4 T.C. 179 (1944)

A transfer of property to a trust is not a taxable gift if the grantor retains significant control over the assets, lacks donative intent, and the trust was created for a specific, temporary purpose.

Summary

Marguerite Schwarzenbach, a Swiss resident, created a trust in the U.S. to protect her assets from potential German confiscation during World War II. She reserved the right to revoke the trust with the unanimous consent of the trustees, who had an understanding to allow revocation once the emergency passed. The Tax Court held that the transfer to the trust did not constitute a taxable gift because Schwarzenbach retained substantial control and lacked the intent to make a completed gift. The trust was a temporary measure, not an irrevocable transfer.

Facts

Fearing German invasion of Switzerland and potential asset confiscation, Schwarzenbach, through her U.S.-based brother and attorney, established a trust in May 1940. She transferred U.S. securities worth $536,907.65 to the trust, naming her brother, attorney, and son as trustees. The trust instrument allowed her to receive the income for life, with the remainder to her children. She retained the right to revoke or amend the trust with unanimous trustee consent. There was an understanding that the trustees would consent to revocation after the emergency.

Procedural History

Schwarzenbach filed a gift tax return, reporting a gift to her son, a remainderman. The Commissioner of Internal Revenue assessed a deficiency, claiming the transfer to the trust was a taxable gift of the remainder interest. Schwarzenbach contested the deficiency and claimed an overpayment. The Tax Court reviewed the case.

Issue(s)

Whether the transfer of securities to the trust constituted a taxable gift for gift tax purposes, considering the grantor’s retained power of revocation and the intended purpose of the trust.

Holding

No, because Schwarzenbach retained significant control over the trust assets and lacked the necessary donative intent to make a completed gift. The trust was established for a specific, temporary purpose (asset protection) with the understanding that it could be revoked once the emergency passed.

Court’s Reasoning

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The court emphasized that a taxable gift requires the donor to relinquish dominion and control over the property with the intent to make an irrevocable transfer. The court cited precedent like *Commissioner v. Prouty* and *Sanford's Estate v. Commissioner*, which hold that transfers with retained powers of revocation are incomplete gifts. Even though the revocation required unanimous trustee consent, the court found that the trustees had a prior agreement to consent to revocation, effectively placing the power solely in the grantor's discretion. The court also highlighted the lack of donative intent, quoting *Adolph Weil*: the donor must have a "clear and unmistakable intention to absolutely and irrevocably divest herself of the title, dominion and control of the subject matter of the gift, in praesenti." The court considered the trust's purpose, communications between the parties, and Schwarzenbach's subsequent withdrawals from the trust, all of which indicated a lack of intent to make a completed gift. The court saw the entire transaction as a "sham, a fetch, a disguise" to protect assets from potential German confiscation.

Practical Implications

This case illustrates that the form of a transaction does not always control its tax consequences; the substance and intent behind the transaction are critical. Attorneys must carefully analyze the grantor's retained powers and the surrounding circumstances to determine if a completed gift has occurred. Creating trusts with the explicit understanding that they are temporary measures to circumvent potential legal or political issues may prevent these transfers from being considered completed gifts. Later cases have distinguished *Schwarzenbach* by focusing on the presence or absence of a clear agreement among parties regarding the revocability of the trust and the grantor's control over trust assets.

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