Termination of Inter Vivos Trusts Under State Law and the Internal Revenue Code Section 2038

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III. Termination by a Settlor Acting in Conjunction with the Beneficiaries

Under state law a trust may be terminated prematurely if the settlor and all of the trust beneficiaries agree, provided none of them is under an incapacity. According to the American Law Institute, termination is not possible unless all of the beneficiaries consent, and this rule prevents termination of a trust if any of the beneficiaries are unascertained or unborn. This result has been criticized on policy grounds, and it has been suggested that the settlor should need only the consent of beneficiaries in being at the time the settlor seeks to terminate the trust.

A few courts, aided by technically inaccurate application of property law concepts concerning the validity of remainders, have concluded that not only persons not in being but also unascertained persons have no interest in a particular trust so as to permit its premature termination by the settlor-beneficiary with the consent of any other ascertained beneficiaries. Thus, in Dunnett v. First Nat'l Bank & Trust Co., a husband and wife created a trust wherein they reserved the right to the net income during their joint lives, except for a nominal monthly payment to their son, with the surviving settlor entitled to the net income for life. If both settlors predeceased the son, the latter

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225 Id. §340 (1). The Institute recognizes three exceptions. Partial termination is permissible under certain conditions. Id. §340 (2). Complete termination can still be had if the settlor's purpose in creating the trust is either illegal or impossible of accomplishment and where a subsequent emergency arises which would defeat or substantially impair accomplishment of his purpose. Id. §§335, 336.

226 Id. §340, comment c. The example given here is a class gift of the remainder to the income beneficiary's issue, a class not only subject to open but subject to contraction by death of any issue prior to the death of the income beneficiary.

227 Id. comment f. One illustration here involves a class gift of the remainder to the income beneficiary's children and the income beneficiary is unmarried at the time. The other is of a settlor as income beneficiary with remainder to his issue and no children yet born.

228 Note, 36 IND. L. J. 72 (1960).

229 184 Okla. 82, 85 P. 2d 281 (1938).
was to receive the corpus and all accrued income upon his attaining the age of forty-five, but if the son died prior to reaching that age, the residue was to pass as the son appointed by will, in default of appointment to the son's issue, and if default of surviving issue one-half to the husband's heirs determined as if he had died when the son did and one-half to the wife's heirs determined as of the same time. No provision was made for disposition of the corpus if the son predeceased his parents, possibly because the stated purpose of the trust was to secure a periodic income for the settlors and their son plus providing for the son's maintenance, education and financial establishment. The settlors and their son subsequently sued the corporate trustee for termination of the trust, the latter contending that termination should not be granted because of the interest of the unascertained heirs of the settlors as well as of the interest of the son's possible unborn issue. By applying the Doctrine of Worthier Title here, even though the heirs of each settlor were not to be determined as of his or her death,\footnote{The American Law Institute's position is that the Doctrine only applies where the heirs of the transferor are to be determined as of the transferor's death. \textit{Restatement, Property} §314, comment c (1940). In accord: \textit{Simes & Smith, The Law of Future Interests} §1606 (2d ed. 1956).} the court held that the heirs could not take by purchase as remaindermen but only a reversion by descent from the settlors and, hence, they did not have such a beneficial interest in the trust as to require their consent. As to the possible unborn issue of the son, the latter being 24 years of age and unmarried when the suit was instituted, the court did not expressly attempt to apply the Doctrine of Worthier Title but instead found, considering the primary purposes of the settlors to provide for themselves and their son, that the settlors did not intend the son's issue to take by purchase so their consent was not needed for termination of the trust.\footnote{Here the court also relied on New York cases decided under a statute which has been construed as requiring only the consent of living beneficiaries for the termination of a trust. See citations in note 299 infra.}

Such a "flexible" approach to the problem of identifying the beneficiaries whose consent is needed for termination of a trust may result from legal proceedings that are not really adversary but merely designed to protect the trustee by a decree that the trust should be terminated. In \textit{Bottimore v. First & Merchants Nat'l Bank}\footnote{170 Va. 221, 196 S.E. 593 (1938).} an unmarried woman created a trust wherein she reserved the right to the net income for life plus a general testamentary power of appointment. In default of appointment the corpus remaining at her death was to pass to any children that survived her and the issue of any then deceased children but, if no issue survived her, to her then surviving sisters and the issue of deceased sisters. After her marriage, the settlor petitioned for termination of the trust at a time when she had no
children and her next of kin were four sisters, alleging that she was the sole beneficiary of the trust. The four sisters were made parties defendant, but in their answer they consented to termination of the trust so far as their interests were concerned. The corporate trustee was also made a party defendant, and in its answer neither affirmed nor denied the right of the settlor to terminate the trust, but consented so far as it had either a power or interest to termination of the trust.233 Although the court admitted that if any of the beneficiaries of the trust were not in being the trust could not be terminated, the court proceeded to find, not only that any possible appointees were not beneficiaries whose consent was required since the settlor might not make a will exercising her power of appointment, but also that any surviving children and issue of deceased children of the settlor acquired no "... vested interest in the estate, because there are no such children or issue in being with a present capacity to take."234 Perhaps realizing the inconsistency of this position, the court added that any interest in the settlor's children or their issue was also contingent upon the settlor not making a will wherein she excluded them from sharing in the property.235 The court then proceeded to negative any "vested interest" in the settlor's sisters and their issue because of the double contingency that the settlor might appoint the property to others or die intestate survived by issue. The next conclusion was that in effect the trustee merely had the legal title to the trust assets for the duration of the settlor's life, i.e., an estate for the life of another, with a reversion in the settlor which would pass under her will or by intestacy to her next of kin.236 After quoting authority with respect to the

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233 The lower court having refused termination, no attorney appeared for the defendants on appeal. Should the doctrine of virtual representation be applied in such a situation so as to bind unborn issue of the settlor-beneficiary and of her four sisters? The factors affecting application of the doctrine are discussed in SIMES & SMITH, THE LAW OF FUTURE INTERESTS §1805 (2d ed. 1956). Cf. Their discussion of representation by a fiduciary, id §1811, and representation by the donee of a power of appointment, id §1812.

