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Federal Estate Taxation -- Revenue Ruling 67-463 Has Been Dealt A Grave Injustice

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in a position whereby he has any powers over insurance polices on his life capable of being exercised for his own benefit. Thus, in order to avoid the *Fruehauf* tax trap the estate planner must provide for two trusts—one containing only the insurance policies, over which the surviving spouse should have no powers in the nature of "incidents of ownership;"[81] the other containing noninsurance assets, over which the surviving spouse may safely act as trustee. Additionally, *Fruehauf* indicates that should the surviving spouse act as executor, he must be expressly prohibited from exercising any powers in the nature of "incidents of ownership" over insurance policies on his life owned by his spouse, if these policies are to ultimately become a part of a *Fruehauf* trust. Until this area is resolved, this is the only safe course of estate planning to take when faced with life insurance trusts.

THOMAS R. CRAWFORD

Federal Estate Taxation—Revenue Ruling 67-463 Has Been Dealt A Grave Injustice

As the smoke clears from the aftermath of the decision of *First National Bank (of Midland) v. United States*,[1] we find that the Commissioner of the Internal Revenue Service has once again met defeat. The score now stands: taxpayers, three, the Commissioner and Revenue Ruling 67-463, zero.[2] Completely realizing the possible adverse consequences to taxpayers and estate tax planners, it will be shown, nevertheless, that the Commissioner has been dealt a grave injustice.

Several years ago the Commissioner decided to review the estate tax consequences of gifts of life insurance in situations where the deceased-insured paid part of the premiums in contemplation of death, but had given away all incidents of ownership in the policy more than three years prior to death.[3] To determine the amount to be included in the decedent's gross estate the Commissioner issued Revenue Ruling 67-463:

[81] In fact, the surviving spouse should never be designated as trustee over the insurance trust since many states have provisions providing that a trustee has certain broad powers, such as the power to sell, even though not specifically granted by the trust instrument.

[1] 423 F.2d 1286 (5th Cir. 1970).

[2] Rev. Rul. 67-463, 1967-2 CUM. BULL. 327.

[3] For example, decedent took out a fifty thousand dollar face amount policy on his life six years before death. He paid all six thousand dollars of the premiums (one thousand dollars annually), with one-half (three thousand dollars) of the

> A decedent, within three years of death and in contemplation of death, paid the premiums on a policy of insurance on his life. He had transferred the incidents of ownership in the policy to his wife more than three years prior to his death. *Held*, such payment was a transfer of an interest in the policy measured by the proportion the amount of premiums so paid bears to the amount of premiums paid. Accordingly, the value of the proportionate part of the amount receivable as insurance that is attributable to those premiums paid by the decedent within three years of death is includable in his gross estate under section 2035 of the Internal Revenue Code of 1954. This conclusion is also applicable where the wife originally applied for the insurance.[4]

The Commissioner's first setback with regard to Revenue Ruling 67-463 came in 1968 in *Gorman v. United States*,[5] in which the life insurance company issued a policy on the decedent's life that designated his wife as beneficiary and owner of all rights and privileges.[6] In procuring the insurance, the insured had requested that the policy be so written. The policy was issued, and the insured paid the first and, as it turned out, the only premium. Less than one year later the decedent-insured died. The district director of the Internal Revenue Service sought to include the proceeds of the policy in decedent's gross estate,[7] arguing that the decedent's procurement of the policy or his payment of the premiums amounted to a gift in contemplation of death within the meaning of section 2035 of the Internal Revenue Code.[8] Plaintiff, decedent's wife and

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premiums being paid within three years of his death. When he took out the policy initially, he immediately transferred all the incidents of ownership to the beneficiaries. It is conceded that the last three premium payments were made in contemplation of death.

[4] Rev. Rul. 67-463. Under this revenue ruling, in the example set forth in note 3 *supra*, the inclusion would be twenty-five thousand dollars because one-half of the premims were paid in contemplation, and one-half of the face amount equals twenty-five thousand dollars. Under the ruling the same result would be reached even if the beneficiaries or donees originally applied for the policy on the life of the decedent.

[5] 288 F. Supp. 225 (E.D. Mich. 1968).

[6] *Id.* at 236.

