Estate of Klein v. Commissioner, 40 T.C. 286 (1963)</p>

For a trust to qualify for the marital deduction under the Internal Revenue Code, the surviving spouse must have the power to appoint the entire corpus, not just a portion of it.

Summary</p>

The Estate of Klein sought a marital deduction for a trust established in the decedent's will. The will granted the surviving spouse a life estate with the power to appoint two-thirds of the trust corpus. The IRS disallowed the deduction, arguing that the power of appointment did not extend to the "entire corpus" as required by the Internal Revenue Code. The Tax Court agreed, holding that the statute's plain language and the relevant regulations required the surviving spouse to have the power to appoint the entire corpus to qualify for the marital deduction. The court rejected arguments that "entire corpus" should be interpreted to mean only the portion subject to the power, and also rejected the argument that the will should be construed to create two separate trusts. The court's decision underscores the strict requirements for claiming the marital deduction, particularly regarding powers of appointment.

Facts</p>

The decedent's will established a trust for his surviving spouse, Esther. She was entitled to all of the income for life and had the power to appoint two-thirds of the trust corpus by her will. The will directed that the remaining one-third of the corpus would go to the decedent's grand-nephews. The estate sought to claim a marital deduction for the value of the trust under Internal Revenue Code §812(e)(1)(F) (now IRC §2056), arguing that the power of appointment over two-thirds of the corpus satisfied the requirement for the "entire corpus."

Procedural History</p>

The Commissioner of Internal Revenue disallowed the estate's claimed marital deduction. The estate then brought a case in the United States Tax Court to challenge the IRS's determination. The Tax Court reviewed the case based on stipulated facts and addressed the legal interpretation of the relevant Internal Revenue Code section.

Issue(s)</p>

1. Whether a power of appointment over two-thirds of a trust's corpus satisfies the requirement of Internal Revenue Code §812(e)(1)(F) that the surviving spouse have the power to appoint the "entire corpus."
2. Whether the decedent's will should be construed to create two separate trusts, thereby allowing a marital deduction for the trust with the power of

appointment over two-thirds of the corpus.

Holding</p>

1. No, because the plain language of the statute and the accompanying regulations require the power of appointment to extend to the entire corpus, not just a portion of it.
2. No, because the will clearly established a single trust, and there was no indication in the will to support the creation of separate trusts.

Court's Reasoning</p>

The court focused on the interpretation of Internal Revenue Code §812(e)(1)(F), which allowed a marital deduction for property passing in trust if, among other conditions, the surviving spouse was entitled to all the income and had a power to appoint the "entire corpus." The court found that the statute's language was clear and unambiguous, requiring the power of appointment to cover the entire corpus of the trust. "If Congress had intended the words 'entire corpus' to mean 'specific portion of corpus subject to the power,' it would have been a simple matter to express the latter view in clear and unmistakable language."

The court also examined relevant legislative history, including a Senate Report and regulations, which supported the requirement that the power of appointment must extend to the entire corpus. Furthermore, the regulations specifically stated that if the surviving spouse had the power to appoint only a portion of the corpus, the trust would not meet the conditions for a marital deduction. "If the surviving spouse is entitled to only a portion of the trust income, or has power to appoint only a portion of the corpus, the trust fails to satisfy conditions (1) and (3), respectively."

Regarding the estate's alternative argument that the will created two separate trusts, the court found no indication in the will to support this interpretation. The will consistently referred to a single trust. The court emphasized that whether an instrument creates one or more trusts depends on the grantor's intent, as demonstrated by the instrument's provisions. Absent any evidence of such intent, the court refused to rewrite the will.

Practical Implications</p>

This case highlights the importance of carefully drafting testamentary instruments to comply with tax law requirements, particularly when seeking marital deductions. Estate planners and attorneys must ensure that any trust intended to qualify for the marital deduction grants the surviving spouse the power to appoint the entire corpus. It's a crucial aspect that can't be circumvented by claiming the testator intended otherwise or that the statutory language should be interpreted in a way that favors the taxpayer. This case emphasizes that courts will strictly interpret the requirements for the marital deduction, and failure to meet the specific conditions can result in significant tax liabilities.

Later cases have continued to emphasize the specific requirements of IRC Section 2056 (formerly IRC Section 812(e)(1)(F)). It remains critical that the power of appointment granted to the surviving spouse be over the entire trust corpus to qualify for the marital deduction.

