Estate of Alvin Hill, Deceased, Chilton Hill, Executor, Petitioner v. Commissioner of Internal Revenue, Respondent, 64 T. C. 867 (1975)

A trust is revocable for federal estate tax purposes under IRC Section 2038(a)(1) if it lacks express terms making it irrevocable, regardless of the possibility of judicial reformation.

Summary

Alvin Hill established a trust for his daughter, Polly, but the trust instrument did not explicitly state it was irrevocable. The U. S. Tax Court held that under Texas law, the trust was revocable because it did not contain express terms of irrevocability. The court further ruled that the possibility of judicial reformation to correct the trust's terms could not be considered in determining federal estate tax consequences. Additionally, the court found that a gift of a lake cottage to Hill's son, Chilton, was not made in contemplation of death. This case underscores the importance of clear language in trust instruments to avoid estate tax inclusion and clarifies that judicial reformation does not impact federal tax treatment.

Facts

Alvin Hill, a Texas resident, created a trust (the Trigg trust) for his daughter Polly in 1970, transferring stocks worth $158,171. 05. The trust was to last for 10 years, with income distributed annually and the corpus to Polly at the end. The trust document did not state that it was irrevocable. Concurrently, Hill gifted a lake cottage to his son Chilton, which he had long intended to do. Hill was 82 and facing exploratory surgery when he made these transfers. He died seven months later.

Procedural History

The Commissioner determined a deficiency in Hill's estate tax, arguing the trust assets should be included in the estate under IRC Section 2038(a)(1) due to Hill's retained power to revoke the trust, and that the cottage gift was made in contemplation of death under IRC Section 2035. The Estate appealed to the U. S. Tax Court.

Issue(s)

1. Whether the Trigg trust was revocable at Hill's death, making its assets includable in his gross estate under IRC Section 2038(a)(1)?
2. Whether the gift of the lake cottage to Chilton was made in contemplation of death under IRC Section 2035?

Holding

1. Yes, because the trust instrument did not expressly make it irrevocable, and the possibility of judicial reformation does not affect federal tax treatment.

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2. No, because the gift was consistent with Hill's lifetime practice of making gifts to his children and was not motivated by the thought of death.

Court's Reasoning

The court applied Texas law, which presumes trusts are revocable unless expressly made irrevocable. The Trigg trust lacked such express terms, despite arguments that certain language implied irrevocability. The court rejected the Estate's contention that judicial reformation could change the trust's status for tax purposes, citing ample authority that federal tax consequences of a completed transaction cannot be altered by reformation. For the cottage gift, the court considered Hill's long-standing intent to gift it to Chilton, his pattern of lifetime gifts, and the fact that the gift was a small portion of his estate, concluding it was not made in contemplation of death despite his age and health.

Practical Implications

This decision emphasizes the need for clear, express language in trust instruments to avoid unintended estate tax consequences. Estate planners must ensure trusts intended to be irrevocable contain explicit language to that effect. The ruling also clarifies that the possibility of judicial reformation to correct trust terms does not impact federal tax treatment, a point practitioners should consider in estate planning. For gifts, the case illustrates that a pattern of lifetime giving can rebut the presumption of gifts made in contemplation of death, even when the donor is elderly or facing health issues. Subsequent cases have followed this precedent in determining the revocability of trusts and the contemplation of death for gifts.

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