234 Bottimore v. First Merchants Nat'l Bank, supra note 232 at 228, 196 S.E. at 595. It is not surprising that the court did not attempt to explain how any beneficiary not in being would ever have a present capacity to take.

235 Professor Scott apparently does not consider a retained general testamentary power sufficient to dispense with the necessity of obtaining consent from takers in default of appointment. SCOTT, TRUSTS §340, at 2489 (2d ed. 1956). Cf. Note 36 Inv. L. J. 76, 81 (1960).

236 The corpus of this trust consisting of personal property, the American Law Institute's position is that, unless the settlor manifests a different intention, the trustee takes an interest of unlimited duration. RESTATEMENT (SECOND), TRUSTS §§88 (2) (1959). Since in the Bottimore case the settlor retained a general testamentary power to appoint at her death and the trust instrument provided for a gift in default of appointment, it is difficult to find an intent on her part to limit the duration of the trustee's legal title to her life. It would seem more accurate to conclude that a trust would result in favor of the settlor's estate only if she died without exercising her power of appointment and was not survived by issue, sisters, or issue of sisters. Id. §340.
Doctrine of Worthier Title, the court held that the settlor was the sole beneficiary of the trust and could terminate it.\textsuperscript{237} Since only a few states will recognize the rule in Shelley’s Case,\textsuperscript{238} the latter is less often available to aid a court in terminating a trust. But in Fowler v. Lampher\textsuperscript{239} the court may have obtained some help from the Rule. There a widow transferred both real and personal property to a corporate trustee, reserving the right to the income for life. Upon her death the trustee was to divide the corpus into six equal parts, and pay one part to each of her six named children if then living or to the child’s heirs if the child were then dead. Several years later a suit for termination of the trust was instituted. The widow, her six children and three adult grandchildren were plaintiffs. In addition to the trustee as defendant, minor grandchildren were joined and represented by a guardian ad litem.\textsuperscript{240} The trustee contended that all of the grandchildren had a contingent interest in the trust as heirs apparent of the children. Probably because the settlor was also the life income beneficiary of the trust, the court’s opinion confused the Rule in Shelley’s Case with the Doctrine of Worthier Title, and it is not clear which in fact was applied.\textsuperscript{241}

Respondent’s contention that the grandchildren have a contingent interest in the trust estate cannot be sustained. The trust agreement makes a definite provision for the division of property and designates just who should have the divided shares. It makes no provision for grandchildren unless one of the children dies before the death of the maker of the trust agreement.

In Burton v. Boren, 308 Ill. 440, 139 N.E. 868, 869, it was said: “Where a grantor conveys a life estate, with a remainder over to his heirs, the heirs do not take a remainder at all. The word ‘heirs’ will be regarded as defining or limiting the estate which the first taker has. In such case the heirs would take as reversioners by descent from the grantor and not under the deed.”\textsuperscript{242}

\textsuperscript{237} One technical difficulty in applying the Doctrine on the facts of the Bottimore case was the lack of a gift to the settlor’s heirs or next of kin generally. A gift to individuals or a class who in fact turn out to be the sole heirs of the transferor is not normally considered sufficient justification for applying the Doctrine. See citations in note 230 supra.

Furthermore, since the Doctrine is generally considered only a rule of construction, it may be rebutted and an intent to create a remainder found where the settlor has retained a testamentary power of appointment. See Matter of Burchell, 299 N.Y. 351, 87 N.E. 2d 293 (1949).

\textsuperscript{238} Simes & Smith, The Law of Future Interests §1563 (2d ed. 1956).

\textsuperscript{239} 193 Wash. 308, 75 P. 2d 132 (1938).

\textsuperscript{240} The lower court having decreed termination, only the trustee appealed.


\textsuperscript{242} Here the court is in fact stating the Doctrine of Worthier Title.
The Rule in Shelley's Case is a part of the law of this state. Fowler v. Wyman, 169 Wash. 307, 13 P. 2d 501.243

In Shufeldt v. Shufeldt, 130 Wash. 253, 227 P. 6, 11, the Rule in Shelley's Case was stated to be as follows: "Under the Rule in Shelley's Case, if an estate for life is granted by an instrument and the remainder is limited by the same instrument, either mediately or immediately, to the heirs of the life tenant, the life tenant takes the remainder as well as the life estate."244

Applying that rule we find that the grandchildren are not interested parties in the trust agreement and their consent is not necessary in order to compel its termination.245


Courts can only ascertain the intent of the parties to an agreement by the language used, and from that used in the trust agreement made by Mrs. Fowler we conclude that she did not desire to give at that time any property to her grandchildren, some of whom were living when the trust agreement was executed. Had Mrs. Fowler intended the grandchildren to have an interest in the trust she would, without doubt, have mentioned them in the agreement.247

243 This paragraph, since it immediately follows the statement of the Doctrine of Worthier Title, suggests the court thought it was in fact quoting the Rule.

244 In this paragraph the court is quoting the Rule in Shelley's Case but it appears to be unaware of the fact that the Rule deals with a remainder to the heirs of the life tenant while the Doctrine of Worthier Title, set forth in the second preceding paragraph of the quoted portion of the opinion, is concerned with a remainder to the heirs of the grantor.

245 Under the ordinary rules of grammatical construction, "that rule" should refer to the immediately preceding statement of the Rule in Shelley's Case, but doubt still remains as to whether the court in fact applied the Rule or the Doctrine of Worthier Title since the court did not elaborate as to whether the settlor as life income beneficiary also had an equitable remainder (or executory) interest or whether as grantor she had a reversion. Had the court been able to distinguish the Rule from the Doctrine, it might then have also discovered that each has different requirements for its application and a different legal effect when it is applied. E.g., the Rule is normally applied as a rule of law irrespective of the grantor's intent. Simes & Smith, The Law of Future Interests §1544 (2d ed. 1956). As a rule of law, it is confined to real property. Id. §1545; Restatement, Property §312, comment c (1940). It has sometimes been applied as a rule of construction to transfers of personal property. Leesman, The Rule in Shelley's Case in Personal Property Transfers, 32 ILL. L. REV. 935 (1938). Contrari-wise, the Doctrine of Worthier Title applies to both realty and personalty as a rule of construction generally. Simes & Smith, op. cit. supra at §§1601-1605.


