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Marital Deduction Terminable Interests—Federal Estate Tax Hazards

The bequest to surviving spouse, commonly known as the marital deduction,\(^1\) is presently the most important tax-saving feature in the field of federal estate tax planning.\(^2\) Substantial tax savings are available to the decedent's estate through judicious employment of the marital deduction. These could ultimately accrue to the benefit of the beneficiaries of the estate.\(^3\) However, the tax benefit may be lost because of the complexity of the statute and the strict construction given these provisions by the courts.\(^4\) A majority of the difficulties arise out of the terminable interest rule.\(^5\) The central idea behind the complex provisions of the terminable interest rule are noted at the outset. If the dead hand of the testator attempts to exert control over the property given to the spouse, the deduction will be denied. The gift to the spouse must either be outright or without strings attached, except as permitted by the statute.\(^6\) If this test is not met, the bequest fails with resulting tax liability to the decedent's estate.

Because each estate has its own challenge in minimizing the tax impact, this note will analyze present tax hazards to the individual estate plan or will which employs the marital deduction.

THE MARITAL DEDUCTION

The marital deduction is, in the vernacular, an example of an eight-state tail wagging a forty-state dog.\(^7\) Prior to 1948, a surviving spouse

1. \textit{INT. REV. CODE OF 1954} § 2056 \{hereinafter cited as CODE \$\}.
2. See generally \textit{1 BOWE, ESTATE PLANNING \\& TAXATION} § 2.1, at 57-58 (1957); Glassmoyer, \textit{The Terminable Interest and the Marital Deduction}, N.Y.U. 14TH INST. ON FED. TAX 393 (1956).
5. CODE § 2056(b) (1) “Where, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail, no deduction shall be allowed under this section with respect to such interest —

(A) if an interest in such property passes or has passed (for less than adequate and full consideration in money or money's worth) from the decedent to any person other than such surviving spouse (or the estate of such spouse); and

(B) if by reason of such passing such person (or his heirs or assigns) may possess or enjoy any part of such property after such termination or failure of the interest so passing to the surviving spouse; and no deduction shall be allowed with respect to such interest (even if such deduction is not disallowed under subparagraphs (A) and (B)) —

(C) if such interest is to be acquired for the surviving spouse pursuant to directions of the decedent, by his executor or by the trustees of a trust. ”

6. CODE §§ 2056(b) (3), (5)-(6)
7 Congress has been criticized for making the vast majority of citizens in common law states adopt themselves to a community property rule through the tax statute. Paul, \textit{Erosion of the Tax Base and Rate Structure}, 11 TAX L. REV. 203, 217 (1956); see Surrey, \textit{Federal Taxation of the Family — The Revenue Act of 1948}, 61 HARV. L. REV. 1097, 1117-18 (1948)
in a community property state had a distinct tax advantage over a fellow citizen in a common law state. For example, a Texas spouse's estate paid $4,800 in taxes on a $200,000 estate, while an equivalent New York estate suffered a $31,500 estate tax. To correct this inequality, the marital deduction was enacted by Congress in 1948 to provide equal tax treatment, regardless of domicile. It allows the taxation of one half of the adjusted gross estate to be treated as though it were the wife's property, thereby escaping the immediate tax impact.

Advantages of the Marital Deduction

Deferment of taxation of one half of the husband's estate until the death of his wife can accrue very substantial federal tax savings. Each estate has a $60,000 individual exemption base, and the tax rates are lower for two halves, each half taking advantage of the low initial rates. Moreover, the wife can make substantial, non-tax gifts during her life; the estate can grow, in which case the survivors will benefit from the use of the capital; and, the need for cash liquidations at death of husband is drastically reduced. However, while the tax advantage appears obvious, there are numerous difficulties which make the marital deduction an unwise option in specific estate plans.


10. 1 BOWE, op. cit. supra note 2, at § 2.2.

11. The technical title is Bequest to Surviving Spouse, CODE § 2056 (formerly Int. Rev. Code of 1939 § 812(e), 62 Stat. 110 (1948)).


13. CODE § 2052.

14. Assume the husband gives one-half of his estate to his wife, the other half to other survivors.

15. For example, a $200,000 estate of which one-half goes to the wife, one-half to the children, the husband's estate would pay $4,800 tax. If the wife gave all of her share to the children on her death, she would also pay $4,800 tax. However, if the husband attempted to pass the entire estate to the children on his death, or give the wife a life estate, remainder to the children, the tax would be $32,700. Thus, the marital deduction tax saving would be $23,100. See CODE § 2001; but see note 22 infra for complications due to state inheritance taxes, administration expenses, etc.

