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James C. Ervin Jr.
University of Michigan Law School

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COMMENTS

Loopholes and Ambiguities of Section 2036

The possibility of divergent tax treatment of economically similar situations has made section 2036 of the Internal Revenue Code[1] one of the most abused of the federal estate tax provisions. Originally enacted to ensure inclusion within the gross estate of the value of all property ostensibly transferred by the decedent prior to his death and yet beneficially enjoyed by him during his lifetime,[2] the section is being circumvented by an increasing number of tax avoidance patterns. Although some of the confusion can be traced to the erratic approach of the courts to cases involving section 2036,[3] the primary interpretive difficulty stems from Congress' failure to define precisely what it hoped to accomplish by the enactment of that section.[4] Under section 2036, the inter vivos gift of property in which the lifetime income is reserved for the transferor is clearly includible in the gross estate of the decedent-transferor. On the other hand, it is equally

1. INT. REV. CODE OF 1954, § 2036: TRANSFERS WITH RETAINED LIFE ESTATE.

(a) GENERAL RULE.—The value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death—

(1) the possession or enjoyment of, or the right to the income from, the property, or

(2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom.

(b) LIMITATIONS ON APPLICATION OF GENERAL RULE.—This section shall not apply to a transfer made before March 4, 1931; nor to a transfer made after March 3, 1931, and before June 7, 1932, unless the property transferred would have been includible in the decedent's gross estate by reason of the amendatory language of the joint resolution of March 3, 1931 (46 Stat. 1516).

2. See Treas. Reg. § 20.2036-1 (1960); 3 MERTENS, FEDERAL GIFT AND ESTATE TAXATION § 24.06 (Supp. 1965). It has been remarked, however, that the section was meant to be limited to a trust with a retained life estate. See Comment, *The Construction of Section 2036*, 60 MICH. L. REV. 631, 636-37 (1962). For a review of the history of section 2036 see, *e.g.*, BITTKER, FEDERAL INCOME, ESTATE AND GIFT TAXATION 1177-82 (3d ed. 1964); LOWNDES & KRAMER, FEDERAL ESTATE AND GIFT TAXES §§ 8.1-.5 (2d ed. 1962); 3 MERTENS, *op. cit. supra*, § 24.01 (Supp. 1965).

3. See Covey, *Section 2036—The New Problem Child of the Federal Estate Tax*, 4 TAX. COUNS. Q. 121 (1960); Comment, 60 MICH. L. REV. 631 (1962).

4. See 1 PAUL, FEDERAL ESTATE AND GIFT TAXATION § 7.01 (1942), where the author says:

> The estate tax provisions dealing with transfers intended to take effect at death and inter vivos trusts are probably the most esoteric provisions of the federal revenue laws. It requires the most painstaking analysis to make any headway in understanding them; even today, after many years and attempts at clarification, few would be bold enough to say they had mastered them. Bewildered administrative authorities and puzzled courts have added words to words, but little meaning emerges from the resulting thicket of obscurity.

Unfortunately, much of this statement remains true today. See BITTKER, *op. cit. supra* note 2, at 1177.

clear that the transferor may accomplish the same economic result, without subjecting the property to inclusion within his taxable estate by virtue of section 2036, simply by dividing his property and giving away an amount equal to the actuarial value of the remainder interest while retaining an amount equal to the actuarial value of the lifetime income. Taxation under section 2036 thus seems to turn on the form utilized by the decedent in dividing and transferring his property, rather than on the economic result. Unfortunately, most of the tax avoidance patterns fall within the gray area between the two forms of transfers mentioned above. A discussion of some of these patterns may serve to focus attention on the need for a review of the congressional purpose underlying section 2036 and for a possible statutory recasting of that section.

