Estate of Eckhardt v. Commissioner, 5 T.C. 673 (1945)

The reciprocal trust doctrine holds that trusts created by two settlors are considered made in consideration of each other when they are interrelated and leave the settlors in approximately the same economic position as if they had created trusts naming themselves as beneficiaries, and a reversionary interest that does not enlarge the estate of remaindermen upon the decedent's death is not includible in the gross estate.

Summary

The Tax Court addressed whether trusts created by a husband and wife were reciprocal and includible in their respective estates under Section 811(c) of the Internal Revenue Code. The court found that the trusts were indeed reciprocal, as they were created under a common plan where each grantor received a life estate in the trust nominally created by the other. However, the court held that a reversionary interest in a separate trust, where the decedent's death did not enlarge the estate of the remaindermen, was not includible in the gross estate.

Facts

John and Kate Eckhardt, husband and wife, executed trusts in July 1935. John created a trust with Kate and their daughter, Alice Becker, as successive life beneficiaries, and Kate created a similar trust for John and Alice. The subject matter of the trusts was jointly owned real estate. Kate also created another trust for her grandson, Dean Becker, with a possibility of reversion to Kate if Dean and his issue, and Dean's mother, Alice, predeceased her. The IRS determined that the trusts were reciprocal and included the corpus of each trust in the respective decedent's estate, and also included the value of the reversionary interest in Kate's estate.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in the estate tax returns of John and Kate Eckhardt. The Estate appealed to the Tax Court, contesting the inclusion of the trust assets and the reversionary interest in the gross estate.

Issue(s)

1. Whether the trusts executed by John and Kate Eckhardt were created independently or were reciprocal and made in consideration of each other.

2. Whether the value of a reversionary interest in the trust created by Kate L. Eckhardt for the benefit of her grandson is includible in her gross estate as a transfer intended to take effect in possession or enjoyment at or after her death.

Holding

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1. No, the trusts were reciprocal because the evidence showed a common plan and understanding between John and Kate, such that each grantor was the real settlor of the trust nominally created by the other.

2. No, the value of the reversionary interest is not includible in Kate's gross estate because her death did not enlarge the estate or affect the interests of the trust's beneficiaries.

Court's Reasoning

Regarding the reciprocal trusts, the court noted the intimate financial and business relationship between John and Kate throughout their marriage, the similarity of the trust provisions, and the near-simultaneous execution of the trusts. The court found it implausible that each settlor would independently conceive a plan to create a trust with such similar provisions. The court stated, "From the evidence, we are satisfied that these trusts were executed under such circumstances as would justify the respondent in determining that they were reciprocal and executed in consideration of one another." Therefore, the court concluded that each decedent retained a life estate in the trust created by him, and the value of the corpus of such trust is includible in his gross estate under Section 811(c) of the Internal Revenue Code.

Regarding the reversionary interest, the court relied on *Frances Biddle Trust, 3 T.C. 832*, holding that the decedent's death did not enlarge or augment the estate of the remaindermen. The court distinguished *Fidelity-Philadelphia Trust Co. v. Rothensies, 324 U.S. 108*, because, in this case, no interest in the trust estate passed or was created by virtue of the death of Kate L. Eckhardt. The court reasoned, "The remote possibility of her reacquiring the corpus, in the event she survived the named beneficiaries, does not require the conclusion that she intended the trust to take effect at her death. On the contrary, we think she intended that the interests created by the trust were to vest immediately."

Practical Implications

This case illustrates the application of the reciprocal trust doctrine. Attorneys must carefully analyze the facts and circumstances surrounding the creation of trusts by related parties to determine if a common plan exists. If trusts are deemed reciprocal, the assets may be included in the grantors' estates, leading to significant estate tax consequences. Estate planners should advise clients to avoid creating trusts that are too similar or are executed within a short time of each other. The case also highlights the importance of demonstrating the independent purpose and intent behind each trust. Finally, the case reiterates that a mere possibility of reverter does not automatically cause inclusion in the gross estate if the decedent's death does not change the beneficiaries' interests.

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