Vander Weele v. Comm'r, 27 T.C. 347 (1956)

A transfer in trust is not a completed gift for gift tax purposes if the settlor retains sufficient dominion and control over the trust assets, either through the ability to access the corpus or because creditors can reach the income.

Summary

The case concerns whether a transfer of assets to a trust constituted a completed gift subject to gift tax. The court held that the transfer was not a completed gift. The settlor retained substantial control over the income, as creditors could reach it. Additionally, the trustees had nearly unrestricted power to invade the trust corpus for the settlor's benefit. Because the settlor retained significant dominion and control, the court found the transfer was not a completed gift, thereby avoiding gift tax liability.

Facts

Sarah Gilkey Vander Weele (the petitioner) created a trust. She transferred stocks, bonds, and a contingent remainder to the trust. The trust's terms provided the petitioner would receive all net income for life. Upon the death of her mother, the trustees could pay her "such reasonable and substantial portion of the entire net annual income" as they deemed desirable for her well-being. The trustees also had the power to invade the corpus for the petitioner's benefit, including the power to pay her up to $10,000 from principal after her mother's death and every five years thereafter. The Commissioner of Internal Revenue asserted that this transfer was a completed gift and assessed gift tax.

Procedural History

The case was initially heard in the United States Tax Court. The Tax Court considered the question of whether the transfer in trust was a completed gift, subject to gift tax under Section 1000 of the Internal Revenue Code of 1939. The Tax Court ruled in favor of the taxpayer, finding that the transfer was not a completed gift.

Issue(s)

1. Whether the transfer of assets to the trust by the petitioner constituted a completed gift under Section 1000 of the Internal Revenue Code of 1939.

2. If a gift occurred, whether the value of the gift should be reduced by the value of a retained life estate.

Holding

1. No, because the petitioner retained sufficient dominion and control over both the

income and the corpus of the trust, the transfer was not a completed gift.

2. This issue was not reached.

Court's Reasoning

The court relied heavily on the principle that a gift must be complete to be taxable. It cited its prior decisions, particularly *Alice Spaulding Paolozzi* and *Estate of Christianna K. Gramm*. In *Paolozzi*, the court found that the transfer was not a completed gift because the settlor's creditors could reach the trust income. The *Vander Weele* court found a similar situation existed in this case: under Michigan law (governing the trust), the petitioner's creditors could access the income distributable to her, so she had retained dominion over the income.

The court also focused on the trustees' power to invade the trust corpus for the benefit of the petitioner. The trust instrument gave the trustees essentially unrestricted power to pay the petitioner "such part or all of the principal" as they saw fit. Because the trustees had broad discretion to use the principal for the petitioner's benefit, the court found that the transfer of the corpus was not a completed gift. The court reasoned that there was an "unlimited possibility of withdrawal of the trust fund." The court took into account the trustees' understanding that the corpus could be used for the petitioner's personal expenses.

Practical Implications

This case provides clear guidance on the factors courts consider when determining whether a transfer in trust constitutes a completed gift for gift tax purposes. It underscores the importance of: (1) examining the settlor's continued control over the trust assets. If the settlor's creditors can reach the income, or the trustee can use the principal for the settlor's benefit, the gift may not be complete; (2) the breadth of the trustee's discretion. If the trustee has unlimited discretion to invade the principal for the settlor's benefit, a completed gift will likely not be found; and (3) the purpose of the trust. If the settlor created the trust for their own financial security, this will be a factor considered by the court.

This case helps attorneys advise clients on structuring trusts. Lawyers must carefully consider the trust's terms to ensure their client achieves their tax planning goals. Clients who want to avoid gift tax on a trust transfer must relinquish substantial control. Attorneys drafting trusts must carefully balance the client's desires for financial security with the need to make a completed gift.

The case is often cited for its discussion of completed gifts and how the grantor's control impacts the gift tax consequences of a trust. Later cases have followed the reasoning in *Vander Weele*, specifically regarding the unlimited possibility of withdrawals from the trust fund, to determine whether or not a completed gift has been made.