I. The "Tax Avoidance" Patterns

A. *The Insurance-Annuity Combination*

The insurance-annuity combination[5] furnishes a logical starting point, for this device most clearly illustrates the dichotomy between the taxable and the non-taxable forms of transfer. Under this plan, an individual purchases a life insurance policy and concurrently purchases a single premium, non-refundable annuity.[6] Although the annuity and insurance premiums are set at the normal rates, the size of the annuity is calculated so that in the event the annuitant-insured dies prematurely, the purchaser's "loss" from premature termination of the annuity payments is offset by the gain resulting from early realization of the full amount of the insurance policy.[7] The insured will have irrevocably assigned all of his rights in the insurance policy to a beneficiary or a trustee, while retaining for himself the annuity payments. In *Fidelity-Philadelphia Trust Co. v. Smith*,[8] the Supreme Court held that the value of the assigned policy was not within the transferor's estate under section 2036.[9] The Court viewed

5. See generally Friedman & Wheeler, *The Insurance-Annuity Combination in Estate Planning*, Prac. Law., Oct. 1959, p. 48.

6. The person is often aged, infirm, or for some other reason uninsurable, but there is no risk to the insurance company if the policies are purchased in combination.

7. For an extremely simplified example, assume that an individual with a life expectancy of 15 years has $1,000,000 from which he now receives an annual income of $35,000. He could purchase an annuity which would pay him $35,000 per year for the rest of his life at a cost of $400,000. He could, at the same time, purchase a single premium $1,000,000 life insurance policy at a cost of $600,000. In this way the insured-annuitant receives $35,000 per year which is equal to the annual interest of 3½% on $1,000,000 and on death, $1,000,000 is returned in the form of the life insurance payment. From the point of view of the insurance company, $400,000 is the amount necessary to produce $35,000 per year for 15 years assuming 3½% compound interest. Similarly, $600,000 is the present value of $1,000,000 due in 15 years also assuming a compound interest rate of 3½%. For purposes of simplification these figures have been rounded off and the insurance company's normal "load" factor has been ignored.

8. 356 U.S. 274 (1958), 56 Mich. L. Rev. 1366 (1958).

9. The Court resolved a conflict among several circuits. Conway v. Glenn, 193 F.2d

the annuity and life insurance as two separate and distinct policies, even though they were purchased in combination.[10] With this as the Court's point of departure, it was easy to find that the prerequisite for the application of section 2036—that a right be retained to income from the transferred property—had not been fulfilled, since the transferred property had been the insurance policy and the transferor's retained annual income was produced by the separate annuity policy.[11] The three justices who dissented in *Fidelity-Philadelphia Trust* thought that the majority had surrendered to a form over substance approach.[12] They believed that the insurance and annuity policies, when taken in combination, so closely resembled a transfer in trust with retained lifetime income that section 2036 should clearly have been applied. This conclusion is a realistic one, for when the several components are viewed as a single transaction, the insured has transferred a sum of money to the insurance company (which, according to this theory, stands in the place of a "trustee"), has retained a lifetime income, and has directed the "trustee" as to the disposition of the remainder at the death of the insured. However, it can be argued with equal facility that the insurance-annuity combination resembles perhaps even more closely another type of transfer which is at the tax-free end of the section 2036 taxable-nontaxable spectrum. The transferor could have purchased an annuity and then given a sum equal to the life insurance premium directly to the proposed beneficiary. If insurance is the primary goal, and if this intended beneficiary has an insurable interest in the life of the transferor, the beneficiary, using the sum received, could purchase the insurance policy himself. As an alternative, the beneficiary could invest the sum received, and at the death of the transferor, the amount of the principal plus the interest would perhaps equal or even surpass the insurance proceeds payable under the insurance-annuity combination. Neither of these alternatives would fall within section 2036, since in neither did the transferor retain a right to income from the transferred property. Thus, when viewed in light of these various alternatives, the majority opinion in *Fidelity-Philadelphia Trust Co.* does not seem to be as great a surrender to form over substance as the dissenting justices suggest.

Despite its high cost and relatively low investment yield, the

965 (6th Cir. 1952) and Burr v. Commissioner, 156 F.2d 871 (2d Cir.), *cert. denied*, 329 U.S. 785 (1946), held the proceeds includable. On the other hand, Bohnen v. Harrison, 199 F.2d 492 (7th Cir. 1952), *aff'd per curiam by equally divided court*, 345 U.S. 946 (1953), held for the taxpayer.

