4 T.C. 34 (1944)

When an insured, while insolvent, changes the beneficiary of life insurance policies to his wife, such transfer is fraudulent and the wife is liable as a transferee for the insured's unpaid income tax to the extent of the policy proceeds.

Summary

The Tax Court held that a widow was liable as a transferee for her deceased husband's unpaid income taxes. The husband, while insolvent, changed the beneficiary of several life insurance policies to his wife. The court determined that under Pennsylvania law, this transfer was fraudulent as to creditors, including the government. Therefore, the widow, as the beneficiary of the life insurance proceeds, was liable in equity as a transferee for her husband's unpaid income tax liabilities.

Facts

Martin Pearlman was insolvent and owed substantial debts. During his insolvency, he changed the beneficiary of several life insurance policies to his wife, Florence Pearlman. Pearlman died in 1941, still insolvent and without an estate. At the time of his death, deficiencies in his income tax for several years were pending. The insurance companies issued claim settlement certificates to Florence Pearlman, who began receiving monthly payments.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in Pearlman's income taxes for 1934-1937 and 1940. Pearlman initially petitioned the Tax Court for redetermination, but the petition was dismissed. After Pearlman's death, the Commissioner sought to hold his widow, Florence Pearlman, liable as a transferee of assets. The Tax Court ruled in favor of the Commissioner.

Issue(s)

1. Whether Florence Pearlman, as the beneficiary of proceeds from life insurance policies on her deceased husband's life, is liable in equity as a transferee for his unpaid income tax.
2. Whether the Commissioner properly disallowed the deduction of amounts claimed by the debtor as interest accrued upon indebtedness.

Holding

1. Yes, because the change of beneficiary was a fraudulent transfer under Pennsylvania law, making Florence Pearlman liable as a transferee.
2. Yes, because Pearlman's business was essentially defunct and the accrued interest deduction was an attempt to exalt form over substance.

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Court’s Reasoning

The court applied Pennsylvania state law to determine whether the change in beneficiary was a fraudulent conveyance. Citing *Fidelity Trust Co. v. Union National Bank of Pittsburgh, 313 Pa. 467*, the court recognized that Pennsylvania law deems such transfers fraudulent when made by an insolvent individual to the detriment of creditors. The court emphasized that Pearlman was

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