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## Exclusion of Group Life Insurance Proceeds From Insured's Gross Estate for Estate Tax Purposes

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## COMMENTS

### EXCLUSION OF GROUP LIFE INSURANCE PROCEEDS FROM INSURED'S GROSS ESTATE FOR ESTATE TAX PURPOSES

#### I. INTRODUCTION

Group term life insurance,<sup>1</sup> provided by an employer for the benefit of his employees,<sup>2</sup> is becoming an increasingly popular form of insurance, due, in large part, to the favorable tax treatment afforded such policies. For example, to a large extent, the premiums, paid and deductible by the employer,<sup>3</sup> are not considered part of the employee's gross income.<sup>4</sup> Another attractive feature of group life policies is that each member of the group, including those who might otherwise be uninsurable, may take advantage of the policy at low cost<sup>5</sup> to the employer or to both the employer and employee where there is joint contribution. Group life insurance coverage is afforded to all the employees<sup>6</sup> and,

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1. Group term life insurance is protection covering a number of lives under a single policy, the insured persons not being the contracting parties with respect to the group policy. A situation where an employer takes out individual policies of life insurance on the lives of his employees does not fall within the group term definition. The amount of protection provided each employee under a group policy must be based upon some plan which precludes the individual selection of such amounts. Proposed Treas. Reg. § 1.79-1(b)(1), 29 Fed. Reg. 10517 (1964).

2. Group life insurance was made available for civilian officers and employees of the federal government by the Federal Employees' Group Life Insurance Act of 1954, 68 Stat. 736, 5 U.S.C. § 2091 (1964).

3. Int. Rev. Code of 1954, § 162(a); 2 Cum. Bull. 88 (1920).

4. Int. Rev. Code of 1954, § 61(a)(1); Treas. Reg. § 1.61-2(d)(2) (1957). The 1964 amendments to the Code, however, provide that the cost of group term life insurance exceeding the face value of \$50,000 paid by the employer constitutes gross income to the employee. Int. Rev. Code of 1954, § 79. See generally Nagel, *How the New Group-Term Life Insurance Sections of the Internal Revenue Code Will Operate*, 1964 Ins. L.J. 412.

5. Term insurance is not without its disadvantages, the most significant of which stems from the very basis of the policy—the employment contract. Frequently, a termination of the employment contract and a termination of group coverage are mutually inclusive and concurrent events. An option given the insured to convert his group coverage, upon retirement, into permanent life insurance may afford an opportunity for coverage regardless of the insured's physical condition. However, the premiums, no longer formulated on a group basis but, rather, determined by reference to the actuarial tables, may prove too great a financial burden. Allyn, *Group Life Insurance: Development, Codification, Trends and Use*, 1953 Ins. L.J. 389, 392.

6. N.Y. Ins. Law § 204(1)(d)(1); Proposed Treas. Reg. § 1.79-1(b)(1)(v)(b), 29 Fed. Reg. 10517 (1964).

therefore, high-salaried executives,<sup>7</sup> subject to high income tax rates, frequently avail themselves of this comparatively low cost insurance.<sup>8</sup>

Under present law, the proceeds of ordinary life insurance are included in the decedent's gross estate if the decedent possessed any "incidents of ownership" in the policy immediately prior to his death.<sup>9</sup> Although the term "insurance" is not defined by the Internal Revenue Code, group life insurance is given the same treatment as other types of life insurance for estate tax purposes.<sup>10</sup> From the standpoint of the insured's family and dependents, it is desirable that they receive the full insurance proceeds, undiminished by the federal estate tax.<sup>11</sup>

## II. THE POLICY

The typical group plan involves renewable term insurance<sup>12</sup> which terminates with the insured's employment.<sup>13</sup> A master policy is issued to the employer, which does not require medical examination of the employees and which may preclude individual selection.<sup>14</sup> The master policy constitutes the contract of insurance between the employer and the insurer, with a certificate being issued to the employee as evidence of that insurance coverage.<sup>15</sup> The employer may pay the entire premium, although it is common for the employee to contribute.<sup>16</sup>

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7. "The policy may provide that the term 'employees' shall include the officers, managers, employees and retired employees of the policyholder . . . . The policy may provide that the term 'employees' shall include the individual proprietor or partners if the employer is an individual proprietor or a partnership." N.Y. Ins. Law § 204(1)(a). A provision to this effect is not uncommon in state insurance law. E.g., Okla. Stat. tit. 36, § 4101(A)(1) (1961); Wash. Rev. Code § 48.24.020(1) (1951).