10. The transferee of the life insurance policy could, after all, turn in that policy for its cash surrender value without in any way affecting the right of the annuitant to receive his annual payments.

11. 356 U.S. at 280-81. After a seven-year wait, the Treasury acquiesced in the holding in *Fidelity-Philadelphia Trust*. See Rev. Rul. 69, 1965-1 CUM. BULL. 440.

12. 356 U.S. at 281 (dissenting opinion). See *The Supreme Court, 1957 Term*, 72 HARV. L. REV. 1366 (1958).

insurance-annuity combination has been considered by some writers as an important estate planning device.[13] However, the Treasury, although it acquiesced in the result of *Fidelity-Philadelphia Trust Co.*,[14] seems to view with suspicion any increased activity in the use of this combination and has recently attacked one of the combination's main features in Revenue Ruling 65-57.[15] This ruling provides that the proceeds of the life insurance part of the combination shall be treated as ordinary income to the recipient, although proceeds of life insurance in non-combination contexts are normally excluded from the recipient's gross income.[16] The Treasury's position was based on the holding in *Helvering v. LeGierse*[17] that the elimination of the risk of premature death in the calculation of the premiums for an insurance-annuity combination indicates that there is no actual "life insurance." Although this ruling has been subject to some criticism,[18] for the purposes of this discussion, it is significant to note that the Treasury, which has been unable to attack directly the insurance-annuity combination, has invoked the income tax sections of the Code in order to lessen the combination's desirability as an estate plan. Thus, it appears that if the insurance-annuity combination is to be subject to federal estate tax consequences, new legislation will be needed.[19] However, Congress will then need to decide to what extent it wishes to restrict the use of the currently tax-free

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13. The advantages of the insurance-annuity combination are spelled out in Friedman & Wheeler, *supra* note 5, at 64:

> The Insurance-Annuity Combination permits planning with precision. . . . [The insured-annuitant knows the amount by which his estate is reduced, the amount which his beneficiary will receive and the amount which he will receive each year;]
>
> The Insurance-Annuity Combination enables the donor to make a larger gift of insurance than he would otherwise make, because he will have the security afforded by the retained annuity.
>
> The Insurance-Annuity Combination is simple in its operation. . . .
>
> The Insurance-Annuity Combination is the only method by which an uninsurable person may obtain life insurance . . . .

See also Friedman & Wheeler, *Life Insurance Policies as the Subject of Gifts: Outright or in Trust*, N.Y.U. 22D INST. ON FED. TAX. 1323, 1335-36 (1964).

14. See note 11 *supra*.

15. Rev. Rul. 57, 1965-1 CUM. BULL. 56.

16. If paid by reason of the death of the insured, the proceeds of a life insurance contract are generally excluded from the gross income of the recipient. INT. REV. CODE OF 1954, § 101(a).

17. 312 U.S. 531 (1941).

18. See Schlesinger, *New Revenue Rulings on Annuity-Insurance Combinations Pose Fresh Tax Dangers*, 104 TRUSTS & ESTATES 344 (1965). Prior to Rev. Rul. 65-57, it had been assumed by some writers that the proceeds would be free from the income tax. See Friedman & Wheeler, *Life Insurance Policies as the Subject of Gifts: Outright or in Trust*, N.Y.U. 22D INST. ON FED. TAX. 1323, 1335 n.36 (1964); Friedman & Wheeler, *The Insurance-Annuity Combination in Estate Planning*, Prac. Law., Oct. 1959, pp. 53-54.

19. LOWNDES & KRAMER, *op. cit. supra* note 2, § 13.11, at 290: "[W]hen considered in relation to the overall backdrop of section 2036, it becomes apparent that the Court has given to insurance companies a device which, if effectively exploited, can virtually emasculate that section of the code." See Note, 56 MICH. L. REV. 1366, 1370 (1958).

alternatives and it must recognize that the insurance-annuity combination is only one phase of the problem.

