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Estate and Gift Tax--Gratuitous Conveyance in Fee Simple--Oral Retention of Enjoyment by Grantor for Live

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not be removed without destroying the surface, they would have specifically mentioned limestone had they intended to convey it. *Beury v. Shelton,* 151 Va. 28, 144 S.E. 629 (1929). In viewing this case, at least one noted authority has stated that by a similar process of reasoning, "strip" coal is not a mineral. Indeed, there are indications that the West Virginia court may so hold. DONLEY, COAL, OIL & GAS IN WEST VIRGINIA AND VIRGINIA §§ 30-33 (1951).

In conclusion, West Virginia has tended to follow the majority and better view that petroleum oil and natural gas are included in the term "minerals" as used in a conveyance or exception in a deed, unless a contrary intent is clearly shown. Under this view the principal case, which states the applicable and recognized law of Pennsylvania, is contra to this theory and is definitely the minority holding. In the writer's opinion, this case would therefore be followed by very few courts today.

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ESTATE AND GIFT TAX—GRATUITOUS CONVEYANCE IN FEE SIMPLE—ORAL RETENTION OF ENJOYMENT BY GRANTOR FOR LIFE.—Decedent gratuitously executed general warranty deeds to his children for income-producing real estate. The deeds did not recite any reservation of interest in either the realty or rents; however, decedent entered into oral agreements with his grantees under which he was entitled to, and actually did receive, all rents until he died. The Tax Court of the United States upheld the commissioner's inclusion of the realty in decedent's estate. *Held,* that the retention of the right to the rents, even though disassociated from the instruments of conveyance, did not preclude the application of the retention-of-enjoyment meaning of the statute (Int. Rev. Code of 1954 § 2036) if decedent in fact did so enjoy the property during his life. Thus, the value of the premises was properly included in decedent's gross estate for federal estate tax purposes. *McNichol v. Commissioner,* 265 F.2d 667 (3d Cir. 1959).

The element making this case worthy of attention was not the gratuity of the transaction, but the oral retention of the enjoyment of the property for life. It is true that the absence of any consideration prevented the transfer from being a bona fide sale, but it is equally true that the presence of nominal consideration would not have been "adequate and full consideration in money or money's worth" and thus the transfer would still not have been eligible for denomination as bona fide. Before examining the various attempts to circumvent the statutory section in issue, a brief resumé of its history appears germane.

May v. Heiner, 281 U.S. 238 (1930), holding that retention of life income did not result in the corpus of a trust being included in the settlor's estate, wreaked havoc upon previous judicial and administrative interpretations of section 302 of the Revenue Act of 1926 which had theretofore uniformly and frequently been construed to apply to the reserved life estate situation. The decision was followed in three per curiam opinions on March 2, 1931. *Commissioner v. Northern Trust Co.,* 283 U.S. 782 (1931); *Morsman v. Commissioner,* 283 U.S. 783 (1931); *McCormick v. Commissioner,* 283 U.S. 784 (1931). To close this obvious tax loophole a joint resolution was enacted by Congress on March 3, 1931, to make the retention of a life estate sufficient to require the inclusion of the corpus upon which it was based in the gross estate of the settlor. The relevant part of the codification of this resolution provided that the estate would be taxed if the decedent "has retained for his life . . . (1) the possession or enjoyment of, or the right to the income from, the property. . . ." INT. REV. CODE of 1954 § 2036. The Treasury attempted to give retroactive effect to the joint resolution until *Hasset v. Welch,* 303 U.S. 303 (1938), declared its operation prospective only, at which point the Treasury regulations were conformed. An amendment in 1949 provided that no estate tax was created by the retention of a life estate where the transfer was made before March 4, 1931, and where the decedent died before January 1, 1950. 63 Stat. 895 (1949) (now INT. REV. CODE of 1954 § 2036). It should be noted, however, that the amendment only reflected congressional solicitude for taxpayers who, in reliance upon the *May* case, *supra,* had refrained from divesting themselves of life estates reserved prior to the Joint Resolution of 1931. The rationale of that resolution remained constant. S. Rep. No. 831, 81st Cong., 1st Sess. (1949).