[7] *Id.* at 234-35.

[8] INT. REV. CODE of 1954, § 2035, states:

(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, in contemplation of his death.

(b) APPLICATION OF GENERAL RULE.—If the decedent within a period of 3 years ending with the date of his death (except in case of a bona fide sale for an adequate and full consideration in money or money's worth) transferred an interest executrix under his will, paid the tax and sued for refund. The district court held that the premium was paid in contemplation of death but that the amount to be included in the decedent's gross estate was only the actual cash premium paid and not the pro rata amount of the proceeds.[9]

In December of 1968, the Commissoner temporarily found reason to rejoice. In *First National Bank (of Midland) v. United States*,[10] also a refund suit, the United States District Court upheld Revenue Ruling 67-463.[11] In this case the decedent and his wife purchased two life insurance policies on decedent's life, one for each of their daughters. The daughters were named as the owners of the policy and held all the incidents of ownership in their respective policies. The premium payments, including three in contemplation of death,[12] were made with community property funds. A portion of the proceeds of the two policies were included in the decedent's gross estate under section 2035. The court did not discuss prior case law or legislative history but merely cited Revenue Ruling 67-463 as the basis for its decision.[13] The Commissioner's apparent victory was swept aside when the fifth circuit reversed the district court on March 23, 1970.[14] The court of appeals relied on the *Gorman* case and *Estate of Coleman*[15] discussed below.

The Tax Court was faced with this issue for the first time in 1969. A full court review dealt the Commissioner another defeat. In *Coleman* the decedent's three children purchased, as record owners and beneficiaries, an insurance policy on the decedent's life. The decedent had paid all the premiums, and it was admitted that several premiums were paid in contemplation of death. The government contended that the amount to be included in the gross estate was "that part of the total proceeds which bears

in property, relinquished a power, or exercised or released a general power of appointment, such transfer, relinquishment, exercise, or release shall, unless shown to the contrary, be deemed to have been made in contemplation of death within the meaning of this section and sections 2038 and 2041 (relating to revocable transfers and powers of appointment); but no such transfer, relinquishment, exercise, or release made before such 3-year period shall be treated as having been made in contemplation of death.

The purpose of section 2035 is to reach substitutes for testamentary dispositions and thus prevent evasion of the estate tax.

[9] 288 F. Supp. at 234.

[10] 69-1 U.S. Tax. Cas. ¶ 12,574 (W.D. Tex. Dec. 11, 1968).

[11] *Id.* ¶ 12,574, at 84,831.

[12] *Id.* The plaintiffs made no effort to disavow the presumption that the premiums were made in contemplation of death.

[13] *Id.*

[14] 423 F.2d 1286 (5th Cir. 1970).

[15] 52 T.C. 921 (1969).

the same proportion to the total proceeds as the premiums paid in contemplation of death bear to the total premiums paid."[16] The court held that the amount includable in the gross estate was limited to the premiums paid in contemplation of death.[17]

Even though the Commissioner has lost three cases, he has not and probably will not concede defeat at the moment because the opinions in the three decided cases have been far from convincing and well-reasoned. In *Gorman* the court began its attack on the Commissioner's position by relating the legislative history of section 2042.[18] The court reasoned that the deletion of the "premium payment test" in section 2042 indicated a congressional intent to prohibit any inclusion of policy proceeds in an insured's estate based on the insured's payment of premiums.[19] The court decided that to allow the IRS to use a premium-based test to include part of the proceeds of life insurance—even in valuing a transfer in contemplation of death under section 2035—would effectively defeat the congressional policy evidenced by the changes in section 2042.[20] The court felt that Revenue Ruling 67-463 was an administrative attempt to adopt in part the premium payment test, which was deleted from the revenue laws by the enactment of the 1954 Code.[21]

In so reasoning the court seems to have adopted an unnecessarily broad interpretation of the 1954 changes. Congress rejected the "payment of premiums" test as too harsh a basis for inclusion of insurance proceeds in the taxable estate under section 2042 but gave no indication that it intended to make payments of premiums irrelevant to taxation under other sections of the federal estate tax.[22] The majority of the House Ways and Means Committee indicated that "payment of premiums is no longer a factor in determining the tax liability *under this section* (section 2042) of insurance proceeds."[23] Thus the court failed to distinguish between "payment of premiums" as an independent basis for inclusion under section 2042, a basis that had been deleted from the Code in 1954, and the payment of a premium as a transfer made in contemplation of death

