13 T.C. 742 (1949)

When a decedent provides the assets for a trust nominally created by another, and retains a lifetime interest and power of appointment, the decedent is considered the true settlor, and the trust corpus is includible in their gross estate for estate tax purposes.

Summary

Grace D. Sinclaire transferred assets to her father, who then created a trust with those assets, naming Grace as the lifetime income beneficiary with a testamentary power of appointment. The Tax Court held that Grace was the de facto settlor of the trust because she provided the assets, and the trust corpus was includible in her gross estate under Sections 811(c) and 811(d)(2) of the Internal Revenue Code. This case emphasizes that the substance of a transaction, rather than its form, determines who is the actual settlor of a trust for estate tax implications.

Facts

Grace D. Sinclaire received a trust fund from her grandmother's will, to be paid out at age 25. Before reaching that age, on June 30, 1926, Grace executed a deed of gift to her father, Alfred E. Dieterich, transferring her interest in the trust and other securities. On the same day, Alfred created a trust with the transferred assets, naming Grace as the income beneficiary for life and granting her a general power of appointment over the remainder. The deed of gift was attached to the trust instrument. Grace directed the trustees of her grandmother's trust to deliver the funds to her father on her 25th birthday.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in Grace Sinclaire's estate tax, including the corpus of the 1926 trust in her gross estate. The executors of Sinclaire's estate petitioned the Tax Court, arguing that the trust assets should not be included because the power of appointment was not legally exercised. The Tax Court upheld the Commissioner's determination, finding that Grace was the true settlor of the trust.

Issue(s)

Whether the corpus of the trust created by Alfred E. Dieterich on June 30, 1926, is includible in the gross estate of Grace D. Sinclaire for estate tax purposes under Sections 811(c) and 811(d)(2) of the Internal Revenue Code, given that Sinclaire provided the assets used to fund the trust.

Holding

Yes, because in substance and reality, Grace D. Sinclaire was the settlor of the trust.

Even though her father was the nominal settlor, she provided the assets and retained significant control and enjoyment of the trust property.

Court's Reasoning

The court reasoned that while the deed of gift appeared to be an unqualified transfer, the surrounding circumstances indicated a prearranged plan. The court emphasized the simultaneous execution of the deed of gift and trust instrument, the identical property transferred, and Grace's retention of lifetime income and a testamentary power of appointment. The court stated that, "Although the deed of gift from decedent to her father on June 30, 1926, and the deed of trust by her father on the same date do not recite any agreement or understanding that the gift constituted the consideration for the trust, respondent's determination that there was a concert of action, or at least a tacit agreement, between the decedent and her father is presumptively correct and the burden of proof otherwise is on the petitioners." The court found that Grace retained the essential elements of complete ownership and control, making her the de facto settlor. The court cited Section 811(c), which includes in the gross estate property transferred where the decedent retained the right to income or the power to designate who shall enjoy the property, and Section 811(d)(2), which includes property subject to a power to alter, amend, or revoke. The court relied on precedent such as *Lehman v. Commissioner*, which established the principle that reciprocal trusts should be treated as if the settlors created the trusts for themselves.

Practical Implications

This case demonstrates that tax authorities and courts will look beyond the formal structure of transactions to determine their true substance. Attorneys structuring trusts must consider the source of the assets and the extent of control retained by the individual providing those assets. Nominal settlors who merely act as conduits for the true grantor will be disregarded for estate tax purposes. This ruling informs how similar cases should be analyzed by focusing on the economic realities of the trust arrangement rather than the legal formalities. Later cases have applied this ruling to prevent taxpayers from circumventing estate tax laws by using intermediaries to create trusts while retaining beneficial interests.