B. *Joint Tenancy Transfers*

A second method which is used to avoid the consequences of section 2036 is the joint tenancy transfer. The implementation of this plan is somewhat more complex than the insurance-annuity combination and often requires the cooperation of a second party. Generally, a husband will purchase property in, or convert presently held property to, the name of his wife and himself as joint tenants. If the husband were to die immediately after such a purchase or conversion, section 2040[20] requires that, if the wife had not supplied any of the consideration for the property, the entire value of the jointly held property be included in his gross estate. However, prior to the husband's death, the couple may convey the jointly held property to their children, with each parent retaining a life estate in half of the property. Such a conveyance effects a severance of the jointly held property, and consequently takes it out of the scope of section 2040. In this context, the courts have held that at the husband's death, section 2036 requires that only one-half of the original property be included in his gross estate,[21] since the husband conveyed to his children only his interest in the property, which at the time of the conveyance was an undivided one-half interest, and he retained the life benefits only from the part conveyed.[22] A variation of this same tax-avoidance plan is that after a severance of the joint tenancy, either tenant could convey the actuarial equivalent of the remainder interest in the property, while retaining the equivalent of the lifetime income. This disposition, like the same disposition by the insurance-annuity transferor, would not result in any section 2036 consequences.

The significance of the joint-tenancy transfer becomes immediately apparent when its resulting tax consequences are compared with those which would have occurred had the husband and wife retained

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20. INT. REV. CODE OF 1954, § 2040.

21. See, *e.g.*, Glaser v. United States, 306 F.2d 57 (7th Cir. 1962); Heasty v. United States, 239 F. Supp. 345 (D. Kan. 1965). Other cases have held that a transfer of a joint tenancy interest in contemplation of death required the inclusion of only the one-half interest in the transferor's gross estate, even if the transferor had contributed the full consideration toward the acquisition of the jointly held property. See, *e.g.*, Sullivan's Estate v. Commissioner, 175 F.2d 657 (9th Cir. 1949); Estate of A. Carl Borner, 25 T.C. 584 (1955), *nonacq.*, 1962-1 CUM. BULL. 4; Estate of Brockway, 18 T.C. 488, 499 (1952), *aff'd on other grounds*, 219 F.2d 400 (9th Cir. 1954). See generally Wright, *Transfers of Joint Property in Contemplation of Death—A Call for Immediate Statutory Revision*, 55 MICH. L. REV. 1 (1956).

22. See Glaser v. United States, 306 F.2d 57, 60-61 (7th Cir. 1962); Heasty v. United States, 239 F. Supp. 345 (D. Kan. 1965). See generally Comment, *Problems of Estate and Gift Taxation of Joint Ownership Interests*, 10 U.C.L.A.L. REV. 1205 (1963).

the property as joint tenants until the husband's death. Section 2040 reflects a congressional policy decision that the owner of property should not be able to escape estate taxation merely by conveying the property to another and himself as joint tenants. It would seem initially that the tax-wary joint tenant should not be allowed to avoid the effect of section 2040 simply by conveying, with his wife's cooperation, the jointly held property to their children while retaining life estates. However, joint tenancies are severable by the unilateral action of either party,[23] and it would seem to be very harsh to include the value of the entire property in an individual's estate if he had conveyed his half of the property to his children, retaining a life estate, after an *involuntary* severance.[24] Furthermore, the utility of the joint tenancy transfer as an estate plan is somewhat doubtful, particularly since the same economic result could be obtained by the creation of a tenancy in common or by an outright gift of one-half of the property by the husband to the wife, either of which dispositions of the property would avoid any section 2040 difficulties.

C. *Non-Retention Transfers*

Another pattern, several variations of which have enjoyed recent popularity, may be labeled the "non-retention" plans. Section 2036 provides that the transferred property is to be included in the decedent's gross estate only if he retains either the "possession or enjoyment of, or the right to income from, the transferred property."[25] In an illustrative case,[26] decedent had transferred nearly all of her property to her sister, who in turn promised to care for the decedent for the rest of her life. The Commissioner, analogizing the transaction to a transfer to a trust with income retained for life, included the value of the transferred property in the decedent's gross estate. The analogy failed, however, because of the transferee-sister's unfettered ability to dispose of the transferred property as she saw fit. The court drew a distinction between a transfer with retained enjoyment of the property transferred, and a transfer in exchange for services which may, but *need not necessarily*, be financed by the transferred property.[27] Another instance in which a court adhered to this distinction involved a trust, the corpus of which was to provide, upon liquidation, the funds to purchase $10,000 annuities for its beneficiaries.[28] Prior to the liquidation and purchase of the annuities, the beneficiaries were to receive annual payments from the trust equal to the proposed

23. See Polasky, *Current Tax Developments Including Joint Tenancy and Widow's Election*, 103 TRUSTS & ESTATES 253, 254-55 (1964).

