7 T.C. 921 (1946)

When a settlor retains the power, even if exercisable only with the consent of others, to terminate a trust and thereby affect remainder interests, the value of those remainder interests is includible in the settlor's gross estate for federal estate tax purposes.

Summary

The Tax Court addressed whether the value of remainder interests in a trust should be included in the decedent's gross estate for estate tax purposes. The trust, created in 1918, allowed for termination upon the request of life beneficiaries and the consent of the settlor. The court held that because the decedent retained the power to terminate the trust, the remainder interests were includible in his gross estate under Section 811(d)(2) of the Internal Revenue Code. The court further held that this inclusion did not violate the due process clause of the Fifth Amendment.

Facts

Charles M. Thorp created a trust in 1918, naming his wife as the initial trustee and life beneficiary. Upon his wife's death, the income was to be paid to their six children for life, with the remainder to their grandchildren. The trust could be terminated if all life beneficiaries requested termination in writing and the settlor consented in writing. The settlor's wife and one child predeceased him. At the time of Thorp's death in 1942, the fair market value of the trust corpus was $285,527, with the remainder interests valued at $129,865.67.

Procedural History

The Commissioner of Internal Revenue included the value of the trust remainders in Thorp's gross estate. The executors of Thorp's estate, the petitioners, contested this inclusion, arguing that the decedent did not possess a power of termination within the meaning of Section 811(d)(2) and that retroactive application of the section would violate the due process clause. The Tax Court heard the case to determine the validity of the Commissioner's assessment.

Issue(s)

1. Whether the decedent reserved to himself a power of termination within the meaning of Section 811(d)(2) of the Internal Revenue Code.
2. If the decedent did possess a power of termination, whether the retroactive application of Section 811(d)(2) would violate the due process clause of the Fifth Amendment.

Holding

1. Yes, because the trust instrument reserved to the settlor the right to control

the vital act necessary to terminate it, even though the request to terminate had to be initiated by the life beneficiaries.

2. No, because the power to terminate affected only the remainder interests, and the transfer of those interests was not complete until the settlor's death extinguished the power.

Court's Reasoning

The court reasoned that although the life beneficiaries initiated the request to terminate, the settlor's consent was required for termination. Therefore, the settlor retained a power to affect the remainder interests. Quoting *Commissioner v. Estate of Holmes*, 326 U.S. 480, the court emphasized that the termination power meant the transfer was incomplete until the settlor's death. The court distinguished *Helvering v. Helmholz*, 296 U.S. 93, noting that in *Helmholz*, termination required the consent of all beneficiaries, including remaindermen, which was not the case here. Furthermore, the court noted that Pennsylvania law required the consent of all beneficiaries, including those with indeterminate interests, for trust termination, implying that the settlor's power was particularly significant. The court rejected the argument that including the remainder in the gross estate violated due process, as the transfer remained incomplete due to the retained power.

Practical Implications

This case clarifies that even a power to terminate a trust exercisable in conjunction with others can cause the trust assets to be included in the grantor's estate. It highlights the importance of carefully analyzing the specific language of trust agreements to determine the extent of control retained by the grantor. Attorneys drafting trusts must advise clients that retaining any power to alter beneficial enjoyment, even if seemingly limited, can have significant estate tax consequences. This decision reinforces the principle that estate tax inclusion turns on the degree of control a grantor maintains over transferred assets, rather than the precise form of the retained power. Subsequent cases applying Section 2038 of the Internal Revenue Code (the modern equivalent of Section 811(d)(2)) often cite *Thorp* for the proposition that a retained power, even if conditional, can trigger estate tax inclusion.