[16] *Id.* at 922. The government relied on Rev. Rul. 67-463.
[17] *Id.* at 924.
[18] 288 F. Supp. at 227-28. *See* INT. REV. CODE of 1954, § 2042. This section deals with the rules governing the includibility of proceeds of life insurance when the insured retains "incidents of ownership."
[19] 288 F. Supp. at 227-28.
[20] *Id.*
[21] *Id.* at 227.
[22] *See* H.R. REP. No. 1337, 83d Cong., 2d Sess. A316-17 (1954).
[23] *Id.* at A316 (emphasis added).

under section 2035.[24] It must be re-emphasized that in *Gorman*, as well as in *First National Bank (of Midland)* and *Coleman*, the courts were concerned only with a section 2035 inclusion and not with a section 2042.[25]

The next problem in the *Gorman* decision concerns the court's view as to what constitutes a "transfer" under section 2035.[26] The court stated that

> [t]he specific interpretative issue is what is the value of the property transferred by the decedent . . . when he pays in contemplation of death directly or indirectly premiums on a life insurance policy.[27]

The court decided that once it has been determined that an interest in property has been transferred in contemplation of death, the amount included in decedent's gross estate is the value of the interest transferred as of the applicable valuation date.[28] The court stated that "our focus must at all times be directed to what was in fact transferred by the decedent when he paid a premium in contemplation of death."[29] The court then relied on the "specific asset theory"[30] and decided that if anything were to be included in the gross estate, "it should be limited to the value of the asset transferred, namely the premium."[31] Thus the court in *Gorman* failed to come to grips with the issue to what constitutes a "transfer."

The government asserted that the procurement of the insurance policy by the decedent for his wife was a "transfer" of the policy within the meaning of section 2035[32] and that the total proceeds from the policy, as a result of payment of the premium, is includable in the estate of the decedent. The government cites *Chase National Bank v. United States*[33]

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[24] The government argued that the conclusion reached by the ruling is actually consistent with the intent of Congress in dropping the premium payment test from the code because it places life insurance on an equal footing with other property.

[25] *See* INT. REV. CODE of 1954, § 2042; Treas. Reg. § 20-2042 (1954).

[26] 288 F. Supp. at 228.

[27] *Id.*

[28] *Id. See* Treas. Reg. § 20-2035-1(e), T.D. 6501.

[29] 288 F. Supp. at 230-31. The court's discussion fails to shed light on the problem.

[30] *Id.* at 233.

[31] *Id.*

[32] *Id.* at 226.

[33] 278 U.S. 327 (1929). The decedent purchased three policies payable to his wife as beneficiary. He reserved the right to change the beneficiary and to surrender the policies. After his death, his executor contended that there was no transfer because the proceeds did not come directly from the decedent but instead came from the insurer. The Supreme Court refused to accept this distinction and reasoned that because of his retained rights, the decedent until his death retained a legal interest in the policy, which effectively gave him a power of disposition over the proceeds. The Court concluded that the termination of such power was

in support of its view. The government contended that even though ownership in the policy was created in the wife, the transaction itself was really a transfer by the decedent of those rights since he was the one who provided the consideration or motivating force for the transaction. The insured was the master of his offer and the transferor of the policy when he made application to the insurance company and decided to have the company's "bargained for promise" run to his wife.[34] This position is appealing since the law should not distinguish between the situation where *A* pays *B* to give something to *C* and the situation where *A* purchases the thing and makes a gift of it to *C*.[35] The court in *Gorman*, however, dismissed the argument by noting that the Supreme Court in *Chase* never considered the relationship of premiums to proceeds.[36] In so doing, the court simply avoided the fact that the procurement of the policy itself may have been a transfer in contemplation of death. Inclusion of a gift under section 2035 should not be affected by the fact that, at the time of the transfer, the decedent immediately and absolutely parted with the enjoyment of or title to the property.[37] As stated in *United States v. Wells*:[38]

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a constitutionally taxable transfer and need not have been preceded directly by a transfer from the decedent to the recipient of his bounty. It thought the word "transfer" should not be restricted to direct transfers, but should "at least include the transfer of property procured through expenditures by the decedent with purpose, effected at his death, of having it pass to another." *Id.* at 337.