246 The Johnson case in a dictum raised the question of whether the Rule applied to devisees in wills since the second of the two cited statutory sections directed courts to have due regard for the true intent and meaning of the testator.

247 This paragraph could be considered an alternative ground for the decision which is prompted by the Johnson decision's reference to the importance of giving effect to the testator's intent, note 246 supra, even though no will was involved in the Fowler case. On the other hand, it may have resulted from a belief that whatever law concerning the validity of remainders was in fact applied by the court there was a rule of construction, note 245 supra, which needed buttressing by an attempt to determine the settlor's actual intent.
It is our opinion that those interested in the Fanny Fowler trust were Mrs. Fowler and her living children, and all being of age and competent were entitled to have her trust determined.\textsuperscript{248}

The mishandling, in trust termination cases such as the three described above, of "conveyancing rules" concerning the "existence" of future interests has been explained as an attempt by the courts to determine the "quality" of such interests, \textit{i.e.}, whether, considering the settlor's subjective intent, the consent of the person or persons who may be entitled to such interests is needed for their destruction by a premature termination of the trust which brought such interests into existence.\textsuperscript{249} Requiring only the consent of beneficiaries in being at the time that termination of a trust is sought has been justified on the ground that: "The settlor, had he thought about it, would not have intended to create in such unborn persons interests which were beyond the power of the immediate parties to defeat."\textsuperscript{260} It seems dangerous to make any broad statements as to what settlors do or do not consider when they create trusts since these involve unverified assumptions.\textsuperscript{251} The possibly more Spartan alternative to modification of the law on trust termination is to require a settlor who desires a terminable trust to specify in the trust instrument the beneficiaries whose consent is required for termination.

\textsuperscript{248} Fowler v. Lampher, \textit{supra} note 239 at 319-320, 175 P. 2d at 137.
\textsuperscript{249} \textit{Id.} at 86. A second reason presented in support of such a rule is that it would further the "... policy of the free alienation of property. ..." \textit{Ibid.} But so would not requiring the consent of unascertained beneficiaries in being, resurrection of the Rule in Shelley's Case, and refusal to permit the creation of any future interests in property. The competing consideration, of course, is whether a property owner, in pursuit of various objectives, should be permitted to dispose of his property in a way which has the effect of indirectly restraining the alienation of property. For example, it may be socially desirable to permit a settlor to create a trust which cannot be terminated prematurely so as to protect the settlor and his family against his own indiscretions. See \textit{Casner, Estate Planning} 150-151 (3d ed. 1961).

A third reason advanced in favor of requiring only the consent of beneficiaries in being for the termination of a trust is that "The main attribute of the trust arrangement is that it is flexible, and this rule promotes flexibility in the control and management of property." \textit{Note, supra} note 249, at 86-87. The same could be said of a rule that makes all trusts revocable by the settlor acting alone and yet the writer of the comment apparently does not question the desirability of the present majority rule, note 50 \textit{supra}, that if a settlor does not reserve an express or implied power of revocation he cannot revoke a trust. More broadly, the issue raised here is whether the desired degree of flexibility is to be obtained by rules of law or by careful drafting of trust instruments.

\textsuperscript{251} When proponents of "law in action" research have the time, energy and money to explore this particular area, they may find it enlightening to ascertain how many trusts designed to divert income from the settlor for federal income tax purposes, at least for the term required by §673, are not administered by professional fiduciaries but rather by relatives or friends who are more likely to consent to an informal termination of such a trust in the event that the settlor needs the trust corpus prior to the formal termination date specified in the trust instrument.
A. Pursuant to the Express Terms of the Trust Instrument

State law permits a settlor to reserve a power to terminate a trust with the consent of one or more of the beneficiaries, but in such a situation termination is possible only if the settlor has obtained such consent and such a trust creates tax problems under section 2038.

Reinecke v. Northern Trust Co., involved five of such trusts. The settlor having died in 1922, the Treasury contended that such reserved powers required inclusion of the assets of the five trusts in the settlor's gross estate under the provision of the Revenue Act of 1921 concerning transfers intended to take effect in possession or enjoyment at or after a decedent's death. The Supreme Court disagreed.

If it be assumed that the power to modify the trust was broad enough to authorize disposition of the trust property among new beneficiaries or to revoke the trusts, still it was not one vested in the settlor alone. . . . He could not effect any change in the beneficial interest in the trusts without the consent, in the case of four of the trusts, of the person entitled to that interest, and in the case of one trust without the consent of a majority of those so entitled. Since the power to revoke or alter was dependent on the consent of the one entitled to the beneficial, and consequently adverse, interest, the trust, for all practical purposes, had passed as completely from any control by decedent which might inure to his own benefit as if the gift had been absolute.

The Board of Tax Appeals considered itself constrained by this decision even after Congress in the Revenue Act of 1924 had added a provision expressly applicable to the creation of an interest in trust by a settlor “. . . . where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any other person, to alter, amend, or revoke. . . .” (Emphasis added.) Hence, when a settlor created a trust in 1930 wherein her husband was a beneficiary and she reserved a power to terminate the trust with the consent of the corporate trustee and her husband, the Board refused to include the trust assets in her gross estate when she died.

252 Restatement (Second), Trusts §330, comment k (1959).
253 278 U.S. 339 (1929).
254 Revenue Act of 1921, §402(c), 42 Stat. 278 (1923).
255 Reinecke v. Northern Trust Co., supra note 253, at 346. The corpora of two other trusts, where the power of revocation was vested in the settlor alone, were held includible in his gross estate. See text preceding note 4 supra.
257 "The Settlor shall have the right, at any time, and from time to time during her life, by an instrument or instruments in writing delivered to the Trustee to modify, alter or revoke this agreement in whole or in part, or to change any beneficial interest hereunder, provided however, that no such revocation, alteration or change of beneficial interest shall be effected without the consent in writing of the Trustee and of the said Samuel James [the settlor's husband] during his life and, after his death, of the Trustee and of Frank Samuel James, brother of the said Samuel James, during his life and in case of disagreement between the Settlor and the City Bank Farmers Trust Com-
We have . . . held that Reinecke v. Northern Trust Co., . . . which arose under the Revenue Act of 1921, is controlling in cases arising under the Revenue Acts of 1924 and 1926 and that the language "through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend, or revoke" contained in section 302(d) should be construed to mean "any person not a beneficiary of the trust . . ."\textsuperscript{258}

