Estate of Edward J. Tully, Sr. v. Commissioner, 52 T.C. 266 (1969)

The court determines whether a trust corpus should be included in a decedent's gross estate based on whether the trust was created in contemplation of death, or whether the decedent retained any rights or incidents of ownership over the trust property.

Summary

The Estate of Edward J. Tully, Sr. challenged the Commissioner's determination that certain assets should be included in the decedent's gross estate for tax purposes. The Tax Court addressed several issues, including whether an inter vivos trust was created in contemplation of death, whether the decedent retained a life estate or incidents of ownership in the trust corpus, the reasonableness of a widow's allowance, and the inclusion of jointly held property. The court found that the trust was not created in contemplation of death, the decedent did not retain a life estate or incidents of ownership, the widow's allowance was reasonable, and the jointly held property was properly included. The court's decision clarified the application of several Internal Revenue Code sections related to estate taxation, including transfers in contemplation of death, retained life estates, and jointly held property.

Facts

Edward J. Tully, Sr. created an irrevocable trust more than 15 years before his death, with the stated purpose of providing financial security for his wife. The trust corpus consisted of life insurance policies on the decedent's life. The trustee was substituted as beneficiary on these policies and held the policies. Although one policy was withdrawn from the trust and dividends were paid to the decedent, the trust instrument stated it was irrevocable. The decedent and his wife also held a residence and a bank deposit in joint tenancy. Upon the decedent's death, the Commissioner determined that the value of the trust corpus, the entire value of the jointly held property, and other items should be included in the gross estate, leading to a tax deficiency.

Procedural History

The case was brought before the United States Tax Court to challenge the Commissioner of Internal Revenue's assessment of a deficiency in the estate tax. The Tax Court reviewed the facts, the applicable law, and the arguments presented by both the estate and the Commissioner. The Tax Court ruled in favor of the estate on some issues and in favor of the Commissioner on others, leading to this appeal.

Issue(s)

1. Whether the inter vivos trust was created in contemplation of death, thus includible in the decedent's gross estate under Section 811(c)(1)(A) of the Internal Revenue Code.

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2. Whether the decedent retained the right to the income from the trust corpus for life, rendering the trust corpus includible under Section 811(c)(1)(B) of the Internal Revenue Code.
3. Whether the decedent possessed at death any incidents of ownership of the life insurance policies that would warrant inclusion of the proceeds in his gross estate under Section 811(g)(2)(B) of the Internal Revenue Code.
4. Whether the widow's allowance from the estate was reasonable.
5. Whether the entire value of jointly held property should be included in the gross estate under Section 811(e).

Holding

1. No, because the dominant purpose of the trust was to provide financial security for the wife, not to contemplate death.
2. No, because the trust instrument was irrevocable, and the decedent did not retain the right to income; the actions of the trustee in allowing the decedent to receive income were a result of the trustee disregarding its duties.
3. No, because the decedent did not possess incidents of ownership.
4. Yes, the widow's allowance was reasonable.
5. Yes, the entire value of the jointly held property was includible.

Court's Reasoning

The court considered the following factors:

- **Contemplation of Death:** The court found that the primary motive for creating the trust was to secure the wife's support, which is a life-related motive. The court quoted Judge Learned Hand from *Estate of Paul Garrett*, noting that transfers of property that can only be used after the grantor's death are considered testamentary unless there is evidence of other motives.
- **Life Estate:** The court examined the trust instrument, which specifically stated it was irrevocable. The court found that the actions of the trustee, in allowing the decedent to withdraw a policy and receive dividends, did not reflect a retention of income rights by the decedent but a failure of the trustee to perform its duties. The court cited *Mahony v. Crocker* and other cases to determine that assignments were complete and that income was the property of the trust estate.
- **Incidents of Ownership:** The court found that the decedent did not possess at death any incidents of ownership.
- **Widow's Allowance:** The court determined the allowance was reasonable based on the surviving spouse's expenditures, the size of the estate, and the lack of evidence that the administration was prolonged for an unreasonable time.
- **Jointly Held Property:** The court applied the applicable Internal Revenue Code sections to include the jointly held property in the gross estate, as the record was devoid of any evidence of separate property or earnings of the

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surviving spouse.

The court quoted from the trust instrument: “The said insurance policies, together with any additional policies which may hereafter be made payable to the Trustee, and the proceeds thereof received by the Trustee shall constitute the Trust Estate and shall be held by the Trustee in trust subject to all of the provisions of this agreement.”

The Court’s reasoning emphasized the intent of the decedent and the actions, or inactions, of the trustee.

Practical Implications

This case provides guidance on estate planning and the tax implications of inter vivos trusts, particularly in the context of life insurance. Attorneys should consider the following when advising clients:

- **Dominant Motive:** When establishing trusts, the dominant motive behind the transfer of assets is crucial. If the primary purpose is to provide for the beneficiaries’ financial security, the trust is less likely to be considered in contemplation of death.
- **Trust Instrument:** The terms of the trust instrument are paramount. If the trust is intended to be irrevocable and the grantor does not retain the right to income or incidents of ownership, the trust corpus is less likely to be included in the gross estate.
- **Trustee’s Actions:** The trustee’s actions must align with the trust instrument. If the trustee disregards its duties and allows the grantor to benefit from the trust in ways not permitted by the instrument, this could lead to the trust corpus being included in the gross estate.
- **Jointly Held Property:** The entire value of jointly held property is includible in the gross estate unless the surviving spouse can demonstrate that they contributed to the property’s acquisition.
- **Widow’s Allowance:** Reasonable widow’s allowances can reduce the taxable estate.

Subsequent cases have built on *Estate of Tully*, particularly in evaluating the grantor’s intent when setting up the trust. The case also highlights the importance of meticulously drafting trust instruments and the need for trustees to follow their fiduciary responsibilities to avoid potential estate tax issues.

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