

1961

Estate and Gift Taxation: Final Examination (January 1961)

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I (40)

H and W are contemplating entering into a written separation agreement which will provide:

- (1) that H will pay W \$500 a month for her support during their joint lives,
 - (2) that he will direct his executor to purchase a commercial annuity which will pay W \$300 a month for the balance of her life if she should survive him,
 - (3) that he will give her his secured note for \$100,000, payable with interest at \$10,000 a year for 10 years for the release of her dower rights.
- (a) What would you advise him as to the gift tax consequences, both upon the making of such agreement and upon payment in each subsequent year of \$6,000 for support and a \$10,000 installment on the note, assuming that they will not divorce, and considering all applicable exclusions and deductions other than the specific exemption?

They enter into the agreement as set forth above in January, 1955. H makes the prescribed payments of \$6,000 for W's support and \$10,000 installment on the note in each of the years 1955 through 1960. He dies on Dec 31, 1960, his will making provision for W's support annuity as agreed. Discuss (b) the potential includibility in his gross estate of any amounts paid by H to W before his death pursuant to the agreement, (c) the deductibility of the estate's indebtedness for W's survivorship annuity and the unpaid balance of installments on the note, and (d) the applicability of an estate tax marital deduction for such interests thereby passing to W.

II (20)

Father established an irrevocable inter vivos trust for his two adult daughters with provisions that the income was to be divided equally between them during F's lifetime and one-half the principal paid to each at his death. In the event of prolonged illness of either daughter, or other emergency whereby one-half of the income would not be sufficient for one's needs, F was to have the power to reapportion the income interests between them to the extent warranted by such circumstances. If either should die before F, her issue, if any, should have her share of the income and principal, and if no issue, the survivor of them should then have the whole of the income until F's death and then the whole of the principal. F dies in January, 1961, survived by both daughters, neither of whom were married or had issue. Discuss the includibility of the trust corpus in F's gross estate, making such assumptions as to the value of interests as you find to be necessary in reaching conclusions.

40,000

III (10)

H has an opportunity to buy some investment realty for \$20,000. He has reliable information that a shopping center and other improvements are likely to locate in that area whereby the property may well increase in value to \$100,000 in a matter of 5 years, and he contemplates holding the property for that time and then disposing of it in the peak market. He wishes to give his wife an one-half interest in the enterprise and he has in mind that a tenancy by the entirety will accomplish his purpose. He desires to know the gift tax considerations involved. What information and advice would you give him, assuming that he has previously used his specific exemption?

IV (30)

F was a widower, 50 years old, with an actuarial life expectancy of 25 years. He owned all of the stock of a corporate business, F Mfg Co, and desired to establish a trust for his only child, son S, age 15, who he hoped to bring into the business and ultimately turn it over to him. The business is firmly established, stable, and with a consistent dividend record of at least 6% over many years. F placed 40% of the F stock in the trust for S with these provisions:

- (1) that the dividend income would be accumulated and added to principal until S reached 21, unless the independent trustee, controlled by the same considerations as would control a guardian, should determine that S should have the income of any year in the best interests of his welfare;
- (2) that upon S reaching age 21, the annual income be paid to him during the balance of the trust term;
- (3) that the corpus be distributed to S free of trust upon his reaching age 30;
- (4) if S should die before attaining age 30, the trust would thereupon

terminate and the corpus distributed to S's estate; and

(5) F retained the power to direct that at any time after S reached 21 shares up to one-half of the total number in trust be distributed outright to S if, in F's opinion, S evidenced sufficient interest and endeavor in the business to warrant outright ownership.

(a) Is F entitled to a gift tax annual exclusion for any part of the value of the stock with which he will fund the trust and, if so, for what interest or interests?

(b) Discuss the potential includibility of any trust interests in F's gross estate if he should die survived by S, 19 years old and unmarried.

(c) Would your analysis in (b) be any different if S were 22 years old at the time of F's death and no stock had been distributed outright to him pursuant to F's power?

V (20)

H designated his wife, W, to be the sole beneficiary of a \$50,000 insurance policy on his life. He did not reserve the right to change the beneficiary, nor did he name alternates in the event of W predeceasing him. Local law provides that if a beneficiary predeceases an insured and no alternates are designated, the proceeds are payable to the insured's estate. Subsequently H transferred all of his rights in the policy to W, including the right to the cash surrender value. H, however, continued the premium payments of \$2,000 annually until his death, survived by W, in 1960. The total of premiums paid by H prior to his death was \$20,000, of which \$6,000 had been paid within the 3 years immediately preceding his death. Following his death, the insurer paid W the \$50,000 proceeds in lump sum. What amount, if any, is likely to be included in H's gross estate resulting from the above?

VI (40)

Settlor, S, intends to establish an irrevocable inter vivos trust for the benefit of his brother, B, B's only child, Nephew N, and N's children. The income of the trust should ordinarily be sufficient, coupled with their own sources of support, for B's and N's needs, however, he wishes them to be able to draw upon principal for a sound purpose, at least to the extent that it would not impair his tax objective. His tax objective is that the trust fund should incur only his own initial gift tax liability and no further gift or estate taxes for such part of it as may ultimately pass in remainder to N's children. He is contemplating using the following provisions, in summary, and wishes to know which of them, if any, would impair his tax objective and in what respects:

(1) Income to B for life, then to N for life, and the principal to such of N's children as the survivor of B and N should by will appoint, and in default of appointment, then to the issue of the survivor per stirpes;

(2) that the principal may be drawn upon without limitation by either B or N, but only with S's consent if living, and

(3) following S's death, then only by joint consent of B and N, and

(4) if S and either B or N are deceased, then the survivor of them may draw upon the principal to the extent of 5% of the amount thereof in any one year, except that if prolonged sickness or other emergency should require extraordinary expenditures, any amount of the principal may be drawn upon to meet such expenses,

(5) but, notwithstanding (4), such survivor may draw upon the principal without limitation and for any non-frivolous purpose with the consent of the independent corporate trustee whose decision as to the soundness of the purpose shall be final.

What would you advise, considering each of the above numbered provisions separately in its affect upon S's tax objectives?

VII (20)

estate tax

Will the following interests acquired by W qualify for the marital deduction?

(a) H transferred rental property to his son, S, more than 3 years prior to his death in consideration for S paying an amount equal to one-half of the annual net rental income from the property to H during his lifetime and then to W for her life. H is survived by W and S.

(b) H sells property worth \$20,000 to X, taking \$5,000 cash and a mortgage on the property for the balance of \$15,000, payable at \$1,000 a year with interest. Five years later H bequeaths his interest as mortgagee to W.

(c) H devises realty to W and his son, S, jointly with right of survivorship.

(d) H devises realty to his daughter, D, for life, remainder in fee to D's issue, and if none, then to W for life, remainder in fee to W's estate. D is a 55 year old spinster at H's death.