7 T.C. 1303 (1946)

The grantor of a trust retains the power to alter, amend, or revoke the trust for estate tax purposes under Section 811(d)(2) of the Internal Revenue Code if the grantor's prior modification of the trust did not fully exhaust their reserved power and did not vest indefeasible rights in beneficiaries.

Summary

The case concerns whether the value of a trust's corpus should be included in the decedent's gross estate for tax purposes. The decedent created a trust in 1922, reserving the right to change the beneficiaries. In 1936, she modified the trust to alter the beneficiaries in a specific contingency. The Tax Court held that the 1936 modification did not exhaust her power to alter the trust, as it did not vest absolute rights in any beneficiary and left her with the power to change beneficiaries at the trust's termination. Thus, the trust was includible in her estate under Section 811(d)(2) of the Internal Revenue Code.

Facts

- Addie Ludlow Bingham executed a trust in 1922, naming her daughter and granddaughter as beneficiaries.
- The trust included a provision (Paragraph 3(b)) specifying who would receive the corpus if her daughter and her descendants died before the trust's termination.
- Paragraph 11 of the trust expressly reserved to Addie Bingham the right to change the beneficiaries who would receive the trust corpus upon termination.
- In 1936, Bingham modified Paragraph 3(b) to change the beneficiaries in the event that her daughter and her descendants died before the trust terminated, substituting her own heirs. This change was motivated by her daughter's pending divorce.
- Addie Bingham died in 1942, survived by her daughter and three granddaughters (one of whom later had a son).

Procedural History

- The Commissioner of Internal Revenue determined a deficiency in the estate tax, arguing the trust corpus should be included in the gross estate.
- The estate challenged the deficiency in Tax Court.

Issue(s)

1. Whether the decedent, by modifying the trust in 1936, exhausted her reserved power to change beneficiaries, or whether she retained this power until her death.
2. Whether, if the power was retained, Section 811(d)(2) of the Internal Revenue Code is constitutional as applied to a trust created before its enactment.

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Holding

1. No, because the modification did not vest indefeasible rights in any beneficiary and did not eliminate her power to change beneficiaries at the trust's termination.
2. No, because the constitutionality of applying the statute to trusts created before its enactment has already been upheld.

Court's Reasoning

- The court determined that Colorado law, incorporating common law principles, governed the interpretation of the trust.
- The court distinguished the present case from prior cases such as *Day v. Commissioner*, where the exercise of a power had vested property rights, making subsequent changes impermissible.
- The court reasoned that the 1936 modification was contingent and did not prevent Bingham from later changing the beneficiaries entitled to the corpus at the trust's termination.
- The court cited authorities like Sugden on Powers and Farwell on Powers to support the view that the partial execution of a power does not necessarily exhaust it, especially when the initial exercise does not deprive anyone of vested rights. The court quoted Farwell on Powers: "* * * The principle of this decision — namely, that an instrument executing a power must expressly reserve any powers which may be intended to be retained…"
- The court also noted that the 1936 modification expressly ratified and confirmed the declaration of trust in all other respects, implying that the power to change beneficiaries under Paragraph 11 remained intact.
- Regarding the constitutionality of Section 811(d)(2), the court cited precedent establishing that its application to trusts created before its enactment is constitutional.

Practical Implications

- This case clarifies that merely modifying a trust does not automatically exhaust a grantor's power to alter, amend, or revoke it for estate tax purposes.
- Practitioners must carefully analyze the scope of any modifications to determine if they vest indefeasible rights in beneficiaries or otherwise eliminate the grantor's retained power.
- The case emphasizes that a grantor's intent, as expressed in the trust instrument, is paramount in determining whether a power has been exhausted. The court considered that

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