There can be no doubt that the decedent's husband, Samuel James, was a beneficiary of the trust in question. After the death of the grantor he was to receive the income from the trust for life or for the remaining term of the trust. The facts are that the grantor died in 1931 and that Samuel James has since received and is still receiving the entire trust income. Under clause 3 of the trust agreement . . . the trustee was authorized to apply so much of the principal of the trust fund as it deemed advisable to his, Samuel James', "care, comfort or advancement in life." Under clause B he was entitled upon the termination of the trust, if then living, to receive the entire principal of the trust fund.\textsuperscript{259}

On appeal, a majority of the second circuit affirmed the Board's decision.\textsuperscript{260} Fortunately because of a contrary decision by the seventh circuit\textsuperscript{261} the Supreme Court agreed to review the case. The Supreme

\textsuperscript{258} One of its prior decisions cited at this point elaborated on the Board's reasoning as to why a reserved power exercisable only with the consent of a beneficiary was considered "not one of substance." This was due not only to the reasoning in the \textit{Northern Trust} decision, quoted in the text preceding note 255 supra, but also because, considering the legislative history, "it is not believed that Congress by the language of 302 (d) meant to require the inclusion in a decedent's estate of the value of property which the decedent in his lifetime . . . could revoke the trust only by acting in conjunction with such adverse interest." David J. Lit, 28 B.T.A. 853, 858-859 (1933), aff'd, 72 F. 2d 551 (3rd Cir. 1934).

\textsuperscript{259} City Bank Farmers Trust Co., \textit{supra} note 257, at 1144. Here the Board did not explicitly attempt to determine whether the interest of the other beneficiaries of the trust were includible in the settlor's gross estate. But in \textit{Lit}, \textit{supra} note 258, it had held that where the settlor could revoke or amend with only the consent of the beneficiary entitled to income for life, the remainder interest was includible in the settlor's gross estate.

Likewise, no consideration was given to the fact that in the event of deadlock between the settlor and the corporate trustee, \textit{supra} note 257, the power of termination was in effect in the husband-beneficiary alone. \textit{Cf.} Anna B. Kneeland, 34 B.T.A. 816 (1936), holding not taxable a trust terminable by a beneficiary other than the settlor.

\textsuperscript{260} 74 F. 2d 242 (1934). The majority considered the interest of the other beneficiaries so uncertain, because of the trustee's power of invasion in favor of the husband, that it was unfair to include them in the settlor's gross estate. The dissenting opinion considered the Board's interpretation of the legislative history of §302(d) erroneous, note 258 \textit{supra}, and that this section applied to reserved powers requiring the consent of a beneficiary. But then finding the section unconstitutional so far as it attempted to tax the husband's interest, L. Hand, J., favored disregarding the trustee's power of invasion and including in the settlor's gross estate the corpus of the trust less the actuarial value of the husband's interest in income and corpus.

\textsuperscript{261} Comm'r v. Strauss, 77 F. 2d 401 (1935), where the court applied the section literally and considered Porter v. Comm'r, 288 U.S. 436 (1933), discussed at pages 180-181 in text \textit{supra}, as both distinguishing \textit{Northern Trust Co.} and...
Court appeared to distinguish *Northern Trust Co.* as merely a different construction of a different statute. After holding that section 302(d) clearly applied to a power of termination held by a settlor in conjunction with any other person, whether or not the latter was a beneficiary of the trust, so that under the "plain meaning" rule no resort could be had to legislative history, the Court addressed itself to the constitutionality of the statute as so construed.

supporting "... the view that section 302(d) ... is a valid enactment." 77 F. 2d at 405.

The *Reinecke* case involved §402(c) of the Revenue Act of 1921 ... which directed the inclusion in the gross estate of all property "To the extent of any interest therein of which the decedent has at any time made a transfer, or with respect to which he has at any time created a trust, in contemplation of or intended to take effect in possession or enjoyment at or after his death..." It was held that a gift beyond the power of the grantor to alter, amend or revoke could not be said to take effect in possession or enjoyment at or after his death. Conversely, one which he alone held the power to revoke or modify came within this section, since, at his death, substantial interests passed from his control and were for the first time confirmed in others. The case involved nothing more than a determination whether transfers were complete when made. If they were the statute did not reach them. Here we have a different problem, for §302(d) of the 1926 Act on its face embraces Mrs. James' transfer, although complete when made and thereafter beyond her unfettered control." Helvering v. City Bank Farmers Trust Co., 296 U.S. 85, 88 (1935).

Despite this moderate language, two other decisions handed down the same day held that §302(d) would be unconstitutional if applied retroactively to trusts created in 1918 and 1919. Helvering v. Helmholz, 296 U.S. 93, 97-98 (1935); White v. Poor, 296 U.S. 98, 102 (1935). See Lowndes, *A Day in the Supreme Court with the Federal Estate Tax*, 22 VA. L. Rev. 261, 279-284 (1936). Hence, Treas. Reg. §20.2038-1(d) provides: "... if an interest in property was transferred by a decedent before the enactment of the Revenue Act of 1924 (June 2, 1924, 4:01 p.m., eastern standard time), and if a power reserved by the decedent to alter, amend, revoke, or terminate was exercisable by the decedent only in conjunction with a person having a substantial adverse interest in the transferred property, or in conjunction with several persons some or all of whom held such an adverse interest, there is included in the decedent's gross estate only the value of any interest or interests held by a person or persons not required to join in the exercise of the power plus the value of any insubstantial interests or interests of a person or persons required to join in the exercise of the power." On whether a transfer in trust was completed prior to the effective date of the Revenue Act of 1924 and, if so, whether the person or persons who must consent to the settlor's termination of the trust have a substantial adverse interest, see *MERTENS, LAW OF FEDERAL GIFTS AND ESTATE TAXATION* §§25.42-25A3 (1959).