A review of the cases has revealed four general methods by which life estates have been retained, and taxability imposed, under section 2036 *supra:*

I. Retention Apart from Any Legal Instrument

The principal case was the only one found in which there was clear and admitted evidence of an oral retention. Indeed, research has yielded only two other federal cases which merit inclusion under the heading. This dearth of pertinent cases is also indicated by the use, in the opinions of these three cases, either of citations to state cases decided under a similar statutory provision, or of citations to analogous federal cases.

In *Wells Fargo Bank & Union Trust Co. v. United States,* 80 F. Supp. 787 (N.D. Calif. 1948) and *Harter v. United States,* 55-1 U.S. Tax Cas. 55,397 (N.D. Okla. 1954) the retentions of life estates in the respective properties were not express. The decedents simply continued to enjoy their property by executing, but failing to deliver, the deeds of conveyance thereto; however, in the *Harter* case, *supra* the arguments of the decedent's executor were directly in point as was the answer of the District Court at p. 55,399:

> "The language of this section . . . does not contemplate, as taxpayer has contended, that the retained interest must be set out and provided for in the instrument of transfer . . . . Rather, [the section] poses a factual test. Under the clearly apparent facts in this case the decedent retained what amounted to a life interest in the property, and the property falls within his gross estate under the provisions. . . ."

II. Express Retention in the Instrument of Transfer

Pamelia D. Holland, 47 B.T.A. 807 (Oct. 6, 1942), *on reconsideration,* 1 T.C. 564 (Feb. 10, 1943), and *Greene v. United States,* 237 F.2d 848 (7th Cir. 1956) both involved the transfer of securities under which transfers the decedents retained a minimum income therefrom for life. The *Holland* case had an added ingredient—in addition to a minimum salary for life, decedent retained possessions of the securities and voting rights for her lifetime as "collateral." The language of the *Greene* case is indicative of the results: "The decisive issue is whether, looking to substance and not merely to form, the decedent had retained for her life the right to the income from the property transferred."

III. Express Retention in an Instrument Other Than the Instrument of Transfer

Typical of the few cases in this area was *George L. Shearer,* 17 T.C. 304 (Sept. 19, 1951). This involved a transfer of a farm by the decedent to a corporation. Decedent received a lease-back at nominal rent, under which lease he was to pay expenses and taxes. The transaction was vulnerable to taxation even though the lease was subject to cancellation by the corporation and the stock was donated to the decedent's children.

IV. Retention in Fact Through Instruments of Reciprocity

This technique involved the reciprocal trust device and was by far the most common method used in attempts to avoid the statute. In *Moreno's Estate v. Commissioner,* 260 F.2d 389 (8th Cir. 1958); *Orvis v. Higgins,* 180 F.2d 537 (2d Cir. 1950); and *Cole's Estate v. Commissioner,* 140 F.2d 636 (8th Cir. 1944), the fact situations were similar. *A* would create a trust naming *B* as life beneficiary with remainder to *B*'s heirs, and *B* would create a trust making *A* the life beneficiary with remainder to *A*'s heirs. Life estates were contained in the trust instruments, but not for the benefit of the respective settlors; nevertheless, the courts took cognizance of the fact that the reciprocity accomplished the same ends by technically different means, and the estates were taxed accordingly.

The point here was that the trusts were so regarded because, in order to ascertain the benefits enuring to *A*, reference had to be made to the trust created by *B* and vice versa. The court in the principal case skillfully employed the reciprocal trust decisions in refutation of petitioners arguments, and in support of its position, "That the reservation need not be expressed in the instrument of transfer. . . ."

The test applied and the decision reached by the court were in accord with the weight of authority as reflected in the variations on the central theme enumerated above. There is an abundance of cases concerning this problem and most of them, to a greater or lesser degree, display some semblance of finesse in their attempted avoidance or evasion. The petitioners in the principal case were fortunate to have a lawyer who had enough imagination to be able to provide some thought-provoking legal basis for their amazingly unsophisticated attempt to avoid the effects of section 2036 *supra.* Indeed, in light of his client's maneuvers, the points of counsel appear ingenuous. By the same token, his client's maneuvers, when viewed in light of the multifarious schemes which have been discussed here, seem pathetically naive. If the effects of the statute could be abrogated by a transaction as uncomplicated and candid as the one tried here, a significant area of revenue would be closed.

E. P. K.