[34] *See* Simmons, *District Court invalidates IRS' three-year premium payment rule*, 29 J. TAX. 338, 339 (1968).

[35] *See generally* Note, *Inclusion of Insurance Proceeds Because of the Decedent's Continuous Premium Payment—The Continued Validity of Revenue Ruling 67-463*, 64 NW. U.L. REV. 116 (1969). Under section 2035 if *A* transfers one hundred dollars in cash to *B* in contemplation of death only one hundred dollars will be included in *A*'s gross estate. However, if *A* transfers a piece of real property in contemplation with a fair market value of one hundred dollars, and when *A* dies the property has a fair market value (FMV) of one thousand dollars, one thousand dollars is included in *A*'s gross estate. What if *A*, in contemplation of death, gives *X* one hundred dollars and tells him to buy a *certain* piece of real property and give it to *B*. If this piece of property has FMV of one thousand dollars when *A* dies, surely no one would doubt that the amount to be included should be one thousand dollars. This same type of analysis should be applied in the life insurance situation being discussed. *See* 1967-2 CUM. BULL. 327, 328, which states that:

> [A] premium payment under a contract of life insurance by other than the owner of the policy is analogous to a gift of specific property by the donor to the owner. Unlike the unrestricted gift of money a premium payment is a gift of insurance protection, a transfer of an interest in the policy which is transmuted at death into the proceeds of the policy.

[36] 288 F. Supp. at 228.

[37] Treas. Reg. § 20.2035-1(a), T.D. 6501.

[38] 283 U.S. 102 (1931).

> [t]he quality which brings the transfer within the statute is indicated by the context and manifest purpose. Transfers in contemplation of death are included within the same category . . . with transfers intended to take effect at or after the death of the transferor. The dominant purpose is to reach substitutes for testamentary dispositions and thus to prevent evasion of the estate tax.[39]

Thus, the *Chase* notion is that the decedent need not transmit property directly to the recipient to be viewed as the "transferor" within the meaning of section 2035. The actions of the insured in *Gorman* could well be viewed as equivalent to a "transfer" of the policy. Certainly, the transaction in *Gorman* is not functionally distinguishable from a situation where the policy was originally issued in the decedent's own name and then transferred to the wife immediately.[40] It should be remembered that while the insurer created the policy rights solely in the decedent's wife, it did so only at decedent's request and because of the consideration supplied by him.

Furthermore, the court in *Gorman* did not adequately consider whether, by paying the premiums, the decedent made a transfer of a pro rata share of the proceeds to his wife. To advance this view, the government relied on *Liebmann v. Hassett*.[41] The court, however, distinguished *Liebmann* (and thereby evaded the issue) by saying:

> *Liebmann* . . . is not authority for the proposition that payment of premiums transfer an interest in an insurance policy in the absence of a provision such as section 302(g) . . . As clearly indicated . . . the court relied on section 302(g) . . . to equate the payment of premiums by the decedent's wife to an addition or improvement made by her to the

[39] *Id.* at 116-17.

[40] *See* Note, *Inheritance and Estate Taxes—Insurance Policies—Premiums Paid in Contemplation of Death Held Taxable to the Estate of the Insured Only to the Extent of the Amount Paid*, 82 HARV. L. REV. 1765, 1767 (1969); Note, *Federal Taxation—Section 2035, Internal Revenue Code of 1954—Life Insurance Proceeds—Revenue Rule 67-463*, 43 TUL. L. REV. 882, 892-93 (1969).

