reverse" QTIP election and allocation of GST tax exemption with respect to Trust 1 are recognized and effective for generation-skipping transfer tax purposes.

- (c) *Cross reference.* For rules applicable to the qualified severance of trusts (whether or not includible in the transferor's gross estate), see [§ 26.2642-6](#).

- (d) *Effective date.* Paragraph (a)(1)(i), paragraph (a)(1)(iii), and *Example 8* of paragraph (a)(5) apply to severances occurring on or after September 2, 2008.

[T.D. 8644, [60 FR 66903](#), Dec. 27, 1995; [61 FR 29654](#), June 12, 1996, as amended at [61 FR 43656](#), Aug. 26, 1996; T.D. 9348, [72 FR 42297](#), Aug. 2, 2007; T.D. 9421, [73 FR 44652](#), July 31, 2008]