2 T.C. 203 (1943)

When a trustor retains a reversionary interest in a trust, the value of that interest, as of the date of death, is includable in the trustor's gross estate for estate tax purposes, less the value of any intervening life estates.

Summary

The Tax Court addressed whether the corpus of a trust created by the decedent, Peter Middlekauff, should be included in his gross estate for tax purposes. Middlekauff established an irrevocable trust, with income payable to his wife for life, then to himself if he survived her, with the remainder to be disposed of per the survivor's will. The court held that because Middlekauff retained a reversionary interest (the income if his wife predeceased him and the power of disposition via his will), the value of the trust's corpus, less the value of his wife's life estate, was includable in his gross estate. The court also allowed a deduction for the widow's allowance paid during probate.

Facts

Peter D. Middlekauff created an irrevocable trust on January 3, 1928, naming Wells Fargo Bank & Union Trust Co. as trustee. The trust provided that the income was to be paid to his wife, Emma, for life, and then to Peter if he survived her. Upon the death of the survivor, the trust property was to be distributed according to the survivor's will, or if no will existed, to their children. Middlekauff died on May 10, 1939, survived by his wife. At the time of his death, the trust corpus was valued at $478,866.27. Middlekauff's estate tax return did not include the value of this trust, which the Commissioner contested.

Procedural History

The Commissioner determined a deficiency in Middlekauff's estate tax, including the value of the 1928 trust in the gross estate. The executor, Wells Fargo Bank, petitioned the Tax Court for redetermination. The cases were consolidated, and the Tax Court reviewed the Commissioner's determination, focusing on whether the trust assets should be included in the gross estate and whether certain deductions were proper.

Issue(s)

1. Whether the value of the trust created by the decedent on January 3, 1928, is includable in his gross estate under Section 811(c) of the Internal Revenue Code as a transfer intended to take effect in possession or enjoyment at or after death.

2. Whether the estate is entitled to a deduction for the $750 per month paid for the support of the widow pursuant to a decree of the Probate Court.

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Holding

1. Yes, because the decedent retained a reversionary interest in the trust, making it includable in his gross estate under Section 811(c), although the value of the wife's life estate must be deducted from the total value of the trust assets.

2. Yes, because the amount received by the widow was actually expended for her support, regardless of whether she had other income.

Court's Reasoning

The court relied on *Helvering v. Hallock*, 309 U.S. 106 (1940), which held that when a trustor retains a reversionary interest, the value of that interest is includable in the gross estate. The court reasoned that Middlekauff retained the right to receive income from the trust if his wife predeceased him, and the power to dispose of the trust property via his will. The court stated, "By his death the retained interest in the trust property was cut off. It was not until his death that the transfer of the reversionary interest took effect". The court distinguished the inclusion of the entire trust corpus from the value of the reversionary interest. Since the wife had a life estate, its value had to be deducted from the total trust assets. Regarding the widow's allowance, the court cited *Mary M. Buck et al., Executors*, 25 B.T.A. 780, noting that the fact that the widow had income of her own was irrelevant, as the amounts were actually expended for her support.

Practical Implications

This case reinforces the principle that retained interests in trusts, particularly reversionary interests and powers of appointment, can cause the trust assets to be included in the grantor's gross estate. It highlights the importance of carefully drafting trust instruments to avoid such retained interests if the goal is to remove assets from the estate. Attorneys must analyze not only the explicit terms of the trust but also the practical effect of those terms. It also confirms that court-ordered spousal support payments are generally deductible from the gross estate if actually paid and used for support, irrespective of the spouse's independent income. Later cases applying *Middlekauff* consider the degree to which a transferor has relinquished control over assets when determining estate tax liability.

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