[41] 148 F.2d 247 (1st Cir. 1945). The decedent transferred a life insurance policy to his wife in December, 1935, and died in October, 1937. After the transfer, the wife paid the two annual premiums. The wife stipulated that the policy was transferred in contemplation of death. The court decided that the interest transferred was to be valued at the date of death. To determine the value, the court turned to section 302g (INT. REV. CODE of 1926, § 302(g)) which made life insurance payable to the named beneficiary includible to the extent that it was "taken out" by the decedent. The court excluded that part of the proceeds which were "purchased" by the last two premiums paid by the wife.

property transferred in an amount equal to a pro rata amount of the proceeds.[42]

Thus, the court in *Gorman* concluded that it was only the existence of section 302(g) that resulted in its conclusion that there was a transfer of a pro rata share of the proceeds.[43] Since the court found no necessary relationship between the payment of premiums and the proceeds of the policy, it was unable to see how the decedent could be characterized as the motivating force behind the proceeds payment. The court concluded that any and all rights to the proceeds came from the contract with the insured, not from the payment of premiums.[44] The court has failed to look through form to substance.

In essence, the court in *Gorman* held that the payment of premiums by a nonowner of a policy was not in any sense a transfer of an interest in the policy or any of the contractual rights of that policy. Since in the court's view only a transfer of these contractual rights would dictate the inclusion of the proceeds of the policy in the gross estate, only the amount of the premium was so included. "This analysis has the apparent virtue of turning upon a transfer that was actually made: the husband's payment of the premium."[45] However, the court's analysis would seem to be correct only if the premium payment were to be valued at the time of transfer rather than at the insured's death. With the exception of cash transfers,[46] property transferred in contemplation of death is valued as of the date of the transferor's death and not at the time of the transfer.[47] Since other transfers, such as those of stocks and real property, are valued in the taxable estate at the time of the donor's death, consistency dictates that insurance be similarly treated.[48]

As indicated, the problem is how to value a premium when the valuation is made at the time of the insured's death and the beneficiary has become entitled to the proceeds of the policy. The valuation favored by the court in *Gorman* is incorrect. The premiums are the consideration furnished for the insurance company's promise to pay the proceeds at the donor's death. When the donor pays the premium, he is not merely giving the

[42] 288 F. Supp. at 229-30. *Cf.* Treas. Reg. § 20.2035-1(e), T.D. 6501.
[43] 288 F. Supp. at 229-30.
[44] *Id.*
[45] Note, 82 HARV. L. REV., *supra* note 40, at 1768.
[46] *Cf.* Humphrey's Estate v. Commissioner, 162 F.2d 1 (5th Cir. 1947).
[47] *See* Treas. Reg. § 20.2035-1(e), T.D. 6501.
[48] See generally Note, 82 HARV. L. REV., *supra* note 40.

amount of the premium; his purpose is to insure that the contractual benefits will be received by the beneficiary. Revenue Ruling 67-463 more clearly reflects the values that were actually transferred. This ruling does not re-establish the old payment of premiums inclusion as only the values transferred in the three years preceding the insured's death can be included in the estate under section 2035. Thus, if the insured had paid no premium and had no interest within the three years, none of the proceeds of the policy could be included in the taxable estate.

The court of appeals in *First National Bank (of Midland)* failed to shed any light on the controversy, and simply relied on *Gorman* and *Coleman* to reach its decision. The court stated that "[w]e are not dealing with a case in which the policy itself was transferred."[49] As pointed out earlier and re-emphasized in the discussion below in *Coleman*, this is a dubious distinction.[50] The court rejected the government's claim that payment of life insurance premiums by decedent on policies owned by his daughters, transferred "insurance benefits" to them for federal estate tax purposes. The government acknowledged that the value of the decedent's payments *at the time they were made* was their dollar value; however, the government explained that the "property or interest in property" actually transferred to the daughters through the agency of the insurance company, was not the cash amount of premium payments, but a "bundle of rights" under the insurance contract. The government concluded that the decedent made a transfer of rights in the same way that a purchaser of real property in the daughters' names would transfer the property to them rather than the consideration paid for it.[51] The daughters therefore received insurance benefits, not cash, and the payment of the premiums produced the proceeds. The court, relying on *Gorman* and *Coleman*, rejected the government's argument.[52] The government's argument in *Gorman* and *Coleman* are equally applicable to the *First National Bank (of Midland)* decision.

The majority opinion in *Coleman* displays on its face the weaknesses of its arguments. The court stated:

> Section 2035, by its terms, applies only to a "transfer" of an interest in property by a decedent. In Rev. Rul. 67-463, 1967-2 C.B. 327,

[49] 423 F.2d at 1287.
[50] See examples in note 35 *supra*.
[51] 423 F.2d at 1287-88.
[52] *Id.* at 1288.