The respondent says that the section ought to be construed in the light of the analogous §219(g). The latter, part of the income tax title, is "Where the grantor of a trust has, at any time during the taxable year, either alone or in conjunction with any person not a beneficiary of the trust, the power to revest in himself title to any part of the corpus of the trust, then the income of such part of the trust for such taxable year shall be included in computing the net income of the grantor." The two sections have a cognate purpose but they exhibit marked differences of substance. The one speaks of a power to be exercised with one not a beneficiary; the other of a power to be exercised with any person. The one refers to a power to revest the corpus in the donor; the other has no such limitation. It is true, the Report of the Ways and Means Committee on §302(d) said 'this provision is in accord with the principle of Section 219(g) of the bill which taxes to the grantor the income of a revocable trust.' But to credit the assertion that the difference in phraseology is without significance and in both sections Congress meant to express the same thought, would be to disregard the clear intent of the phrase 'any
The respondent insists that a power to recall an absolute and completed gift only with the consent of the donee is in truth no power at all; that in such case the so-called exercise of the power is equivalent to a new gift from the donee to the donor. And so it is claimed that the statute arbitrarily declares that to exist which in fact and law is nonexistent. The position is untenable. The purpose of Congress in adding clause (d) to the section as it stood in an earlier act was to prevent avoidance of the tax by the device of joining with the grantor in the exercise of the power of revocation someone who he believed would comply with his wishes. Congress may well have thought that a beneficiary who was of the grantor's immediate family might be amenable to persuasion or be induced to consent to a revocation in consideration of other expected benefits from the grantor's estate. Congress may adopt a measure reasonably calculated to prevent avoidance of a tax...  

But a companion decision handed down the same day created confusion as to when an express provision permitting the settlor to terminate the trust with the consent of specified beneficiaries would attract a tax at the settlor's death. In Helvering v. Helholz on it was not completely clear under the terms of the trust instrument involved as to which beneficiaries had to consent to termination of the trust, nor whether the Supreme Court understood the American Law Institute's position on when such a trust could be terminated under state law in the absence of any reserved power of termination. There Patrick Cudahy, his wife and then living children owned most of the stock of the Patrick Cudahy Family Company. In 1918, desiring to keep the ownership of such stock confined "... so far as practicable to those of the immediate family of ... Patrick Cudahy, their descendants and appointees, ... the subscribers hereto ... transfer to Wisconsin Trust Company ... in trust the shares of stock ... set opposite their respective names. ..." A total of 10,491 shares were transferred to the trust by the members of the family, decedent contributing 999 out of the 1000 shares she owned. The substantive provisions of the primary trust provided that each subscriber was to receive for life the net dividends earned on the shares of stock each contributed to the trust. In addition, each subscriber

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265 The entire trust instrument is set forth in Exhibits A and B, pp. 7-19 of the Record on Appeal filed with the Wisconsin Supreme Court in First Wis. Trust Co. v. Helholz, 198 Wis. 573, 225 N.W. 181 (1929).

266 Waldemar R. Helholz, 28 B.T.A. 165, 167-168 (1935). Decedent's four sisters and one of her brothers each also contributed 999 shares, her other brother contributed 899, her mother 3,549 and her father 49. The other stockholders, the estate of a deceased sister and the Patrick Cudahy Institute, each owned 1000 shares but did not contribute to the trust.
had a testamentary power to appoint his or her right to dividend income to any natural person or persons for life or to one or more charitable organizations at least for the duration of the primary trust. Upon failure of any subscriber to effectively exercise his or her power of appointment at death, his or her right to dividend income passed to any surviving issue, but if a subscriber died without surviving issue or the issue subsequently became extinct, the right to dividend income passed to the surviving subscribers or their issue by right of representation. The paragraph concerning termination of the primary trust provided:

The term of the primary trust hereby created shall end (1) upon the death of the last surviving grandchild of Patrick and Anna M. Cudahy, they being then deceased, or (2) upon delivery to the said trustee of a written instrument signed by all of the then beneficiaries, other than testamentary appointees, declaring said trust at an end, or (3), upon delivery to said trustee of a copy . . . of a resolution adopted by the unanimous vote of the board of directors of said corporation declaring said trust term at an end,268 whereupon and in either of said events the said trustee shall distribute the capital stock of said The Patrick Cudahy Family Company to the beneficiaries then entitled to receive the net dividends thereon other than testamentary appointees; excepting the shares to the dividends upon which such testamentary appointees are entitled, which shall be held by said trustee as hereinbefore provided.269 (Emphasis added.)

The term of the primary trust hereby created shall also terminate upon the dissolution of said The Patrick Cudahy Family Company in the manner and for any of the causes provided by law, whereupon the trustee shall distribute all the proceeds and assets by it received upon the liquidation of said corporation to the beneficiaries other than testamentary appointees then entitled to receive net dividends or income in the proportion in which they are severally entitled, excepting the proceeds and (or) assets of shares to the net dividends or income upon which testamentary appointees are entitled.

269 As to appointments to one or more natural persons, the prior dispositive provisions provided: "In the event of the termination of the primary trust hereby created, no capital stock of The Patrick Cudahy Family Company or other capital assets shall be distributed to any such testamentary appointee, but the portion thereof to the dividends or income upon which such testamentary appointee is then entitled shall thereafter be held by said Wisconsin Trust Company for the term of such appointment, in trust, to pay the net dividends or income thereof pursuant to such appointment, . . . and upon the termination of the term of said testamentary appointment the said capital stock . . . or other capital assets shall be distributed as hereinafter provided for the distribution of the same upon the termination of the primary trust hereby created." In the event that a subscriber named a charitable organization as testamentary appointee, upon the termination of the primary trust the portion of the corpus from which the charitable organization was entitled to receive income was to be turned over to the Milwaukee Foundation, a community trust, and, to the extent permissible under the rules governing this secondary trust, was to be used for the benefit of the charitable organization which the subscriber had named as testamentary appointee.
appointees are entitled, which shall continue to be held in trust as hereinbefore provided.\textsuperscript{270} (Emphasis added.)

