Estate of Murray J. Siegel, Deceased, Frederick Zissu and Norman Lipshie, Executors, Petitioner v. Commissioner of Internal Revenue, Respondent, 74 T.C. 613 (1980)

Payments to a decedent's children under an employment contract are not includable in the gross estate under Section 2039 if the decedent's right to disability payments was considered wage continuation and not post-employment benefits, but are includable under Section 2038 if the decedent retained the power to alter the beneficiaries' enjoyment in conjunction with the employer.

Summary

The Tax Court addressed whether payments to the children of Murray J. Siegel under an employment contract with Vornado, Inc. were includable in his gross estate for federal estate tax purposes. Siegel's contract provided for salary continuation in case of disability and payments to his children upon his death. The court held that the payments were not includable under Section 2039 because the disability payments were deemed wage continuation, not post-employment benefits. However, the court found the payments includable under Section 2038 because Siegel retained the power, in conjunction with Vornado, to modify the children's rights under the agreement, constituting a power to alter, amend, revoke, or terminate the transfer.

Facts

Murray J. Siegel, president and CEO of Vornado, Inc., entered into an employment agreement that commenced on October 1, 1965, and was extended through amendments to November 30, 1979. The agreement stipulated that if Siegel died or became disabled during the term, Vornado would pay his salary to him or his children. Specifically, in case of death or disability, his children would receive monthly payments equivalent to his salary for the remainder of the contract term. The agreement also contained a clause stating that the children's rights could be modified by mutual consent of Siegel and Vornado. Siegel died on September 21, 1971, while actively employed, and his children became entitled to the payments. The estate excluded the commuted value of these payments from the gross estate.

Procedural History

The Estate of Murray J. Siegel petitioned the Tax Court to contest the Commissioner of Internal Revenue's determination that the commuted value of payments to Siegel's children under the employment contract should be included in the decedent's gross estate for federal estate tax purposes. This case was heard in the United States Tax Court.

Issue(s)

1. Whether the commuted value of payments to decedent's children under the

employment contract is includable in decedent's gross estate under Section 2039(a) because decedent had a right to receive post-employment disability benefits under the contract.
2. Whether the commuted value of payments to decedent's children is includable in decedent's gross estate under Section 2038(a)(1) because decedent retained a power to alter, amend, or revoke his children's rights under the employment contract.

Holding

1. No, because the agreement did not provide for post-employment benefits; the disability payments were considered wage continuation, contingent upon continued service to the best of his ability, not an annuity or other post-employment payment under Section 2039(a).
2. Yes, because the provision in the agreement allowing decedent and Vornado to mutually consent to modify the children's rights constituted a retained power to alter, amend, revoke, or terminate the enjoyment of the transferred property under Section 2038(a)(1).

Court's Reasoning

Section 2039 Issue: The court reasoned that Section 2039(a) includes in the gross estate the value of an annuity or other payment receivable by beneficiaries if the decedent possessed the right to receive an annuity or other payment. The critical question was whether the disability payments under Siegel's contract constituted 'post-employment benefits' or merely 'wage continuation.' The court emphasized that 'annuity or other payment' under Section 2039 does not include regular salary or wage continuation plans. The court found that the agreement, interpreted in light of Vornado's practices and the ongoing service obligation of Siegel even during disability, indicated that disability payments were intended as wage continuation. The court distinguished this case from *Bahen's Estate v. United States* and *Estate of Schelberg v. Commissioner*, noting that in those cases, disability benefits were more clearly post-employment benefits, not tied to a continuing service obligation. The court admitted parol evidence to clarify the terms of the agreement, finding it was not fully integrated regarding the definition of 'disability' and 'termination of employment due to disability.'

Section 2038 Issue: The court determined that Section 2038(a)(1) includes in the gross estate property transferred by the decedent if the enjoyment was subject to change through the decedent's power to alter, amend, revoke, or terminate. Paragraph Fifth of the employment agreement explicitly stated that the children's rights were 'subject to any modification of this agreement by the mutual consent of Siegel and the Corporation.' The court rejected the estate's argument that this clause merely reflected standard contract law allowing parties to renegotiate. The court distinguished *Estate of Tully v. United States* and *Kramer v. United States*, where no such express reservation of power existed. The court reasoned that by explicitly reserving the power to modify the children's rights with Vornado's consent, Siegel retained a greater power than what would exist under general contract law, making the transfer revocable under Section 2038(a)(1). The court noted that under New Jersey law and the Restatement of Contracts, third-party beneficiary rights become indefeasible unless a power to modify is expressly reserved, which was done here.

Practical Implications

This case clarifies the distinction between wage continuation and post-employment benefits under Section 2039 for estate tax purposes. It highlights that disability payment provisions in employment contracts may not trigger estate tax inclusion under Section 2039 if they are genuinely tied to continued service obligations during disability, rather than being considered retirement-like benefits. However, *Estate of Siegel* serves as a crucial reminder that explicitly reserving a power to modify beneficiary rights in an agreement, even if seemingly reflecting general contract law, can have significant estate tax consequences under Section 2038. Legal practitioners drafting employment contracts with death benefit provisions must carefully consider the wording regarding modification rights and the nature of disability payments to avoid unintended estate tax inclusion. This case emphasizes the importance of clear and unambiguous language in contracts, especially concerning estate tax implications, and the potential pitfalls of explicitly stating powers that might otherwise be implied under general law.