> respondent decreed that the mere payment of premiums operated as a transfer of an interest in the proceeds of insurance—in this case, by the decedent to the children. We disagree.
>
> If the decedent had purchased a life insurance policy, initially retaining the ownership in herself, and thereafter assigned it to her children, there clearly would have been a "transfer" of an interest in the policy.[53]

In essence the majority holds that if the insured takes out an insurance policy on his own life, then transfers it to the beneficiary and continues to pay all the premiums, this is a transfer. But, if the beneficiary/owner takes out the policy initially on the insured (as in *Coleman*), even though the insured procures the policy—negotiates for the policy, takes the medical exams, pays the premium— this is a different situation and therefore not a transfer. The court makes one factual element— who first took out the policy—the crucial factor as to whether there is a transfer.[54] Obviously, the majority does not come to grips with the Commissioner's argument for inclusion of a proportionate part of the proceeds. Instead, the majority makes matters hinge upon pure formalism, a matter of no meaningful substance to wit: Did decedent, after taking the medical exam and paying the first premium, have the policy run to her and then at once transfer it to her children; or, did decedent, after taking the medical exam and paying the first premium, have the insurance agent draw the policy with it running directly to her children? Surely, there should be no substantive difference in the two situations.

In *Chase*, relied on by the Commissioner, the court gave the proper interpretation and scope to the term "transfer."

> Obviously, the word "transfer" in the statute, or the privilege which may constitutionally be taxed, cannot be taken in such a restricted sense as to refer only to the passing of particular items of property directly from the decedent to the transferee. It must, we think, at least include the transfer of property procured through expenditures by the decedent with the purpose, *effected at his death*, of having it pass to another. Sec. 402(c) taxes transfers made in contemplation of death. It would not, we assume, be seriously argued that its provisions could be evaded by the purchase by a decedent from a third person of property, a savings bank book for example, and its delivery by the seller directly to the

[53] 52 T.C. at 923.
[54] *Id.* at 927-28 (Raum, J., dissenting).

> intended beneficiary on the purchaser's death, or *that the measure of the tax would be the cost and not the value or proceeds at the time of death.*[55]

The majority in *Coleman* chose not to follow the substantive approach of the Court in *Chase* and applied a formal, restrictive definition of transfer, however, there were three well-reasoned dissents.[56] One of the dissenters relied on the above quoted passage from *Chase* and then neatly turned the majority's narrow formalism back upon it.[57] He did this by pointing out how strange it is to include only the amount of cash expended in contemplation of death because that cash was never transferred as such to the children. If "transfer," as the majority indicated, means that a particular form of property must leave the decedent and arrive in that same form in the hands of the beneficiary, then there was no more a "transfer" of the cash than there was of the insurance proceeds.[58] This same dissenter stated:

> The real question is how to value that transfer. I think it should be valued at what the amounts paid as premiums purchased in the way of insurance protection and not at what was actually paid for that protection.[59]

Another dissenter summed up the failure of the majority viewpoint:

> It seems to me that the majority opinion fans the flickering flame of form. The legal and economic substance is indeed interred. Too much emphasis is placed on formalities. Certainly the decedent had an "interest" in the insurance policy on her life. Granted that her children were "the record owners and beneficiaries," it was the decedent who *actually purchased* the policy.[60]

There are several other considerations that must be pointed out concerning Revenue Ruling 67-463. It should be emphasized that none of the cited cases has provided an answer to the valuation problem where the decedent initially took ownership of the policy and then transferred all ownership to beneficiaries more than three years before death, but con-

[55] 278 U.S. at 337 (emphasis added).
[56] 52 T.C. 926-28 (dissenting opinions).
[57] *Id.* at 926-27 (Tietjens, J., dissenting).
[58] *Id.*
[59] *Id.* at 926.
[60] *Id.* at 928 (Dawson, J., dissenting).

tinued to pay the premiums. The cases went no further than recognizing that this was a transfer. Revenue Ruling 67-463 does provide an answer. Therefore, estate planners should be aware that the ruling in this respect has not been rejected and should be considered when planning estates.[61]