24. It should be noted that in the case of tenancy by the entirety, no severance is possible without the concurrence of both parties. Polasky, *supra* note 23, at 254.

25. See statute quoted note 1 *supra*.

26. Estate of Sarah A. Bergan, 1 T.C. 543 (1943).

27. *Id.* at 552.

28. Becklenberg's Estate v. Commissioner, 273 F.2d 297 (7th Cir. 1959).

annuity proceeds. When a contributor of property to the trust, who was also a beneficiary, died before the annuities were purchased, the Commissioner argued that her contribution to the corpus should be included in her gross estate because the annual payments she had received from the trust amounted to a retention of the right to income from the transferred property.[29] The court, rejecting this contention, pointed out that she had simply purchased a contract pursuant to which the trust was to pay her $10,000 a year and that her right to the annual payments was not limited to the property transferred by her or the income therefrom.[30]

Another popular "non-retention" plan involves a husband, who owns his home and who transfers title in the home to his wife, ostensibly in fee with no strings attached, and a wife who very graciously allows her husband to continue to live in the house once she has title. This would seem to be the classic case for illustrating the "enjoyment or possession" language of section 2036, for the legislative history of that section indicates that Congress included the words "possession or enjoyment" in addition to the words "right to income" for the primary purpose of bringing such non-income producing property as a family home within the section.[31] Nevertheless, the courts have consistently demanded proof of at least an implied agreement between the husband and wife before they will say that the husband has "retained" enjoyment or possession so as to require the inclusion of the value of the house in his gross estate.[32] Although some courts are less reluctant than others to imply an agreement in this situation,[33] there is still the possibility of a substantial premium to those husbands who, because of their particularly harmonious marital relationships, are assured that they will be able to continue to enjoy the transferred property without having to extract an agreement from their transferee-wives.[34] What the courts fail to consider, however, is that section 2036 does not require that the transferor retain a *legal* right to the possession or enjoyment of the transferred

29. The applicable section was INT. REV. CODE OF 1939, § 811(c), 53 Stat. 120, the predecessor of INT. REV. CODE OF 1954, § 2036.

30. 273 F.2d at 301. Some of the payments to decedent had been made from the corpus of the trust. *Ibid.* The reasoning of the *Becklenberg* court has been criticized in Covey, *supra* note 3, at 132-37.

31. See H.R. REP. No. 1412, 81st Cong., 1st Sess. 5 (1949); Covey, *supra* note 3, at 129-30.

32. See, *e.g.*, Stephenson v. United States, 238 F. Supp. 660 (W.D. Va. 1965); Union Planters Nat'l Bank v. United States, 238 F. Supp. 883 (W.D. Tenn. 1964), which cite and rely on Markovits, *The Fate of Inter Vivos Transfers Under Internal Revenue Code Section 2036*, 7 TAX COUNS. Q. 395 (1963). See also Clark v. United States, 209 F. Supp. 895 (D. Colo. 1962).

33. An implied contract was found in Estate of Skinner v. United States, 316 F.2d 517, 520 (3d Cir. 1963); Peck v. United States, 16 Am. Fed. Tax R.2d 6125 (M.D. Ga. 1965).

34. A more difficult situation might be presented if the husband transferred the money to his wife and the wife subsequently used the money to purchase the house in her name.

property. It has been held, for example, that section 2036 was applicable when transferees gave the dividend income from transferred securities to their transferor-father, even though the father did not have a legal right to the dividends since the transferees' obligations to give the dividends to their father were pursuant to an oral and unenforceable agreement.[35] The foregoing suggests that Congress, in making any revision in section 2036, should make clear its intention that transferred property be considered part of the transferor's gross estate for estate tax purposes when the transferor does *in fact* retain the benefit of the property which he has ostensibly transferred completely.