Disadvantages of the Marital Deduction

Numerous ordinary tax dollar disadvantages may beset the estate planner in using the marital deduction. Thus, the half of the estate bequeathed to the wife will be subject to a second state inheritance or estate tax because most states do not allow a marital deduction. Moreover, the cost of administration of the estate on the death of the wife may amount to five to ten percent of the estate. Double state inheritance taxes and administration costs alone can be a decisive factor against the use of the marital deduction. Also, the marital deduction may be unattractive where the expected surviving spouse independently has a large estate. Moreover, other planning devices such as the annuity or life insurance may be superior alternative methods to pass tax-free property to the survivors.

Aside from the straight dollar-value factors involved in estate planning, the marital deduction statute and regulations covering the transfer of a property interest which may fail or terminate are treacherous. Thus, the most important initial question to resolve may be the objective of the potential testator.

OBJECTIVES OF TESTATOR

Of foremost importance to a person with a large estate is the desire to pass his accumulated wealth on to his family or survivors with a minimum of tax erosion. This desire, however, may be foiled by the federal tax laws which attempt to extract the maximum legally allowable tax from each testamentary transfer. Therefore, careful planning is the broad, motivating objective of the taxpayer. Unfortunately, however, the testator is seldom willing to follow the simple mandate of the marital deduction statute which directs that one-half of the husband's estate go to the wife with no strings attached. Therein lies the complexity; the husband simply refuses to let his property go. Accordingly, by his will he creates restrictions or conditions which potentially bring the bequest within the penumbra of the terminable interest rule.

17 See, e.g., OHIO REV. CODE § 5731.09 ($10,000 exemption); § 5731.12 (lower tax rates for spouse's succession). But, there is no credit or provision for successive taxable transfers. 29 OHIO JUR. 2d Inheritance & Estate Taxes § 49, at 50 (1958) Cf. CODE § 2013 (credit for taxes on transfers up to 10 years prior).

18. CODE §§ 2039, 2042; see generally I BOWE, op. cit. supra note 2, at § 2.20.


20. Commissioner v. Estate of Ellis, 252 F.2d 109 (3d Cir. 1958); Estate of Pipe v. Commissioner, 241 F.2d 210, 214 (2d Cir.), cert. denied, 355 U.S. 814 (1957). "[I]t appears that Congress looked to an absolute ownership of the surviving spouse in a community property state as the test and that anything less should not be granted the deduction unless it comes squarely within a strict construction of [an exception to the terminable interest rule]." Commissioner v. Estate of Ellis, supra at 114.

21. In Estate of Michael Melamid, 22 T.C. 966 (1954), the estate paid a $91,000 tax de-
The considerations which motivate the propertied spouse may be as follows:

1. The surviving wife may remarry and thereby either consume all of the bequest or leave it to strangers to the decedent's family by gift or will;

2. The surviving spouse may be incapable or untrained in handling large amounts of property;

3. The testator may desire to retain a particular property or business intact;

4. The testator may dislike the uncertain identity of the ultimate recipient of the property if the wife has full control over its disposition, or he may fear the possibility of a stranger exerting undue influence over the widow in the ultimate disposition of the property;

5. The wife may have a tendency to dissipate the property, in which case, the testator may attempt to restrict the wife's use or control over property built up over a lifetime;

6. The husband may fear that the wife will survive him for only a short period and thereby unnecessarily impose excessive tax and administration costs on the multiple transfers of the property.

On the other hand, the statute permits the husband to exercise some direction over the property passing to the surviving wife by the provisions for the life estate in property, a life income from a trust, or insurance and annuity contracts, as long as she alone has the power of appointment over the remainder in all events.

THE TERMINABLE INTEREST RULE

A husband's bequest to his wife will fail or terminate for federal estate tax purposes if: (1) the interest passing may not actually go to...
the wife,²⁹ or (2) if any other person may enjoy the property on failure or termination,³⁰ or (3) if such interest goes to the husband's executor or a trustee for the benefit of the wife without her control.³¹ However, a terminable interest such as a bond, note, patent, or copyright which may expire during the life of the wife, or an interest which she has received by payment of full consideration qualifies as a deduction.³²

The objective of the general rule on terminable interests is clear—to insure that property passing to the wife free of an estate tax will be taxed either at her demise or by an inter vivos transfer tax.

**Interest in Unidentified Assets**

While the terminable interest rule may appear to be an all-or-nothing risk, its most direct mechanical reduction of deductible assets occurs as to an asset which by its nature has a terminable existence.

If a bequest to the wife is based on a formula or percentage of the adjusted gross estate³³ which includes a terminable interest, the marital deduction is reduced by the amount of such asset in the estate.³⁴ A common example of such an asset is rent for a term of years. More importantly, however, are the following three exceptions within the statute.