In addition to the strong arguments supporting the Commissioner's view, there is one additional consideration that would dictate the adoption of Revenue Ruling 67-463. If this ruling is not accepted certain inequalities will actually ensue. Consider the man who cannot obtain life insurance because of age or medical history. He cannot benefit from the *Coleman* rule. For example, if he desires to give real property to his family as a source of income after he dies, and he does so in contemplation of death, the value of the property at his death would be included in his gross estate. If the property has increased in value, his estate tax burden will also be increased. Under the *Coleman* situation, the man who is insurable has a definite advantage. He can acquire an insurance policy with the beneficiaries as initial owners, guaranteeing the payment of proceeds far greater than his paid-in premiums, and will suffer an estate tax inclusion of only the amount of the actual cash premiums paid in contemplation of death. Therefore, for the same dollar outlay and the same ultimate values transferred, the insurable transferor will be able to transfer to his family an increased amount of values by virtue of the lower estate tax cost. Unless the revenue ruling is accepted, insurance will not be on the same footing as all other property. Indeed, values passing by insurance will receive more favorable tax treatment than all other forms of property transmitted at death.

The decisions thus far on Revenue Ruling 67-463 amass a "mixed-bag" of reasoning and create artificial distinctions. Realizing this, the Commissioner is unlikely to give up. As a federal tax system must deal in economic realties, the word "transferor" should be read to include those persons who provide the consideration for a transfer. As one authority has noted:

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[61] For estate tax planners, it should be noted that the commissioner is still free to insist upon the larger inclusion as set out in the ruling although he has lost the three mentioned cases. As far as we here in the fourth circuit are concerned, we must cope with the ruling until such time as this circuit has a court of appeals decision on the matter. While it is true that the Revenue Act of 1969 made the Tax Court a constitutional court, this does not mean that the Tax Court is bound in all later cases by the decision of a single circuit court of appeals. Instead, the present state of affairs is that the Tax Court is bound in later cases only by court of appeals decisions involving cases in that particular circuit. Jack E. Golson, 54 T.C. 742 (1970).

It seems reasonably clear that, if I direct my broker to purchase 100 shares of xyz stock in the name of my son and I pay the purchase price, I have transferred 100 shares of xyz stock, not the dollars paid.[62]

If a decedent seeks out the insurer, negotiates all the terms of the policy, requests the insurer to create all the policy rights in another, and pays the first premium which actually brings the contractual rights, as evidenced by the policy issued, into existence, to say that this is not a "transfer" by the decedent is to put form over substance. If the decedent continues to pay the premiums, he remains the motivating force of the transaction, at least with respect to the amount of proceeds attributable to the premium payments within three years of his death. The premium was paid to the insurer to purchase an asset—the asset being the insurer's promise to pay the policy proceeds on the death of the insured. Inherent in life insurance is the fact that the value of the company's promise to pay is always increasing in value as death draws nearer. The decedent's payment to the insurer is prompted by the knowledge that this manner of payment will assure him of getting something more for his money, *i.e.*, a benefit to the donee greater than the dollars paid for the premium payment, in the form of insurance proceeds in excess of the money paid.

On balance, the pro rata valuation (the Revenue Ruling's procedure for valuation) seems to be the method which best carries out the prior policies and decisions regarding the taxation of gifts in contemplation of death. It takes cognizance of the donor's intent in paying the premiums and does not violate the congressional intent that underlays the amendments to section 2042.[63]

MICHAEL DONWELL GUNTER

Insurance—Life Insurance Applications: Opinion Answers or Material Misrepresentations

With its recent decision in *Prudential Insurance Co. of America v. Barden*,[1] the Court of Appeals for the Fourth Circuit may have demonstrated that the converse of the time-worn judicial apology, "hard cases make bad law," is not necessarily true. Beneath *Barden's* deceptively

[62] Stephens, *The Clifford Shadow over the Federal Estate Tax*, 4 GA. L. REV. 233, 248 (1970).
[63] *See* Note, 82 HARV. L. REV., *supra* note 40, at 1771.

[1] 424 F.2d 1006 (4th Cir. 1970).