8 T.C. 492 (1947)

A transfer of assets to a trust is considered in contemplation of death, and thus includible in the gross estate, to the extent the assets are used to maintain life insurance policies intended to provide for beneficiaries after the grantor's death, but not to the extent the assets are used for the immediate welfare of beneficiaries during the grantor's life.

Summary

The Tax Court addressed whether assets transferred to trusts by Paul Garrett should be included in his gross estate as transfers in contemplation of death. Garrett created two trusts in 1923: Trust No. 1, which included life insurance policies and income-producing securities, and Trust No. 2, solely composed of income-producing securities. A third trust was formed in 1929 using stock from a holding corporation. The court held that Trust No. 2 and a portion of Trust No. 1 intended for the immediate welfare of Garrett's wife were not made in contemplation of death. However, the portion of Trust No. 1 used to maintain life insurance policies and the 1929 trust were deemed to be testamentary in nature and therefore includible in the gross estate.

Facts

Paul Garrett died in 1940 at age 76. In 1923, Garrett established two trusts. Trust Fund No. 1 contained bonds and 30 life insurance policies. The trust income was to be paid to his wife for life, then to his children. Trust Fund No. 2 contained bonds, with income paid directly to his children. In 1929, Garrett formed the Garrett Holding Corporation and transferred real and personal property to it. Stock was issued to trustees for his children and to Garrett and his wife directly. A trust agreement directed income from the stock to be distributed to the beneficiaries, similar to his will. Garrett retained significant control over the Holding Corporation.

Procedural History

The Commissioner of Internal Revenue determined an estate tax deficiency, including the value of assets in the trusts in Garrett's gross estate. The executors of Garrett's estate petitioned the Tax Court for a redetermination. The Commissioner conceded that Trust Fund No. 2 was not includible. The Tax Court then ruled on the includability of Trust Fund No. 1 and the 1929 trust.

Issue(s)

1. Whether the assets transferred to Trust Fund No. 1 in 1923, including life insurance policies and income-producing securities, were transferred in contemplation of death under Section 811 of the Internal Revenue Code.

2. Whether the assets transferred to the 1929 trust, consisting of stock from the

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Garrett Holding Corporation, were transferred in contemplation of death under Section 811 of the Internal Revenue Code.

Holding

1. No, in part. The transfer to Trust Fund No. 1 was in contemplation of death only to the extent of the insurance policies and the proportion of capital necessary to sustain them, because the dominant motive was to preserve an estate that would come to fruition upon death. It was not in contemplation of death with respect to the proportion where Garrett's wife was the life beneficiary, because that was for her immediate welfare.

2. Yes, because the transfers were part of a comprehensive plan for testamentary disposition, with Garrett retaining effective control until his death.

Court's Reasoning

The court reasoned that the dominant motive behind the transfers dictates whether they were made in contemplation of death. Regarding Trust Fund No. 1, the court found that the portion used to maintain life insurance policies was testamentary in nature. The court emphasized that the trust instrument absolved the trustee from any obligation other than safekeeping the policies and paying premiums. The court stated, "the emphasis placed upon the use of that part of the income, not for the current needs during his life of the respective beneficiaries, but for the preservation of the insurance estate" indicated a testamentary motive. Citing *United States v. Wells*, the court emphasized that a dominant motive for the transfer must be proven. As to the 1929 transfers, the court found that Garrett's retention of control through the Holding Corporation and the similarities between the trust and his will indicated a testamentary motive. The court stated that the "essential unity of decedent's will, his life insurance, and the *inter vivos* transfers of his own property" confirmed this motive. The dissent argued that the insurance policies should be treated like any other asset transferred to the trust and that the majority opinion incorrectly assumes a testamentary motive whenever life insurance is involved.

Practical Implications

This case clarifies that transfers to trusts are not automatically considered in contemplation of death simply because they involve life insurance policies. The key is the grantor's dominant motive. If the primary purpose is to provide for beneficiaries after death by maintaining life insurance, the transfer will likely be deemed testamentary. However, if the transfer aims to provide for the immediate welfare of beneficiaries during the grantor's life, it is less likely to be considered in contemplation of death. This case emphasizes the importance of documenting the grantor's intent and purpose when establishing trusts involving life insurance to avoid estate tax complications.

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