Estate of Alfred Dimen, Philip Wolitzer, Executor, Petitioner v. Commissioner of Internal Revenue, Respondent, 72 T. C. 198, 1979 U. S. Tax Ct. LEXIS 131 (U. S. Tax Court 1979)

When a corporation solely owned by a decedent possesses incidents of ownership in a life insurance policy on the decedent's life, the policy proceeds are includable in the decedent's gross estate.

Summary

In Estate of Dimen v. Commissioner, the U. S. Tax Court addressed whether proceeds from a life insurance policy owned by a corporation solely owned by the decedent should be included in the decedent's estate. Alfred Dimen owned Bay Shore Flooring & Supply Corp. , which held a split-dollar life insurance policy on Dimen's life. The policy designated the corporation to receive the cash surrender value, with the remainder going to Dimen's daughter. The court held that because Bay Shore retained significant incidents of ownership, such as the power to change beneficiaries and borrow against the policy, the proceeds were taxable in Dimen's estate, emphasizing the broad interpretation of 'incidents of ownership' under tax law.

Facts

Alfred Dimen was the sole shareholder of Accurate Flooring Co. , Inc. , which purchased a life insurance policy on Dimen's life in 1964. The policy was structured so that upon Dimen's death, the cash surrender value would be paid to Accurate, with the remainder going to Dimen's daughter, Muriel. In 1969, Accurate transferred the policy to Bay Shore Flooring & Supply Corp. , another corporation wholly owned by Dimen. A supplemental agreement allowed Muriel to influence changes to the beneficiary and settlement options, but required her concurrence with Bay Shore. At the time of Dimen's death in 1972, Bay Shore had borrowed against the policy, and the policy's cash surrender value was $17,101. 24.

Procedural History

The estate filed a Federal estate tax return excluding the insurance proceeds from Dimen's gross estate. The Commissioner of Internal Revenue issued a notice of deficiency, asserting that the full proceeds should be included. The estate then petitioned the U. S. Tax Court, which heard the case and issued its decision on April 24, 1979.

Issue(s)

1. Whether Bay Shore, decedent's solely owned corporation, possessed any section 2042(2) incidents of ownership in a life insurance policy on decedent's life sufficient to warrant the inclusion of the proceeds, payable to decedent's daughter, in decedent's gross estate?

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Holding

1. Yes, because Bay Shore retained significant incidents of ownership over the policy, including the power to change beneficiaries, borrow against the policy, and the potential to surrender or cancel it, even though these powers were exercisable in conjunction with Muriel Dimen.

Court's Reasoning

The court found that Bay Shore, and thus Dimen, possessed incidents of ownership in the policy under section 2042(2) of the Internal Revenue Code. The court emphasized that 'incidents of ownership' include not only the power to change beneficiaries but also the rights to surrender or cancel the policy, assign it, pledge it for a loan, or borrow against its surrender value. These rights were retained by Bay Shore, even if they were to be exercised in conjunction with Muriel Dimen. The court also noted that the supplemental agreement did not divest Bay Shore of these powers but rather required Muriel's concurrence, which did not negate Bay Shore's ownership. The court rejected the estate's argument that Muriel's rights made her the sole owner of the 'death benefits portion,' citing the broad definition of 'incidents of ownership' and the corporation's actual exercise of those rights, such as borrowing against the policy. The court distinguished this case from Revenue Ruling 76-274, noting that Bay Shore's powers were more extensive than those of the corporation in the ruling.

Practical Implications

This decision impacts estate planning involving life insurance policies held by closely held corporations. It underscores the need for careful structuring of ownership and beneficiary rights to avoid unintended estate tax consequences. Estate planners must consider that even partial or shared control over policy incidents can lead to estate inclusion. This case has been cited in subsequent rulings to emphasize the broad scope of 'incidents of ownership' and the necessity of clear and complete relinquishment of such rights to exclude policy proceeds from the estate. It also highlights the importance of reviewing existing policies and corporate agreements to ensure they align with estate planning objectives, particularly in light of the potential for policy loans and other transactions to trigger estate tax inclusion.

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