Estate of Abraham Cohen, Deceased, Maurice M. Cohen, William P. Cohen and Norman D. Cohen, Executors, Petitioner v. Commissioner of Internal Revenue, Respondent, 79 T. C. 1015 (1982)

Transferred assets are not included in the estate under sections 2036(a)(2) and 2038(a)(1) if the decedent's retained powers as a trustee are limited by fiduciary duties and require consent of all beneficiaries for significant changes.

Summary

Abraham Cohen transferred common and preferred shares of a Massachusetts realty trust to his descendants. The Commissioner argued these shares should be included in Cohen's estate under sections 2036(a)(2) and 2038(a)(1) due to his retained powers as a trustee. The Tax Court held that the trustees' powers were not unlimited but constrained by fiduciary duties under Massachusetts law. The court ruled that the shares were not includable in the estate because the trustees' discretion over dividends and redemption was limited, and any alteration or termination of the trust required unanimous beneficiary consent.

Facts

Abraham Cohen, over a 28-month period ending four years before his death, transferred all his common shares and 7,350 of his 7,500 preferred shares in the Mezuries Realty Trust to his children, grandchildren, and great-grandchildren. The trust's primary function was to lease property to the Lechmere corporation, operated by Cohen and his sons. Cohen and his sons were trustees of the trust throughout the relevant period. The trust agreement allowed trustees to declare dividends, redeem preferred shares, and, with beneficiary consent, alter or terminate the trust.

Procedural History

The Commissioner determined a deficiency in Cohen's estate tax, asserting the transferred shares should be included in the estate. The estate contested this in the U. S. Tax Court, which heard the case and issued its decision on December 20, 1982.

Issue(s)

1. Whether the decedent's powers as a trustee to declare dividends and redeem preferred shares constituted a "right" to designate possession or enjoyment under section 2036(a)(2)?
2. Whether the decedent's powers as a trustee to alter or terminate the trust required inclusion of the transferred shares in his estate under section 2038(a)(1)?

Holding

1. No, because the trustees' discretion over dividends and redemption was limited

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by fiduciary duties under Massachusetts law and did not constitute an unlimited "right" to shift enjoyment between beneficiaries.
2. No, because any alteration or termination of the trust required the consent of all beneficiaries, and thus did not constitute a power to change enjoyment of the transferred property under section 2038(a)(1).

Court's Reasoning

The court relied heavily on the precedent set by *United States v. Byrum*, which held that a decedent's power to affect dividend policy was not tantamount to a "right" to designate enjoyment if constrained by fiduciary duties. The court found that the Mezuries Realty Trust, though a trust, was functionally similar to a corporation and subject to similar fiduciary constraints under Massachusetts law. The trust agreement's language suggested that dividends were expected to be declared regularly, subject to good faith business judgment, and the trustees' power to withhold dividends was not unlimited. Regarding redemption, the court noted that redeeming shares at fair market value did not diminish the beneficiaries' enjoyment. For the alteration and termination powers, the court held that these required the consent of all beneficiaries, which was consistent with their rights under Massachusetts law and thus did not trigger section 2038(a)(1). The court emphasized that the trust's structure and the decedent's lack of meaningful control over the enterprise supported its conclusion.

Practical Implications

This decision clarifies that for estate tax purposes, a decedent's retained powers as a trustee do not necessarily result in inclusion of transferred assets in the estate if those powers are limited by fiduciary duties and require beneficiary consent for significant changes. Practitioners should carefully review trust agreements to ensure that any retained powers are clearly constrained and that beneficiary consent requirements are unambiguous. This case may influence how similar trusts are structured to minimize estate tax exposure. It also highlights the importance of understanding the functional similarities between trusts and corporations when analyzing tax implications. Subsequent cases, such as *Estate of Gilman v. Commissioner*, have applied or distinguished this ruling based on the specific facts and the nature of the decedent's retained control.

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