**Interests Passing Conditioned on Survival of Spouse**

A bequest to the wife which is conditioned on the wife surviving the husband by not more than six months will not terminate and thereby lose its status as a deduction; however, the wife's death within the six months, or as a result of a common disaster, must not actually occur.³⁵ This provision is an exception to the general rule on terminable interests because it allows the husband to place a minimum survivorship condition on the passing of his property to his wife. But, this exception is clearly limited to the contingency provision. If the wife dies within six months after


²⁹. CODE § 2056(b) (1) (A).
³⁰. CODE § 2056(b) (1) (B).
³¹. CODE § 2056(b) (1) (C); see generally 1 BOWE, *op. cit. supra* note 2, at § 2.10.
³². CODE § 2056(b) (1) In Estate of Nelson v. Commissioner, 232 F.2d 720 (5th Cir. 1956), where the spouses were joint operators of a 55 acre Florida citrus farm and the husband conveyed the land to his wife and self as tenants in the entirety, the court avoided the terminable interest rule which rested on the invalidity of the conveyance for lack of valid consideration by recognition of the wife's past services "and other consideration" as sustaining the transfer under state law.
³³. Presently most estates take full advantage of the marital deduction by giving the wife 50% of the adjusted gross estate. It is called the formula method, because the will-drafter has no way of forecasting the actual pecuniary value of the estate on valuation date. See generally LOWNDES & KRAMER, *op. cit. supra* note 3, at 371. Such a method can lead to strange results and undesirable property and tax consequences. Matter of Gilmour, 18 App. Div. 2d 154, 238 N.Y.S. 2d 624 (1953) ($518,000 to the wife, $99,000 to the children).
³⁵. CODE § 2056(b) (3), Kasper v. Kellar, 217 F.2d 744 (8th Cir. 1954).
the husband’s death, and the event is a condition to the passing of the interest to the wife, the interest is terminable and the husband’s estate does not obtain the benefit of the marital deduction because nothing has vested in the wife.

**Power of Appointment Over the Remainder**

Another exception to the central mandate of the terminable interest rule is the creation of a life estate in the wife together with the power of appointment over the remainder in the wife. Although the general thrust of the statute is to force the husband to give the property outright to the wife, this exception permits the husband to give the wife a life estate; however, the wife alone, either by an inter vivos transfer or by her will must have the power to appoint the remainder in all events and without restriction. To this extent, the statute permits a deviation from the Congressional objective of uniform tax treatment in all states. The interest bequeathed to the wife may be an outright gift of the property or a grant in trust.

**Life Insurance or Annuity Contracts**

The last major exception to the general rule provides that a husband’s estate may obtain the marital deduction for an interest which passes to the spouse by way of an insurance or annuity contract. This is essentially a “trust” arrangement from which the wife receives income for life and, she alone must have the power of appointment over the remainder in all events. The theory underlying this exception is the same as that of the prior exceptions: the wife has received the entire bundle of property rights, either directly or by means of a power. Such interests will be taxable to her estate upon her demise if the property has not been consumed or given away during her lifetime.

**LOSS OF DEDUCTION IF INTEREST IS TERMINABLE**

Litigation between decedents’ personal representatives and the Commissioner of Internal Revenue concerning the applicability of section 2056(b) to bequests to the surviving wife fall into seven categories. Each of these categories represents a functional method of transferring property interests to a survivor. These are: (1) a trust with life income to the

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37. Code § 2056(b) (5).
38. In community property states, the surviving spouse owns one-half of the community property outright. LOWNDES & KRAMER, op. cit. supra note 3, at 384.
39. Id. at 398.
40. Code § 2056(b) (5).
42. Also, a life estate in the property bequeathed.
wife and power to consume the corpus; (2) gift over if wife dies before
distribution or administration of the estate; (3) life insurance contracts
payable under optional modes of settlement; (4) life estate with the
power of appointment; (5) widow's allowance for support; (6) dower
rights; and (7) transfer by intestate succession, widow's election, or set-
tlement.

Trusts With Power to Consume Corpus

In Estate of Michael Melamud,\textsuperscript{43} the testator willed all of his estate
to his wife for her use during her life together with a limited power of
invasion for maintenance of her standard of living, remainder over to
the testator's sons. The Tax Court held that where the decedent names
remaindermen to take the unconsumed estate, a mere life tenancy exists
in the wife even though there is a power in the wife to consume all of the
estate during her life. Because such a bequest is a terminable interest,
the marital deduction was disallowed. On the other hand, in Commis-
sioner v Estate of Ellis,\textsuperscript{44} one half of the estate qualified for the marital
deduction because the wife had a general power of appointment over
that part of the corpus remaining at her death. In Ellis, the estate residue
was bequeathed to a trust. All of the income was bequeathed to the wife
for her life, together with sole power to invade and consume the corpus
during her lifetime. At the widow's death, one half of the remaining
corpus was to go to her estate, the other half to named remaindermen.
However, the portion of the estate over which the widow did not have a
power of appointment was taxable, because under Pennsylvania law the
power to consume was limited. As the widow had no more than a life
estate in the trust, the entire interest did not pass to her and, therefore,
was not entitled to the marital deduction. However, the power of ap-
pointment over a specific portion of the estate did come within the ex-
ception\textsuperscript{45} to the terminable interest rule.