D. *Inter Vivos Transfers of Retained Life Estates*

Another procedure by which it is possible to avoid the effect of section 2036 is by transferring property with a reserved life estate, and subsequently making an inter vivos transfer of the retained estate.[36] However, the now famous case of *United States v. Allen*[37] indicates that there may be some danger in attempting to avoid estate taxation in this manner. In *Allen,* decedent had established an irrevocable trust, reserving a portion of the income to herself for life. Upon being informed that the retention of the life estate would cause the corpus of the trust to be included in her estate, she sold the life estate to her son for a price slightly in excess of its actuarial value. She died a short time later, and the Tenth Circuit Court of Appeals held that since the life estate was transferred without full consideration and in contemplation of death, it was not an effective transfer of the decedent's retained interest in the corpus of the trust, so that section 2036 required the inclusion of the corpus in the decedent's gross estate.[38] With respect to the question of adequate consideration, the court made the rather surprising pronouncement that the fair market value of the life estate was not sufficient consideration for a transfer of this kind; indeed, in order to remove the transferred property from the consequences of section 2036, the court stated that the consideration must equal the commuted value of both the life estate *and* the remainder.[39] Since the court was willing to concede that it was ridiculous to expect that anyone would ever pay this amount, its statement

35. Estate of McNichol v. Commissioner, 265 F.2d 667 (3d Cir. 1959); see Covey, *supra* note 3, at 131.

36. However, it seems that the Treasury may argue that a transfer of the retained life estate for its then value is an "anticipatory realization of income from the life estate." See Polasky, *Current Tax Developments Including Joint Tenancy and Widow's Election,* 103 TRUSTS & ESTATES 253 (1964).

37. 293 F.2d 916 (10th Cir. 1961). See Lowndes & Stephens, *Identification of Property Subject to the Federal Estate Tax,* 65 MICH. L. REV. 105, 120-25 (1966).

38. 293 F.2d at 918. Since the decedent died prior to the adoption of the 1954 Internal Revenue Code, the applicable statutory provision was INT. REV. CODE OF 1939, § 811, 53 Stat. 120.

39. 293 F.2d at 918. This rationale has been criticized in Zissman, *Problem Areas in the Estate Tax,* 41 TAXES 875 (1963).

suggests that it will be difficult if not impossible, for an individual to escape the consequences of section 2036 by selling a life estate which he has purposely or unwittingly retained under a previous transfer.[40] The concurring judge in *Allen* went so far as to state:

> As I read [section 2036] the tax liability arises at the time of the inter vivos transfer under which there was a retention of the right to income for life. The disposition thereafter of that retained right does not eliminate the taxability.[41]

The result in *Allen,* however, is practically mandatory if section 2036 is to be preserved, at least in its present form. If a contrary result had been reached, every life estate retained in a previous transfer would be transferred by its holder on his death-bed, for its value at that time, with the result that only the then nominal value of the life estate would be pulled back into the donor's estate under the provision of the Code which treats gifts in contemplation of death.[42]

II. CONSIDERATIONS IN FORMULATING A VIABLE REPLACEMENT

It is admittedly far easier to condemn than to correct. Any reevaluation of the congressional position on the taxation of estates will necessarily involve numerous factors and should reach beyond the mere correction of section 2036.[43] The initial step is to determine the function which the Congress expects the estate tax to serve in the tax system; such a determination will play an integral role in deciding the scope of possible revision.

A. *The Elimination of the Estate Tax*

The estate tax is essentially a device of social control;[44] its primary aim is to make the accumulation of huge family fortunes more difficult. The revenue it produces is relatively small,[45] which would

40. 293 F.2d at 917; see Brown, *The Allen Case and the Widow's Election,* 36 SO. CAL. L. REV. 229, 236 (1963).

41. 293 F.2d at 918 (concurring opinion). Fortunately, this view has not been adopted. However, the literal language of the statute does firmly support this position. See LOWNDES & KRAMER, FEDERAL ESTATE AND GIFT TAXES § 8.13 (2d ed. 1962).