The term of the primary trust hereby created shall also terminate upon the extinction of issue of the said Patrick and Anna M. Cudahy, they being then deceased, whereupon the said trustee shall convey and transfer the stock of said The Patrick Cudahy Family Company to the Wisconsin Trust Company as trustee, to have and to hold the same upon the trusts and for the uses and purposes embraced in a certain resolution or declaration of trust adopted by the board of directors of the Wisconsin Trust Company May 24, 1915, establishing a certain community trust known as the Milwaukee Foundation for administration and distribution as in said trust declaration prescribed and defined, subject, however, to any existing valid testamentary appointments made by subscribers hereto as hereinbefore provided.\textsuperscript{271}

After decedent’s death in 1927 leaving a will exercising her testamentary power to appoint her right to dividend income in favor of her surviving husband,\textsuperscript{272} the Commissioner contended that the stock transferred in trust by the decedent was includible in her gross estate under section 302(d) of the Revenue Act of 1926. The Board did not expressly attempt to determine which beneficiaries had to consent to termination of the trust as “all of the then beneficiaries, other than testamentary appointees,” but seemed to assume that this phrase included remaindermen entitled to the corpus upon termination of the trust other than the settlor, despite the fact that in quoting the provision on termination by the beneficiaries it also quoted the provision giving the corpus of the trust, upon such a termination, to the current income beneficiaries other than testamentary appointees.\textsuperscript{273} But on appeal, the Court of Appeals for the District of Columbia did attempt to construe this phrase, emphasizing that it required

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\text{... a writing signed by all the then beneficiaries (other than testamentary appointees). Obviously, this gave no power to Mrs. Helmholz to revoke the trust. Granted she became, by virtue of the reservation of a life estate in the income, one of the beneficiaries, she is only one. Her issue, if she has any, from the moment of the making of the trust, are potential beneficiaries. Her father and mother, as well as her brothers and sisters, are likewise potential beneficiaries, and so is the issue of all of them. And nothing is better settled under the statutes, as of the time we are speaking, than the proposition that, where the revocation}
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\textsuperscript{270} Here again, the reference to prior provisions concerning testamentary appointees in the event of termination of the primary trust are those quoted and summarized in the immediately preceding footnote.

\textsuperscript{271} See note 269 \textit{supra}. The entire termination clause was quoted in the Supreme Court’s opinion, Helvering v. Helmholz, \textit{supra} note 265, at 94-96.

\textsuperscript{272} First Wis. Trust Co. v. Helmholz, \textit{supra} note 266.

\textsuperscript{273} The portion of the termination clause quoted by the Board is set forth in the text preceding note 68 \textit{supra}. 

of a trust depends for its exercise upon the assent of the beneficiaries, it is not within the statute.\textsuperscript{274}

This construction may have included more than current income beneficiaries, other than testamentary appointees, in the group whose consent is required for termination of the trust. But it is not clear whether the court of appeals meant to limit the group to current income beneficiaries plus "potential" beneficiaries in being when termination of the trust was sought or to also include yet unborn issue of the settlors. The Supreme Court's interpretation of the phrase is also not clear. In referring to the Commissioner's argument for inclusion of the stock contributed to the trust by the decedent in her gross estate because the trust could be terminated by a writing signed by all the then beneficiaries (other than testamentary appointees), the Court stated:

He points out that such a writing might have been executed by Mrs. Helmholz and her co-beneficiaries while she was alive, with the effect of revesting in her the shares which she had delivered into the trust. This argument overlooks the essential difference between a power to revoke, alter or amend, and a condition which the law imposes. The general rule is that all parties in interest may terminate the trust.\textsuperscript{275} The clause in question added nothing to the rights which the law conferred. Congress cannot tax as a transfer intended to take effect in possession or enjoyment at the death of the settlor a trust created in a state whose law permits all the beneficiaries to terminate the trust.\textsuperscript{276}

The Court may have adopted one of at least three possible constructions of the phrase "all of the then beneficiaries, other than testamentary appointees." One possible construction is that the decedent with the consent of only the other beneficiaries currently receiving trust income, other than testamentary appointees, could terminate the trust. This is a plausible interpretation considering that these persons were entitled to the trust corpus upon such a termination.\textsuperscript{277} If this construction was adopted, the Court appears to be incorrect in stating that this termination provision created no rights beyond those conferred by state law as set forth by the American Law Institute.\textsuperscript{278} A second possible construc-

\textsuperscript{274} 75 F. 2d 245, 247 (1934).
\textsuperscript{275} At this point the Court cited Restatement, Trusts §§337, 338 (1935), since it stated that it had not been referred to any Wisconsin authority to the contrary.
\textsuperscript{276} Helvering v. Helmholz, supra note 265, at 97.
\textsuperscript{277} This construction by the Court was assumed in the prior discussion of Helmholz at pages 174-176 in text supra. It also seems to have been used in a contemporary comment on the decision. Lowndes, The Tax Burden of the Supreme Court 1935 Term, 5 Fordham L. Rev. 426, 447 (1936).
\textsuperscript{278} Restatement, Trusts §340(1), comment d and f (1935). Although Mrs. Helmholz, if the trust were not terminated prior to her death, could have diverted both her share of income and corpus from her issue, the other settlors and their issue by naming a charitable organization as testamentary appointee (each of the other settlors having the same power of diversion as to their respective contributions), note 269 supra, the Restatement gives no indication that this prevents such individuals from being beneficiaries whose consent
tion is that consent to termination had to be obtained not only from current income beneficiaries but also from all "potential" beneficiaries in being at the time termination of the trust was sought, but this also appears contrary to the position of the American Law Institute which forbids termination when the trust terms provide a gift to a class subject to open, i.e., where beneficiaries may yet be born. A third and less plausible construction is that "then beneficiaries" excluded only those who died prior to the time termination was sought. This construction would be consistent with the American Law Institute's position but, if the Court had so interpreted the phrase, it could have simply held that Mrs. Helmholz and her co-beneficiaries in being at her death could not have terminated the trust if there was then still a possibility of additional issue being born to any of the settlors, a result which the settlors may not have intended back in 1918, seventeen years prior to the publication of the American Law Institute's first Restatement of the Law of Trusts.

Considering the variety of possible reactions to Helmholz, it is not surprising that subsequent decisions exhibit a lack of consistency with respect to this case. Thus, where a decedent was entitled to the income for life from a trust, her two nieces being entitled to the income for life after decedent's death, and this was followed by a provision for each niece's surviving heirs of her body with alternative provisions if none survived, the decedent had a reserved power to revoke the trust with the consent of only her two nieces. After decedent's death survived not only by her two nieces but two children of one of the nieces, it was urged that the phrase "all of the then beneficiaries" in Helmholz "had reference only to beneficiaries with vested interests, and did not include beneficiaries with contingent interests." Hence, it was contended that the two nieces were the only beneficiaries with vested interests, in addition to the decedent, and a power to revoke in these three persons was not taxable under Helmholz. But the Board disagreed.