8. For the device of an owner-executive receiving virtually all the coverage under a group policy with just enough employee coverage to meet the underwriting requirements, see Friedman & Bakst, *Synthetic Group Life Insurance: New Opinion May Be the End of a Gimmick*, 12 J. Taxation 172 (1960).

9. Int. Rev. Code of 1954, § 2042; 26 C.F.R. § 20.2042-1(c)(1) (1961). Among the incidents of ownership in an insurance policy, whether it is group life or otherwise, are the insured's: right to the economic benefits of the policy; power to change the beneficiary; power to surrender or cancel the policy; or power to pledge or assign the policy. See notes 27-29 *infra* and accompanying text.

10. 1 CCH Fed. Est. & Gift Tax Rep. ¶ 1650.05 (1962); see M. W. Dobrzensky, 34 B.T.A. 305 (1936).

11. Int. Rev. Code of 1954, § 2042.

12. For a discussion of the word "term," see notes 97 & 103 *infra* and accompanying text. Due to the considerably higher premium cost of group permanent insurance, employers usually prefer term insurance. A disadvantage of group permanent insurance to the employee is that the premiums which the employer pays constitute a part of the covered employee's taxable income. Lefevre, *Use of Life Insurance in Business and Employment Relationships*, N.Y.U. 22d Inst. on Fed. Tax 1281, 1285-86 (1964).

13. 1 Couch, Insurance § 1:54 (2d ed. 1959).

14. 1 Richards, Insurance § 15 (Freedman 5th ed. 1952). In New York, such preclusion is required by statute. N.Y. Ins. Law § 204(1)(a).

15. E.g., *Crawford v. Metropolitan Life Ins. Co.*, 167 S.W.2d 915, 924 (Mo. Ct. App. 1943); 1 Richards, Insurance § 15 (Freedman 5th ed. 1952).

16. N.Y. Ins. Law § 204(1)(a) provides that the premiums may be paid "either wholly

The group life policy is similar to other life insurance policies in that the insured may have the power to change the beneficiary<sup>17</sup> and to elect optional modes of settlement without the consent of the beneficiary.<sup>18</sup> The distinctive feature of the group policy is the provision giving to the employee the right, under certain circumstances, to convert the policy into individual life insurance.<sup>19</sup>

### III. INCIDENTS OF OWNERSHIP

The 1942 amendments to the Internal Revenue Code of 1939<sup>20</sup> provided that proceeds of life insurance were includible in the insured's gross estate if either: (a) the decedent had paid, directly or indirectly, the premiums for the policy; or (b) the decedent possessed any incidents of ownership at the time of his death, exercisable either alone or in conjunction with another.<sup>21</sup>

The Internal Revenue Code of 1954 altered the test for includibility of such proceeds which were payable to the beneficiaries other than the decedent's estate,<sup>22</sup> by abolishing the "payment of premiums" test.<sup>23</sup> Thus, today, life insurance proceeds are includible in the decedent's gross estate only<sup>24</sup> if he

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from the employer's funds or funds contributed by him or from funds contributed jointly by the employer and employees." Several states have adopted similar provisions. E.g., Iowa Code § 509.1(1)(b) (1962); Tex. Ins. Code art. 3.50(1)(b) (1952).

17. See text accompanying notes 42 & 43 *infra*.

18. See generally Sears, *What Every Lawyer Should Know About—Life Insurance Optional Modes of Settlement*, 42 Ill. B.J. 284 (1954).

19. See notes 45-56 *infra* and accompanying text.

20. The Internal Revenue Code of 1939 provided for the inclusion in the insured's gross estate of proceeds of life insurance "receivable by the executor . . . and . . . receivable by all other beneficiaries as insurance under policies taken out by the decedent upon his own life." Int. Rev. Code of 1939, ch. 3, § 811(g), 53 Stat. 122. Some uncertainty arose concerning the definition of "policies taken out by decedent upon his own life." Two tests evolved: "incidents of ownership" and "payment of premiums." 4 Rabkin & Johnson, *Federal Income, Gift and Estate Taxation* § 61.04(2) (1958). At different times, the courts applied either or both of these tests, thus further confusing the issue. *Ibid*.

21. Revenue Act of 1942, § 404(a), 56 Stat. 944; see 4 Rabkin & Johnson, *op. cit.* supra note 20, § 61.04(3).

22. Int. Rev. Code of 1954, § 2042 provides, in part:

"The value of the gross estate shall include the value of all property—

(1) Receivable by the executor.

"To the extent of the amount receivable by the executor as insurance under policies on the life of the decedent.