In Estate of Pipe v Commissioner,\textsuperscript{46} the wife had an unlimited and
uncontrolled power of invasion over the corpus but the power terminated
at her death. By denying to the wife the power of appointment or dispo-
sition through her estate, the husband's estate suffered a $19,000 tax de-
ficiency. However, New York law provided that the contingent re-
maindermen could not enforce their rights against the widow during her
life. As a result, the bequest was of the entire fee. Nevertheless, the
federal court refused to follow New York law and held the interest ter-
minable because Mrs. Pipe might fail to consume all of the corpus and

\textsuperscript{43} 22 T.C. 966 (1954)
\textsuperscript{44} 252 F.2d 109 (3d Cir. 1958); see generally Rev. Rul. 54-20, 1954-1 CUM. BULL. 195.
\textsuperscript{45} Code § 2056(b)(5)
\textsuperscript{46} 241 F.2d 210 (2d Cir.), cert. denied, 355 U. S. 418 (1957).
that interest remaining at her death could pass to another. The same result was reached in the sixth circuit case of Piatt v. Gray, where the wife had the power to invade the estate where necessary for her maintenance without having to account. The testator named his sister a contingent remainderman. The marital deduction was denied because the power of appointment was not exercisable in all events. Also, where the trust limits the wife's power of invasion of corpus to amounts for support of the wife and children, and the trustee was required to keep accounts as to sums expended on each child, the fourth circuit held that the bequest was a terminable interest because the wife did not have an unlimited power to appropriate the property. The court seized on and construed the requirement for accounting of sums spent on each child as an advancement to a remainderman, which proved the interest bequeathed to the spouse was limited to less than the requisite fee interest.

The lesson of these cases is clear: the bequest of a life estate or income for life from a trust together with a power to dispose of the remainder or corpus, which is less than an untrammelled power of appointment, will fail to qualify for the marital deduction.

Gift Over If Wife Dies Before Distribution or Administration

The statute contains another exception to the terminable interest rule based on a contingency in the will that the wife survive the husband by a maximum of six months. In the case of Kasper v. Kellar, the husband willed his wife $100,000 and one third of his residuary estate on the condition she be "alive at time of distribution of his estate." Otherwise, the bequest was to lapse and go over to other named persons. The question of the time of vesting of such a bequest was held to be controlled by South Dakota law. As there were no decisions of the state

47. Id. at 212; see CODE § 2056(b) (1) (B). In a nontrust bequest situation, where the wife had the power to "use any part of the principal," the second circuit held that the bequest was a terminable interest because under New York law it was not a general power of appointment. The grantee had to respect the rights of the remaindermen under a good faith test of invasion of corpus, and she could not make gifts inter vivos of estate property or exercise a general power of appointment over it. United States v. Lincoln Rochester Trust Co., 297 F.2d 891 (2d Cir.), cert. denied, 369 U.S. 887 (1962)

48. 321 F.2d 79 (6th Cir. 1963); accord, Estate of Semmes v. Commissioner, 288 F.2d 664 (6th Cir. 1961) where under Tennessee state law, a life estate with power to encroach upon corpus "for her own benefit, at any time she sees fit" is not equal to a fee interest and does not qualify for the marital deduction; Estate of Elwood Comer, 31 T.C. 1193 (1959), where under Ohio law, invasion for "support, maintenance, and comfort" is a limited power not qualifying for marital deduction; Rev. Rul. 55-395, 1955-1 CUM. BULL. 458.

49. See CODE § 2056(b) (5); see generally, e.g., Estate of Field, 40 T.C. 802 (1963).


51. CODE § 2056.

52. CODE § 2056(b) (3).

courts on which to resolve the issue, the case was remanded to the federal
district court for a decision based on

unreported trial court decisions, percolating judicial trends, accepted
legal climate, and familiarity with professional thought and temper.64

In *Lamar v. Bookwalter*,56 it was held that where the will required
the wife to survive the *administration* of the husband’s estate, the interest
vested at the testator’s death and the marital deduction was accordingly
allowed. On the other hand, in *Farrell v United States*,58 where survival
of the wife at estate *distribution* was a condition of transfer, the court held
the bequest to be a terminable interest even though the wife subsequent-
ly survived the distribution. The opposite result in *Lamar* and *Farrell*
difficult to justify.