We think it clear that Helvering v. Helmholz, . . . is not authority for the proposition stated. The Supreme Court there made no distinction between the holders of vested interests and holders of contingent interests. The Court stated that the gen-

279 See citations in the immediately preceding footnote, especially comment f.

280 Cf. note 251 supra and the text preceding it.

281 Virginia L. Houghteling, 40 B.T.A. 508, 513 (1939). The emphasis on the classification of future interests (cf. the common law distinction between vested and contingent remainders with RESTATEMENT, PROPERTY §157 (1936), which distinguishes three types of "vested" remainders) rather than the trust law distinction between ascertained and unascertained or even unborn beneficiaries may have been dictated by controlling state law on the termination of trusts.

282 This suggests the Board considered the trust in Helmholz required the consent of beneficiaries in addition to those currently entitled to income for termination of that trust.
eral rule is that all parties in interest may terminate the trust, and in a footnote there is a statement to the effect that no authority has been cited to the contrary in Wisconsin, the place of the transaction. Then with respect to the provisions of the trust instrument there under consideration the Court said "The clause in question added nothing to the rights which the law conferred," and then concluded as follows: "Congress can not tax as a transfer intended to take effect in possession or enjoyment at the death of the settlor a trust created in a state whose law permits all the beneficiaries to terminate the trust." 283

The Board then proceeding to determine that under the law of Illinois, which was controlling as to the trust under consideration, the decedent and her two nieces could not cut off the rights of the niece's children, even though their interests were contingent, so the reserved power of the decedent to revoke the trust with the consent of her two nieces gave them rights beyond those conferred under the law of Illinois and required inclusion of the trust assets in decedent's gross estate. 284

But in Estate of Charles M. Thorp; 285 the Tax Court took another look at Helmholz, and concluded that the trust in Helmholz could be terminated by beneficiaries living at the time termination was sought and may have inferred that these were current income beneficiaries other than testamentary appointees. In Thorp a father had created a trust with income payable to his six named children until the death of the last surviving child when the trust was to terminate and the corpus distributed to any then living grandchildren and the children of any then deceased grandchildren. The trust could be terminated earlier by the father in conjunction with any children then living. The trust having been created prior to 1924, the court held that the reserved power to terminate affected only the remainder interests and included them in the settlor's gross estate after his death in 1942.

Since the exercise of such power could cut off those interests, their transfer was not complete until the death of the settlor put an end to its existence. Hence, there is here present no retroactive application of section 811(d)(2) and the due process clause of the Fifth Amendment is not infringed. . . . 286

Petitioners argue that . . . Helmholz . . . prevents this conclusion. We do not agree. In that case the . . . beneficiaries of the remainders were to be the income beneficiaries when the trust.

284 In this decision the Board apparently considered itself constrained by Helmholz to give effect to any type of state law on trust termination. "If they had the same rights to revoke under the laws of Illinois and could thereby cut off the rights of the children, the ruling in Helvering v. Helmholz, . . . would be applicable. . . . Virginia L. Houghteling, supra note 283. However, two years later the Board refused to be bound by a Louisiana statute making all interspousal gifts revocable. Estate of Felicia Gimbel Keiffer, 44 B.T.A. 1265 (1941), discussed at pages 178-179 in text supra. Cf. Estate of Henry Hauptfuhrer, note 292 infra.

286 See note 262 supra.
terminated. The appointees by will could not, under the trust, take remainders. So, in that case, the termination could be brought about only by all the beneficiaries in the remainders who were living when the trust terminated...

There is another difference which distinguishes this case from the Helmholz case. The Supreme Court there held that, under pertinent Wisconsin law, the termination of a trust by the beneficiaries who were living at the time of termination was legally possible. The law of Pennsylvania, which is controlling here, is otherwise. In that state the rule is recognized that a trust can be terminated only by the consent of all the beneficiaries and, where there are interests which can not be determined until the happening of a certain event, the consent of the then living beneficiaries is not sufficient.... Moreover, the present record is silent not only as to the existence of grandchildren, who were the remaindermen, but also as to whether if none, there never could be any.

This reaction to Helmholz was repeated a short time later in Estate of Lelia E. Coulter involving a trust created in 1920 by a mother and her three adult children, the mother contributing half of the corpus. The income was payable to the four co-settlors until the death of the mother when the corpus was to be distributed to the three children. If a child died before his mother, his or her share of the income and corpus was to go to his or her testamentary appointees or, upon death intestate, to his or her heirs at law. The settlors reserved a power to terminate the trust prior to the mother’s death with the corpus then being distributed in the same way that it would had there been no termination until the mother’s death. Here the Tax Court first treated both the children’s testamentary appointees or heirs at law as contingent remaindermen whose interests would be cut off by the exercise of the power of termination prior to the children’s deaths. Helmholz was then discussed.

On first impression, the situation here might appear to resemble that in... Helmholz wherein it was held that the transfer there involved was not includible in the decedent’s gross estate. As was pointed out in... Thorp... termination of the trust in the Helmholz case could be brought about by all the beneficiaries in the remainders who were living at the time of termination. In the instant case, participation by devisees or legatees or heirs at law of a deceased child-grantor was not required to terminate, since this could be accomplished only by

287 Estate of Charles M. Thorp, supra note 285, at 923-924. Although the state court decisions are divided, the American Law Institute’s position is: "If the unascertained beneficiaries are the children of a designated woman, and the woman is beyond the age of childbearing or otherwise physically incapable of bearing children, the court may terminate the trust." Restatement, Trusts §340, comment e (1959); Scott, Trusts §340.1 (2d ed. 1956).

288 7 T.C. 1280 (1946).