(2) Receivable by other beneficiaries.

"To the extent of the amount receivable by all other beneficiaries as insurance under policies on the life of the decedent with respect to which the decedent possessed at his death any of the incidents of ownership, exercisable either alone or in conjunction with any other person."

23. The test was abolished for decedents dying after August 16, 1954. Int. Rev. Code of 1954, § 2042. But see note 113 *infra* and accompanying text.

24. Proceeds of life insurance which are not includible in the gross estate under § 2042 may be included, however, depending upon the facts, under § 2035. See 26 C.F.R. § 20.2042-1(a)(2) (1961).

possessed any incidents of ownership which he could exercise either alone or with another,<sup>25</sup> immediately prior to his death.<sup>26</sup>

The Treasury Regulations attempt to give an illustrative, rather than exhaustive, list of these incidents:

[T]he term "incidents of ownership" is not limited in its meaning to ownership of the policy in the technical legal sense. Generally speaking, the term has reference to the right of the insured or his estate to the economic benefits of the policy. Thus, it includes the power to change the beneficiary, to surrender or cancel the policy, to assign the policy, to revoke an assignment, to pledge the policy for a loan, or to obtain from the insurer a loan against the surrender value of the policy, etc.<sup>27</sup>

The courts are in general agreement with the Regulations. It has been held that the determination of whether a decedent possessed any incidents of ownership and the interpretation of such incidents is one of fact.<sup>28</sup> As a result, recurring fact patterns have given the courts sufficient opportunity to rule on the examples contained in the Regulations.<sup>29</sup> As will be seen,<sup>30</sup> group term life insurance policies contain several incidents of ownership,<sup>31</sup> the presence of any of which would result in making the proceeds payable thereunder includible in the decedent's taxable estate.

25. Although only a few cases have dealt with the phrase "in conjunction with any other person," the interpretation that they have imposed is indeed a liberal one. Thus, a mere power in the decedent, in his capacity as trustee or otherwise, to veto changes to be effected by others, has been held within the section. 2 Mertens, *Federal Gift and Estate Taxation* § 17.15 (1959); see *Commissioner v. Estate of Karagheusian*, 233 F.2d 197 (2d Cir. 1956); *Estate of Goldstein v. United States*, 129 Ct. Cl. 264, 122 F. Supp. 677 (1954), cert. denied, 348 U.S. 942 (1955).

26. "[A]lthough the insured must possess incidents of ownership at his death, he need not have retained or reserved these incidents in connection with any transfer of the insurance or designation of a beneficiary thereunder . . ." Lowndes & Kramer, *Federal Estate and Gift Taxes* 295-96 (1956). (Footnotes omitted.) (Emphasis omitted.)

27. 26 C.F.R. § 20.2042-1(c)(2) (1961). The term "incidents of ownership" also includes a reversionary interest arising out of operation of law or the express term of the insurance contract which is in excess of 5% of the value of the policy. 26 C.F.R. § 20.2042-1(c)(3) (1961).

28. *Fried v. Granger*, 105 F. Supp. 564 (W.D. Pa. 1952), aff'd per curiam, 202 F.2d 150 (3d Cir. 1953).

29. The following incidents of ownership have been ruled on:

(a) The power to change primary beneficiary. *Farwell v. United States*, 243 F.2d 373 (7th Cir. 1957); *Helvering v. Reybina*, 83 F.2d 215 (2d Cir. 1936).

(b) The power to change contingent beneficiary. *Broderick v. Keefe*, 112 F.2d 293 (1st Cir.), appeal dismissed mem., 311 U.S. 721 (1940).

(c) The power to surrender and cancel the policy. *Bessie M. Ballinger*, 23 B.T.A. 1312 (1931); *Chase Nat'l Bank v. United States*, 278 U.S. 327, 335 (1929) (dictum). But see *Central Hanover Bank & Trust Co.*, 40 B.T.A. 268 (1939). See also *Commissioner v. Treganowan*, 183 F.2d 288 (2d Cir.), cert. denied, 340 U.S. 853 (1950).

30. See notes 34-83 *infra* and accompanying text.

31. For the insured to retain the incidents of ownership, it is not necessary that he retain possession of the policy. *Fried v. Granger*, 105 F. Supp. 564 (W.D. Pa. 1952), aff'd per curiam, 202 F.2d 150 (3d Cir. 1953).