*United States v. Mappes*,57 however, is clear authority on survivorship
conditions affecting the marital deduction. In that case, the husband
left the residue of his estate to his wife, but “in the event that my wife
shall die before my estate has been administered I give to
my sons all of the remainder of my property.”58 Under Oklahoma
law the bequest was conditioned and did not indefeasibly vest on the day
of testator’s death. Rather, it vested instead on the day of entry of the
judicial order directing distribution of the husband’s estate. Therefore,
the bequest failed under the terminable interest rule.

Despite the liberal results in the *Kasper*59 and *Lamar*60 cases, *Mappes*
represents the strongest authority in the field. To avoid this trap, the
will should follow the statute61 and condition transfer of the marital
bequest on a definite period of survivorship—not more than six months
after the husband’s death. An unwarranted hazard lies in using admin-
istration or distribution of estate milestones.

*Life Insurance Payable Under Optional Modes of Settlement*

The statute62 permits a marital deduction for an interest passing by
life insurance or annuity contract. The proceeds may be payable in in-
stallments so long as the wife has the sole power to appoint all of the
proceeds inter vivos or by her estate. However, in *Meyer v. United

54. 217 F.2d 744, 747-48. On remand, the district court held that the estate vested at the
testator’s death, and the six month limitation of *CODE* § 2056(b) (3) was inapplicable. 138
F. Supp. 738, 744 (D. S.D. 1956); accord, Steele v. United States, 146 F. Supp. 316 (D.
Mont. 1956) (government failed to carry burden of proof state court decree was collusive)
56. 198 F. Supp. 461 (S.D. Cal. 1961)
57 318 F.2d 508 (10th Cir. 1963).
58. *Id.* at 510.
59. 217 F.2d 744 (8th Cir. 1954)
60. 213 F. Supp. 860 (W.D. Mo. 1962), rev’d, 323 F.2d 664 (8th Cir. 1963).
61. CODE § 2056(b) (3)
62. CODE § 2056(b) (6)
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States, a $25,000 insurance contract provided for payments to the wife for life, but if she died before receiving monthly payments for twenty years the insurance company was to make the remaining payments to the daughter. The insurance company set up two funds: $18,000 to fund the twenty-year payments and $7200 to fund the post-twenty-year actuarial life expectancy of the 42 year-old widow. On the issue of whether the $7200 should qualify for the marital deduction, the Supreme Court decided that the insurance policy constituted a single property. Since it failed under the terminable interest rule none of the actuarial funds could be deducted nor did such a funding operation create any severable rights in the widow. Justice Douglas urged without success that the abstract interest representing the $7200 was deductible because it could neither fail nor pass to another person.

The Court's strict application of the statute in this insurance case parallels case developments in the trust and life estate bequest area. Where the insurance policy allowed minor administrative limitations, such as 90-day withdrawal intervals and minimum amounts on withdrawal by the widow, the policy qualified for the marital deduction as the wife had the requisite power of appointment. The rule to be gained from the Meyer case is explicit: the bequest of insurance or annuity proceeds is analogous to other forms of transfer and such transfer will be strictly interpreted against deviating estates which do not give the wife complete ownership. The entire bundle of ownership rights must go to the surviving spouse to qualify for the marital deduction.

Life Estate With Power of Appointment

The most important exception to the terminable interest rule is the life estate with a power of appointment in the wife alone and in all events. Litigation abounds on the issue of whether, in any case, the husband gave the requisite, unfettered power of appointment. The results

64. The $18,000 fund was concededly a terminable interest because it could fail and another person could succeed to it. Reg. § 20.2056(b)-6 (1958).
66. Code § 2056(b)(6); the Court also impliedly overruled In re Estate of Reilly, 239 F.2d 797 (3d Cir. 1957), an almost identical fact situation where the marital deduction was allowed for a portion of the insurance fund. There the court of appeals relied on the liberal construction of the Congressional intent to equalize community property treatment of the federal estate tax. In Meyer v. United States; 364 U.S. 410 (1960), this line of reasoning was rejected.
68. 364 U.S. 410 (1960).
from the diverse jurisdictions are bizarre. For example, in the Tax Court, a deduction was disallowed where the power of appointment was subject to a proviso that the wife retain her mental capacity, and where the wife could "do as she pleases" with the estate. Similarly, in the courts of appeals the marital deduction was disallowed where the power of appointment terminated on the widow's death and also where the widow's power over the estate was limited to selling assets for the purpose of preventing depreciation. In United States v. Lincoln Rochester Trust Co., the second circuit refused to allow the deduction where the wife had the power to use any part of the principal of the estate as under New York law such a bequest is a limited power of invasion conditioned on good faith use of the principal by the spouse.