289 See note 278 supra. At the mother’s death she was survived by her three children, their spouses and children. Each of the three children had executed a will in favor of his or her family.
the decedent and the surviving children-grantors. There is also another difference which distinguishes this case from the Helmholz case. In that case the Supreme Court held that, under applicable Wisconsin law, termination of a trust by the beneficiaries living at the time of termination was legally possible. The law of California, which controls here, is otherwise. In California the rule is that a trust can be terminated by the consent of all the beneficiaries. But where there are interests which cannot be determined until the happening of a certain event, the consent of the living beneficiaries is not sufficient.

The court concluded that after the mother's death in 1942 with the reserved power in effect one-half of the corpus had to be included in her gross estate.

This continuing emphasis on the difference between when a trust could be terminated under a reserved power and when it could be terminated, in the absence of such a reserved power, under controlling state law also attracted a tax where a settlor expressly negatived any right to revoke as settlor but provided that the trust could be terminated "by all the then living beneficiaries hereof who are twenty-one (21) years or more of age" and then made himself a contingent income beneficiary in the event he survived his wife, even though the settlor in fact predeceased his wife.

Helvering v. Helmholz, relied upon by petitioner, is distinguishable. It was therein held that a trust created in a state whose law permits all of the then beneficiaries to terminate the trust was not taxable. The trust there involved was a Wisconsin trust. The trust herein was established in Ohio. Under the laws of Ohio a trust may be terminated by consent if "all the parties who are or may be interested in the trust property are in existence and sui juris." Where there are contingent interests which cannot be determined and adjusted until the happening of certain events, the trust cannot be terminated.

The court did not specifically refer to these contingent interests but the corpus was distributable on the death of the survivor of the settlor and his wife to his son if then living, otherwise to the son's then living issue.

When subsequently faced with the contention that three trusts created by a decedent for each of his three sons (each providing life income for the son plus a special power to appoint the remainder, exercisable during lifetime or by will, with a gift in default of appointment to the son's then surviving children and issue), could have been terminated by the sons, with the consent of the settlor, under Pennsylvania law even though each trust had not expressly reserved a power in the settlor and the son to terminate the trust in favor of the son, the Tax Court stated with respect to Helmholz:

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290 Estate of Lelia E. Coulter, supra note 288, at 1290-1291.
291 Estate of A. Frank Seltzer, 10 T.C. 810, 816-817 (1948), aff'd per curiam, 174 F. 2d 207 (6th Cir. 1949).
The Court did not say that Congress could not tax in the estate of a settlor property which he held a power to terminate, whether the power was reserved in the trust agreement or was conferred by state law. This was the position taken by the Circuit Court of Appeals for the Third Circuit in Commissioner v. Allen, 108 F. 2d 961...

But, on appeal, the third circuit avoided even mention of its prior decision, possibly because it now realized the weakness of its prior attempt to distinguish Helmholz as involving a trust terminable by the decedent as a beneficiary rather than in her capacity as settlor. Instead, the court rejected the taxpayers' contention that the settlor and his three sons could have terminated the trusts under Pennsylvania law in the absence of any reserved power of termination. Since the interests of at least some of the possible appointees of each son and the remainders in the takers in default could not have been extinguished but for the fact that the settlor and each son had a reserved power to terminate each trust in favor of the respective son, the corpora of the three trusts was held includible in the deceased settlor's gross estate.

In the Hauptfuhrer's Estate v. Comm'r case the third circuit stated that the Treasury Regulations had incorporated the rule of the Helmholz case. The Treasury Regulations do provide that "... section 2038 does not apply—... (2) If the decedent's power could be exercised only with the consent of all parties having an interest (vested or contingent) in the transferred property, and if the power adds nothing to the rights of the parties under local law. ..." (Emphasis added.) It is highly doubtful that this is what the Supreme Court held in Helmholz. There is first the question of whether the Treasury in referring to the consent of all parties having a vested or contingent interest meant to include not only unascertained but also unborn beneficiaries, i.e., adopt the American Law Institute's position on when a settlor can and can not terminate a trust with the consent of beneficiaries. If so, this is the most unlikely construction of the "then beneficiaries" phrase in the trust under consideration in Helmholz. In addition, it is not in accord with the Tax Court's reaction to Helmholz in decisions starting with and since Thorp. The last part of the quoted regulation raises the question of whether the first part sets up a standard independent of local law variations so that state law on termination of trusts is relevant.


294 Id. at 551. The court quoted Treasury Regulation 105, §81.20, which is substantially the same as the present regulation.

295 Treas. Reg. §20.2038-1 (a) (2).

296 See text discussion preceding note 280 supra.

297 Note 285 supra.
only in the unlikely event that it sets up requirements in addition to those set forth in the first part of the regulation.  

B. PURSUANT TO THE TERMS OF A STATE STATUTE

Several states have by statute modified the position adopted by the American Law Institute that, absent a reserved power, a trust can not be terminated by a settlor in conjunction with ascertained beneficiaries if there are unascertained or possible unborn beneficiaries. The question of whether trusts governed by such legislation are includible in the settlor's gross estate under section 2038 does not appear to have been answered by judicial decision but it has been discussed. Here again, the question is as to the effect, if any, of *Helmholtz* in such a situation. If the decision means that any state law on trust termination does not attract a tax, then trusts subject to state statutes modifying the American Law Institute's position may escape estate tax where trusts governed by state law in accord with the American Law Institute's position would attract a tax if they contain an express power of termination which confers rights upon the settlor not accorded by state law. As has been seen, courts have not been deterred by *Helmholtz* from taxing trusts made revocable by the settlor alone by virtue of a state statute. According to the Treasury Regulations a power of termination is taxable whether arising from "... the express terms of the instrument of transfer or by operation of law..." In addition, "... section 2038 does not apply ... (2) If the decedent's power could be exercised only with the consent of all parties having an interest (vested or contingent) in the transferred property..." It would seem that settlors and beneficiaries of trusts subject to the laws of such states as New York, North Carolina, Oklahoma and Wisconsin are entitled to an official ruling from the Treasury on the relationship of statutes on termination of trusts in these states to section 2038.

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298 See the discussion in Lowndes & Kramer, *Federal Estate and Gift Taxes* 165-166 (2d ed. 1962).
301 See pages 178-179 in text supra.
302 Treas. Reg. §20.2038-1(c). Although this regulation deals with trusts created prior to June 23, 1936, presumably the same rule is applicable to trusts created after that date.
303 See supra note 295.
304 See citations in note 299 supra.