42. INT. REV. CODE OF 1954, § 2035.

43. The fact that § 2036 overlaps with other federal estate tax provisions has also contributed to the confusion surrounding the section. For example, it has been argued that § 2037 would cover nearly all of the cases which fall within § 2036. ALI, FEDERAL INCOME, ESTATE AND GIFT TAX STATUTE 177 (Tent. Draft No. 10, 1955); see Lowndes & Stephens, *Identification of Property Subject to the Federal Estate Tax,* 65 MICH. L. REV. 105, 112-13 (1966). Some of the powers which are treated under § 2038 may also come within the language of § 2036 although the two sections provide different tax consequences. Such inconsistent treatment has no place in estate taxation. See LEWIS, THE ESTATE TAX 63-66 (1960); LOWNDES & KRAMER, FEDERAL ESTATE AND GIFT TAXES § 9.14 (2d ed. 1962); Pedrick, *Grantor Powers and Estate Taxation: The Ties That Bind,* 54 NW. U.L. REV. 527, 545 (1959).

44. See Lowndes, *Common Sense Correlation of the Estate and Gift Taxes,* 17 U. FLA. L. REV. 507, 508 (1965).

45. See WARREN & SURREY, FEDERAL ESTATE AND GIFT TAXATION 10 (1961 ed.), where it is indicated that these taxes produce about 2% of the federal tax revenues.

indicate that if the estate tax were eliminated, the decrease in revenue could be off-set by the other revenue producing sections of the Code. There is, however, little indication that the Congress would take steps which would drastically modify the estate tax. Thus, possible changes, if any, will probably be aimed at correcting existing "loopholes."

B. *Retention of the Estate Tax—Corrective Considerations*

If the trend of the past few years is indicative of future activity, the major thrust of changes in the estate tax provisions of the Code will not be limited to one or two sections alone. Rather, by means of a sweeping overhaul of the federal tax system,[46] such as the recently proposed Unified Transfer Tax,[47] draftsmen will seek to establish a heretofore non-existent correlation among the gift and estate tax, and possibly even the income tax, sections of the Code.[48] If the purpose of section 2036 is to be preserved in such a revision, a careful consideration of the wording of that section will be necessary.

Section 2036, as presently worded, imposes estate tax consequences on one form of transfer, whereas a second form, which in most cases accomplishes the same economic result, is not affected. The drafters of new estate tax legislation must recognize that a given amount of property is capable of being divided in many ways, both legally and physically. At the present time, section 2036 affects only the legal division of property into a life estate and a remainder; the wording does not cover the physical division of the same property into the actuarial equivalent of a life estate and the actuarial equivalent of a remainder. Unless there are policy reasons for distinguishing between these types of divisions, a difference in tax treatment is not justified where the economic result is essentially the same.

James C. Ervin, Jr.

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46. Perhaps the impetus for such a sweeping change was provided by the admonition:

> We have been like Englishmen who never clean their slates; no language could be thrown away if anyone thought in optimistic vein that he understood its meaning. Amendments consisted of addition, duplication and overlapping. No one suggested the heroic remedy of fresh language which would clear away the debris and say simply what was plainly dictated by disillusioning experience with a statute that had repeatedly failed to say what the Treasury, at least, thought it meant. It was easier to repair at damaged points in a makeshift way, always hoping for a dim best. Some day we shall learn that sound revenue laws are not made in such a piecemeal way, and that postponing such important problems may be an expensive luxury.

1 PAUL, FEDERAL ESTATE AND GIFT TAXATION § 7.01 (1942).

47. ALI, FEDERAL ESTATE AND GIFT TAX PROJECT (Study Draft No. 1, 1965).

48. See Lowndes, *Common Sense Correlation of Gift and Estate Tax*, 17 U. FLA. L. REV. 507, 507-12 (1965) (offering an alternative correlation, insofar as § 2036 would be affected, at 518-20); ALI FED. INCOME, ESTATE & GIFT TAX STAT. (Tent. Draft Nos. 9, 1954; 10, 1955).