On the other hand, the marital deduction was allowed in Gelb v. Commissioner, where a daughter was to be provided for out of the bequest to the widow. The 1958 Amendment to the statute saved this interest from failing since it permitted appointment over only a portion of the trust or estate. Previously the power had to be over the entire corpus. The same result was reached in a liberal decision of the Third Circuit Court of Appeals in Hoffman v. McGinnes. There, the testator gave the wife the power to consume any or all of the estate as she desired. The court interpreted Pennsylvania law as treating the bequest as a power of appointment which merged with the life income to give the widow the fee interest and allowed the deduction. The decision painstakingly distinguished the Ellis and Pipe decisions which had gone against the tax-

69. In the case of Freuler v. Helvering, 291 U.S. 35, 45 (1934), the Supreme Court directed the lower federal courts to follow state property law in deciding federal tax questions. The circuit courts of appeals have not been in harmony with each other on tax decisions ever since. Nevitt, Achieving Uniformity Among the 11 Courts of Last Resort, 34 TAXES 311, 312 (1956).
71. Estate of William A. Landers, 38 T.C. 828 (1962)
74. 297 F.2d 891 (2d Cir.), cert. denied, 369 U.S. 887 (1962).
75. 298 F.2d 544 (2d Cir. 1962)
76. Technical Amendments Act of 1958, 72 Stat. 1606, 1668 (1958), CODE § 2056(b) (5). The amendment had a retroactive provision covering the years 1948-54.
77. Estate of Arthur Sweet, 24 T.C. 488 (1955), aff'd, 234 F.2d 401 (10th Cir.), cert. denied, 352 U.S. 878 (1956), where the deduction was denied because the power was over only a part of the trust, has been legislatively overruled.
78. 277 F.2d 598 (3d Cir. 1960); Annot., 90 A.L.R.2d 414 (1963).
79. 252 F.2d 109 (3d Cir. 1958).
payers. In *Robertson v. United States*, the fifth circuit refused to follow the government's argument that a trust with a power of appointment in the wife failed because no beneficiary could take title to the property during the administration of the estate. The court held that because the wife was also an executrix, she had the equivalent of a power of appointment at all times.

Jointly held property and joint and mutual wills have proven to be excellent means for avoiding the impact of the terminable interest rule. In *Estate of Awtry v. Commissioner*, the husband and wife had executed a joint will, but the property passing to the wife consisted of jointly-owned bank accounts and U.S. Savings Bonds having survivorship features. The Commissioner argued that the wife had only a terminable interest because under the terms of the joint will the wife was bound as to her testamentary disposition of the property. The court held, however, that as the wife had an unlimited power of lifetime disposition of the property under Iowa law, the interest passing was deductible despite the fact that her power of testamentary disposition was foreclosed by the joint will.

In spite of the liberal trend of decisions in this area in favor of the taxpayer, substantial deviations from a strict, literal interpretation of the statute should not be taken without recognition of the grave risk.

**Widow's Allowance for Support**

In sympathy with the plight of widows the law has been generous, both in making allowances and in exempting them from taxation, by considering the transfer of a widow's allowance as a marital bequest. However, the cases have gone in all directions resolving the question of vesting of title seemingly in reliance on state property law. In Ohio,

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81. Compare Hoffman v. McGinnes, 277 F.2d 598 (3d Cir. 1960), with Commissioner v. Estate of Ellis, 252 F.2d 109 (3d Cir. 1958). The facts in each were almost identical, but in one case the wife was limited by her "desires"; in the other, by her "requirements." The results were opposite. Judge Hand said that courts should not make the dictionary a fortress, but here they seem to have done exactly that. See generally Frankfurter, *Some Reflections on The Reading of Statutes*, 47 COLUM. L. REV. 527 (1947).

82. 310 F.2d 199 (5th Cir. 1962).

83. 221 F.2d 749 (8th Cir. 1955); see generally Comment, 55 NW. U. L. REV. 727 (1961).


87. *In re* Estate of Croke, 155 Ohio St. 434, 99 N.E.2d 483 (1951).
Michigan, Illinois, Missouri, Maine, and Massachusetts the widow’s allowance is afforded the tax shelter of the marital deduction on the theory that the widow has an indefeasible title in the allowance at her husband’s death, whether it can be later lost by her death or remarriage vel non. However, in California, Georgia, and Nebraska the widow’s allowance is a terminable interest since it does not vest under state law until the probate court order directs its distribution. The Supreme Court in Jackson v United States expressly approved taxation of a widow’s allowance of $72,000 by a California probate court because, viewing the situation on the date of the husband’s death, the widow had no right to the allowance. Furthermore, the right terminated under state law if the widow died during administration or remarried. Moreover, the Court impliedly disapproved of the allowance as a deduction because of the obvious abuse at the local level. It is questionable whether $3000 per month for twenty-four months is required to support any widow. The Court also noted that Congress had expressly revoked the prior tax exemption for such allowances because of such abuse. In addition, the Court approved and followed United States v. Quivey wherein the allowance was denied deductibility because it was a terminable interest. In view of the Supreme Court’s strong opinion on this issue reliance on the widow’s allowance for tax avoidance is uncertain if more than a modest amount is allowed.