The subject of assignment of group life insurance for federal estate tax purposes is comparatively new. Respecting *individual* coverage, the most common means by which the insured may divest himself of the incidents of ownership is by absolute assignment.<sup>32</sup> However, it has not yet been determined whether the Internal Revenue Service will recognize that an employee may, by assignment, completely divest himself of all his interest in the *group* coverage, so as to satisfy the statutory requirement<sup>33</sup> that he possess no incidents of ownership in the policy at the time of his death.

#### IV. DIVESTMENT OF INCIDENTS OF OWNERSHIP BY ASSIGNMENT

In general, an insurance policy is an assignable chose in action,<sup>34</sup> the assignment of which is not contrary to public policy.<sup>35</sup> However, both the master policy as well as the certificate invariably contain a provision prohibiting assignment.<sup>36</sup> Although a provision of this nature is not a legal requisite to a valid policy, and may be eliminated, the employer may be unwilling to delete the provision from all the policies since this would defeat many of the advantages of group coverage, especially the inducement of continuing employment. Since the prohibition is beneficial to the employer, his consent may be required to vitiate the effectiveness of the prohibition.<sup>37</sup> Furthermore, since it has been stated that limitations on assignment are for the benefit of the insurer,<sup>38</sup> such limitations may also have to be waived by it.<sup>39</sup> It has been suggested<sup>40</sup> that a procedure whereby the employer, employee, and insurer enter

32. 26 C.F.R. § 20.2042-1(c)(1) (1961).

33. Int. Rev. Code of 1954, § 2042.

34. *Grigsby v. Russell*, 222 U.S. 149 (1911); *St. John v. American Mut. Life Ins. Co.*, 13 N.Y. 31 (1855); Annot., 30 A.L.R.2d 1310 (1953).

35. *Senese v. Senese*, 121 N.Y.S.2d 498, 503 (Sup. Ct. 1953) (dictum).

36. See Vance, *Insurance* § 203, at 1039 (3d ed. 1951).

37. See *Metropolitan Life Ins. Co. v. Woolf*, 138 N.J. Eq. 450, 453, 47 A.2d 340, 342 (Ct. Err. & App. 1946). In *Metropolitan Life Ins. Co. v. Brown*, 222 Ky. 211, 213-14, 300 S.W. 599, 600 (1927), the court stated: "The chief reason the coal company [employer] had for effecting and keeping paid the cost of this insurance for its employees was that they might thereby be induced to continue in its service. Such tendency as the insurance had to that end would be destroyed completely by the assignment of the policy and its benefits."

38. *Missouri State Life Ins. Co. v. Robertson Banking Co.*, 223 Ala. 13, 134 So. 25 (1931) (dictum); accord, *Hamilton v. Hamilton*, 255 Ala. 284, 290, 51 So. 2d 13, 18 (1950) (dictum); *Asphalt Paving Inc. v. Ulery*, 149 So. 2d 370, 378 (Fla. Ct. App. 1963) (dictum).

39. See *Oleska v. Kotur*, 113 Ind. App. 428, 48 N.E.2d 88 (1943); *McNamee v. Griffin*, 137 N.Y.S.2d 220, 222 (Sup. Ct. 1954), rev'd per curiam on other grounds, 285 App. Div. 886, 137 N.Y.S.2d 749 (1st Dep't), aff'd mem., 309 N.Y. 864, 131 N.E.2d 264 (1955).

In *Metropolitan Life Ins. Co. v. Poliakoff*, 123 N.J. Eq. 524, 528, 198 Atl. 852, 853 (Ch. 1938) (group life policy), the court stated: "If an assignment under the circumstances of the case will not interfere with fulfillment of the parties' intention, the prohibition will be disregarded." Accord, *Chelsea-Wheeler Coal Co. v. Marvin*, 132 N.J. Eq. 462, 28 A.2d 505 (Ct. Err. & App. 1942), rev'd on other grounds after retrial, 134 N.J. Eq. 432, 35 A.2d 874 (Ct. Err. & App. 1944); *Hasselberger v. Hasselberger*, 102 N.Y.S.2d 520 (Sup. Ct. 1951).

40. McCarthy, *Personal Life Insurance: Transfers of Ownership of Life Policies; Application of Federal Tax Liens to Life Insurance*, N.Y.U. 18th Inst. on Fed. Tax 435, 439 (1960).

into an agreement retaining the prohibition in the master policy, but waiving it for specific employees,<sup>41</sup> would have the desired result of circumventing the assignment prohibition.

Assuming that the problem of the assignment prohibition has been successfully bypassed, the question remains whether, despite its unique features, a group policy can be assigned so as to completely divest the insured of every incident of ownership.

