12 T.C. 1164 (1949)

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A grantor’s power as trustee to withhold income from a beneficiary, which may be paid subsequently or added to the corpus, constitutes the right to designate the person who shall enjoy the income under Section 811(c) of the Internal Revenue Code, thus requiring inclusion in the gross estate for estate tax purposes.

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Summary

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The Tax Court addressed whether the value of assets transferred into trusts by the decedent, Cyrus Yawkey, should be included in his gross estate for estate tax purposes. The trusts, established for his granddaughters, gave the trustees discretion to distribute or accumulate income and, after the granddaughters reached 30, to distribute principal. The court held that the power to distribute or accumulate income constituted a right to designate who enjoys the income, triggering inclusion under Section 811(c). However, the power to distribute principal after age 30, which none of the granddaughters had reached, did not trigger inclusion under Section 811(d). The court also determined that the inclusion of accumulated income in the trust corpus at the time of death was proper.

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Facts

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Cyrus Yawkey (decedent) and his wife created three trusts, one for each of their granddaughters, naming themselves and their son-in-law as trustees. The trust terms allowed the trustees to distribute income to the beneficiaries at their discretion until age 25, after which income was to be distributed quarterly. The trustees could also distribute principal to the beneficiaries after they turned 30. Yawkey contributed 53.2% of the assets to each trust. At the time of Yawkey’s death, the granddaughters were under 30, and the trusts held accumulated, undistributed income.

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Procedural History

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The Commissioner of Internal Revenue determined a deficiency in Yawkey's estate tax, including in the gross estate the value of the trust property and accrued income. The executor of Yawkey's estate, First Wisconsin Trust Company, petitioned the Tax Court, contesting the Commissioner's determination.

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Issue(s)

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1. Whether the trustee's discretion to distribute or accumulate income, guided by the "best interest" of the beneficiary, provided an adequate external standard, thus precluding inclusion under sections 811(c) and 811(d) of the Internal Revenue Code.

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2. Whether the power to distribute principal after a beneficiary reaches 30 years of age constitutes a power to alter, amend, or revoke the trust under section 811(d) when no beneficiary had reached that age at the time of the decedent's death.

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3. Whether the power to withhold income from a beneficiary and add it to the trust corpus constitutes a right to designate who shall enjoy the income under section 811(c).

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Holding

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1. No, because the “best interest” standard does not sufficiently limit the trustee’s discretion, making sections 811(c) and 811(d) applicable.

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2. No, because the power to distribute principal was contingent on the beneficiaries reaching age 30, and this contingency had not been met at the time of the decedent’s death, so it does not fall under Section 811(d).

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3. Yes, because the power to withhold income and add it to the corpus effectively shifts the enjoyment of that income from the life beneficiary to the remaindermen, thus designating who shall enjoy the income under Section 811(c).

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Court’s Reasoning

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The court reasoned that the “best interest” standard for distributing income was too broad to provide an adequate external limitation on the trustees’ discretion. The court stated, “We can not regard the language involved as limiting the usual scope of a trustee’s discretion. It must always be anticipated that trustees will act for the best interests of a trust beneficiary, and an exhortation to act ‘in the interests and for the welfare’ of the beneficiary does not establish an external standard.” Because this discretion existed, the grantor retained the power to designate who would enjoy the income.

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Regarding the power to distribute principal, the court relied on precedent, stating, “Under authorities now too firmly established to question, a power based on such a future contingency does not suffice to bring the situation within section 811 (d).” The court distinguished this case from *Commissioner v. Estate of Church, 335 U.S. 632* and *Estate of Spiegel v. Commissioner, 335 U.S. 701*, noting those cases dealt with Section 811(c) while this issue fell under Section 811(d)(2), which requires the power to exist “at the date of his death.”

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