**Dower Rights**

While the importance of dower has declined as a means of transferring property, two fifth circuit cases arising in Alabama have

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94. United States v. Edmondson, 331 F.2d 676 (5th Cir. 1964), reversing United States v. First Nat'l Bank & Trust, 297 F.2d 312 (5th Cir. 1961). The fifth circuit decided against the widow's allowance on the strength of Jackson v. United States, supra note 93.
95. United States v. Quivey, 292 F.2d 252 (8th Cir. 1961).
96. 376 U.S. 503 (1964).
97. Id. at 505-06; see S. REP. No. 2375, 81st Cong., 2d Sess. 57 (1950).
98. 292 F.2d 252 (8th Cir. 1961).
99. Even though the Ohio Supreme Court vigorously insists on the vested nature of the allowance under OHIO REV. CODE § 2117.20, the law exhibits a degree of diplopia in placing exorbitant widow's allowances out of the reach of the federal tax collector and estate creditors, yet limiting the state inheritance tax exemption to $3000 total. See OHIO REV. CODE § 5731.03; see generally Bush, Widow's Exemption or Allowance and the Marital Deduction, N.Y.U. 22D INST. ON FED. TAx 1131 (1964).
100. See generally ATKINSON, WILLS § 30, at 107 (2d ed. 1953). The Model Probate Code recommends abolition of dower. Id. at 109 n.15.
held that valuable dower rights in lands which the husband owned at his death were a deductible non-terminable interest. To reach this conclusion the court employed a novel theory. That is, although common law dower which Alabama follows was only a life estate in lands which would terminate on the wife’s death, here, it was a commutable chose in action. Hence, large cash payments to the widow in lieu of dower were deductible. Consequently, it may constitute a valuable election mode in states which have a substantial dower law.103

Transfer by Statutory Election Against the Will

Transfers where the estate of the deceased consort passed to the surviving spouse by intestacy104 or through an election to take against the will105 have been held to be a non-terminable interest. Moreover, good faith settlements in lieu of taking against the will are deductible even though not the result of an adversary proceeding.106 The rationale of such decisions is aligned with the theory of the terminable interest rule. That is, intestate shares and outright transfers of cash settlements vests the property irrevocably in an estate which will be taxed on the decease of the surviving spouse. The foregoing depicts only a portion of the reasons why the election statutes107 should be given more consideration in post-estate planning evaluations in existing terminable interest situations.

STATE LAW MAY NOT CONTROL FEDERAL TAXABILITY

While an objective of federal tax law is uniformity of treatment in all states, actual practice has proven to be the opposite. The widow’s allowance cases are examples of this in where state law controls108 vesting, diverse tax results occur in the different states. Judge Mary made a cogent presentation of the dominance of state property law in

101. United States v. Hiles, 318 F.2d 56 (5th Cir. 1963); United States v. Crosby, 257 F.2d 515 (5th Cir. 1958).
102. 3 VERNIER, AMERICAN FAMILY LAWS § 189, at 352 (1935).
103. But see, e.g., Estate of Charles Elson, 28 T.C. 442 (1957), where an election by the spouse under Iowa law to take her dower rights instead of a life estate under a joint and mutual will was held invalid by the Tax Court. As the court interpreted Iowa law, a surviving party to a joint and mutual will is bound upon the death of the other party. This rationale is of questionable validity. See Netter v. Phillips, 202 F. Supp. 270 (S.D. Iowa 1962).
107. E.g., OHIO REV. CODE §§ 2107.39 (election to take up to one-half of the net estate under the statute of descent and distribution); 2117.20 (year’s allowance); 2117.24 (one year’s free rent in the mansion house of the deceased consort); and 2115.13 (exempt property).
the area of federal taxation in *Gallagher v. Smith*. Three situations are presented: (1) the federal law creates its own criteria and state law is inapplicable; (2) either the state decision involves no rule of federal tax law, or the government was not a party to the action in which case the state decisions are not binding; and (3) the state decision has concluded actual property rights in opposition to the intent of Congress which seeks to impose tax liability, in which event the state court must be followed.

