6 T.C. 874 (1946)

When a will contest is settled via a compromise agreement, and that agreement results in a trust arrangement, the property transferred into the trust is considered to have passed directly from the original testator to the beneficiaries, not from the decedent who facilitated the trust's creation; therefore, the value of the trust is not included in the decedent's gross estate for estate tax purposes.

Summary

Mary Clare Milner's estate disputed a deficiency in estate tax assessed by the Commissioner. The dispute centered on property Milner had transferred into a trust in 1929 following a will contest involving her mother's estate. The Tax Court held that because Milner only received a life estate in the property as part of the settlement, the property's value should not be included in her gross estate. The court reasoned that the beneficiaries' interests arose directly from the original testator (Milner's mother) through the compromise agreement, not from Milner's actions as a transferor.

Facts

Gustrine Key Milner died in 1929, leaving behind a will from 1927 that divided her residuary estate equally between her daughter, Mary Clare Milner, and her son, Henry Key Milner. However, Gustrine's granddaughter, Gustrine Milner Jackson, contested the 1927 will, claiming an earlier 1921 will was valid and that she was a beneficiary under that will. To settle the dispute, Mary Clare Milner executed a trust in 1929, placing her share of the property into the trust with herself as the income beneficiary for life, and her daughters as beneficiaries after her death. The 1927 will was then admitted to probate. The Commissioner sought to include the value of the trust property in Mary Clare Milner's gross estate upon her death.

Procedural History

The Commissioner determined a deficiency in Mary Clare Milner's estate tax. Milner's estate petitioned the Tax Court, arguing the trust property shouldn't be included in the gross estate. The Tax Court sided with the estate, finding that Mary Clare Milner never owned the property outright but merely received a life estate as a result of the will contest settlement.

Issue(s)

Whether the property transferred into a trust, as part of a settlement agreement resolving a will contest, should be included in the decedent's gross estate under Section 811(c) of the Internal Revenue Code, when the decedent only received a life estate in the property as part of the settlement.

Holding

No, because the decedent, Mary Clare Milner, only acquired a life estate in the property as a result of the will contest settlement and did not own an interest in the property that passed at or by reason of her death.

Court’s Reasoning

The Tax Court relied heavily on the Supreme Court’s decision in *Lyeth v. Hoey*, which held that property received in settlement of a will contest is considered acquired by inheritance, regardless of the compromise. The court extended this principle to estate tax law, citing cases like *Helvering v. Safe Deposit & Trust Co.* and *Dumont’s Estate v. Commissioner*. The court emphasized that Gustrine Milner Jackson, as a beneficiary under the prior will, had a legitimate claim to a portion of Gustrine Key Milner’s estate. The court found the probate court decree admitting the later will to probate was a consent decree and not a conclusive determination of ownership. Because the trust was created as a direct result of settling this claim, the beneficiaries’ interests in the trust property stemmed directly from Gustrine Key Milner’s estate, not from a transfer by Mary Clare Milner. Therefore, Mary Clare Milner did not transfer any interest in the property within the meaning of Section 811(c) of the Internal Revenue Code. As the Circuit Court stated in *Sage v. Commissioner*, regarding the precedent set in *Lyeth v. Hoey*, “the heir in the Lyeth case did not take under the testator’s will… Like the widow here, he took in spite of the will and not because of it.”

Practical Implications

This case provides crucial guidance for estate planning and tax law. It clarifies that when settling will contests, the substance of the agreement determines tax consequences, not merely its form. It reinforces the principle that settlements should be viewed as if the contestant had prevailed, with assets passing directly from the testator to the ultimate beneficiaries. Attorneys should carefully document the intent and terms of settlement agreements to ensure accurate tax treatment. Later cases have cited *Milner* when analyzing the tax implications of will contest settlements, emphasizing the importance of determining the source of the beneficiaries’ rights. This decision impacts how estate planners structure settlements and advise clients on potential tax liabilities, particularly when trusts are involved.