While the issue of the adversary nature of the state proceeding, or the lack thereof, has controlled many case results, Judge Maris expounds a better rule:

> Whatever may be the case with respect to consent decrees, however, it is clear that if the question at issue is fairly presented to the state court for its independent decision and is so decided by the court the resulting judgment if binding on the parties under the state law is conclusive as to their property rights in the federal tax case, regardless of whether they occupied adversary positions in the state court or were all on the same side of the question.

The more recent decisions exhibit a trend of the federal courts to give more consideration to state decisions.

**CONCLUSION**

The intention of Congress that estates of decedents in common law states be afforded the same tax advantages as those in community property states has proved to be a weak and unsuccessful foundation for obtaining the marital deduction in the face of the terminable interest rule.

The application of the terminable interest rule to diverse fact situations has produced bizarre tax results. In addition, a life estate and a power of invasion of the corpus of the wife has generally failed to qualify for the deduction.

109. 223 F.2d 218 (3d Cir. 1955).
110. See 1 Paul, *Federal Estate & Gift Taxation* § 1.11 (1942). Professor Surrey summed up the situation as follows: "the plan to achieve complete equilization is inherently incapable of accomplishing its purpose. Estate splitting adopts no such nationwide uniform plan that can operate in essential disregard of local property rules, or, rather, than can operate with uniformity regardless of local variations." Surrey, *Federal Taxation of the Family* — *The Revenue Act of 1948*, 61 Harv. L. Rev. 1097, 1156-57 (1948).
113. See, e.g., Nettz v. Phillips, 202 F. Supp. 270 (S.D. Iowa 1962) where the court followed Iowa state law in declaring that the wife had a fee interest in property she received by bequest under a joint and mutual will, in which beneficiaries were named to succeed upon the decease of the survivor. To the same effect is Newman v. United States, 176 F. Supp. 364 (S.D. Ill. 1959). A crucial point of departure in this trend was the case of Estate of Awtry v. Commissioner, 221 F.2d 749 (8th Cir. 1955), reversing 22 T.C. 91 (1954). But see Estate of Charles Elson, 28 T.C. 442 (1957).
114. See, e.g., Estate of Pipe v. Commissioner, 241 F.2d 210, 214 (2d Cir. 1957) (dissenting opinion).
Survivorship for a fixed period after the husband's decease should conform to the statute and avoid use of indefinite events, such as distribution of the husband's estate.\textsuperscript{116} Life insurance contracts with the wife as beneficiary should be carefully drafted to avoid the terminable interest rule as to any portion of the policy which might fail.\textsuperscript{117}

The power of appointment cases\textsuperscript{118} provide little guidance for future action. Also, the liberal construction given recently to testamentary provisions indicates a soft line toward minor deviations in the husband's imposition of restrictions on the power of appointment.

Whether a widow's allowance is deductible is to be decided by reference to state law. However, the Supreme Court's strong disapproval of these allowances for tax deduction purposes threatens the continued efficacy of this device for future transfer of property from the estate of the husband to the widow without tax liability.\textsuperscript{119}

Dower rights,\textsuperscript{120} the widow's election, intestate succession, and settlements\textsuperscript{121} with the deceased's personal representative have all earned the marital deduction. This raises the question as to whether such actions might be useful in post-estate planning.

The most astonishing result of recent federal tax litigation is the pervading authority of local property law,\textsuperscript{122} or the court's view thereof,\textsuperscript{123} resulting in the complete disarray of federal tax decisions.\textsuperscript{124} Application of state property law to federal tax questions will undoubtedly prove to be a rich lode of future tax litigation.

Continued pressure on estates by the Internal Revenue Service's strict interpretation of the terminable interest rule is cause for a reappraisal of the use of the marital deduction. The marital deduction may be of ineffective value in reducing estate taxes.

Greater use of income tax provisions, inter vivos trusts, insurance, annuities, tax-free foundations, pension plans, and long-range investment trusts for children and grandchildren may be advisable in order to pass more property onto the testator's heirs with a minimum tax impact.

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\textsuperscript{116} United States v. Mappes, 318 F.2d 508 (10th Cir. 1963).
\textsuperscript{117} Meyer v. United States, 364 U.S. 410 (1960).
\textsuperscript{118} See, e.g., Hoffman v. Mc Guinness, 277 F.2d 598 (3d Cir. 1960); Commissioner v. Estate of Ellis, 252 F.2d 109 (3d Cir. 1958).
\textsuperscript{119} Jackson v. United States, 376 U.S. 503 (1964).
\textsuperscript{120} United States v. Hiles, 318 F.2d 56 (5th Cir. 1963).
\textsuperscript{121} See, e.g., Estate of Gertrude P. Barrett, 22 T.C. 606 (1954).
\textsuperscript{124} See Comment, Heresy in the Hierarchy: Tax Court Rejection of Court of Appeals Precedents, 57 COLUM. L. REV. 717 (1957).