#### A. *Power To Change the Beneficiary*

The right to designate the beneficiary of a group policy is conferred by the policy itself, as required by state law.<sup>42</sup> Although the power to change the beneficiary is not required by state law, it is, almost universally, conferred by the policy. This power to change the beneficiary is specifically designated in the Regulations as an incident of ownership.<sup>43</sup> That the insured, by an unconditional assignment of the policy, can satisfactorily divest himself of this incident of ownership is uncontested.<sup>44</sup>

#### B. *Conversion Privilege*

Virtually all group life insurance policies contain a provision giving the employee the right to convert the policy into individual life insurance without

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41. The problem of excluding group life insurance proceeds from the gross estate has not been of troublesome nature to the employee who has only \$5,000 group coverage. (The average size group policy as of 1963 was \$4,490. McNeill, *Excess Group Life, Split-Dollar or Deferred Compensation?*, 19 J. Am. Soc'y C.L.U. 255, 256 (1965).) Congress, in declaring a \$60,000 exemption in determining the taxable estate, has alleviated the necessity of assigning what would otherwise be the taxable property of low and middle income employees. Int. Rev. Code of 1954, § 2052. This congressional grace, however, does not solve the \$100,000-a-year executive's dilemma of salvaging, for his surviving spouse and family, as much of his liquid assets as possible. It is submitted that, in order to satisfy the requirements of all parties concerned, the following plan may be considered:

(a) On group policies of \$20,000 or less, there should be an absolute prohibition of assignment;

(b) On policies over that amount, there should be an anti-assignment clause with provision for waiver where the assignment would be to the insured's immediate family or in his best interest. In negative terms, "best interest" of the employee would include the denial of the waiver when the assignment would be for the purpose of creditors, as security for a loan or for reasons other than the security of the employee's family.

42. E.g., Colo. Rev. Stat. Ann. § 72-6-2(6) (1953); N.Y. Ins. Law § 161(1)(d); Wash. Rev. Code § 48.25.150 (1951).

43. See note 27 *supra* and accompanying text.

44. In *Anna Rosenstock*, 41 B.T.A. 635, 637 (1940), the court stated: "By such unconditional assignment the insured was divested of all legal interest in those policies. Also, by such act, insured's right, reserved in the policies, to change the beneficiary was abrogated. *Jacobs v. Strumwasser*, 145 N.Y.S. 916."

It should be noted that some doubt has been raised as to whether an irrevocable designation of a beneficiary would effectually extinguish that incident of ownership for more than one year where the type of insurance is group term. See notes 95-111 *infra* and accompanying text.

evidence of insurability, upon termination either of his employment<sup>45</sup> or of the policy.<sup>46</sup> There appears to be no reason to presume that this conversion privilege is "personal" to the insured and, hence, inalienable.<sup>47</sup> Unfortunately, however, the rationale of several decisions has been employed by some authorities to suggest the contrary.<sup>48</sup>

In *Fearon v. Metropolitan Life Ins. Co.*,<sup>49</sup> the insured's brother was named beneficiary. The group policy contained a conversion option which was exercisable within a thirty-one day period. The insured died after terminating his employment, but prior to the expiration of the option period.<sup>50</sup> His brother, the beneficiary, made a futile attempt to exercise the option—before the expiration of this period—by obtaining a policy on the life of his dead brother.<sup>51</sup> The court refused to allow the exercise of the conversion privilege, and held that the insurance company was only under an obligation to issue a new policy if the person upon whose life the policy was to be issued was alive at the time

45. 1 Appleman, *Insurance Law and Practice* § 125 (1941). The New York Insurance Law provides that no policy of group life insurance can be issued without "a provision to the effect that in case of the termination, for any reason whatsoever, of the employment of any employee while insured under a group policy issued to his employer . . . such employee . . . shall be entitled to have issued to him by the insurer, without evidence of insurability, upon application made to the insurer within thirty-one days after such termination . . . a policy of life insurance only . . . in an amount equal to the amount of his protection under such group insurance policy at the time of such termination . . ." N.Y. Ins. Law § 161(1)(e). See, e.g., Colo. Rev. Stat. Ann. § 72-6-2(3) (1953); Pa. Stat. Ann. tit. 40, § 532.6(8) (1954); Va. Code Ann. § 38.1-428.1 (Supp. 1964).

It is further provided that, "in the event a group life insurance policy . . . permits a certificate-holder to convert to another type of life insurance within a specified time after the happening of an event, such certificate-holder shall be notified of such privilege and its duration within fifteen days after the happening of the event . . ." N.Y. Ins. Law § 204(3). See Ariz. Rev. Stat. Ann. § 20-1269 (1956); Pa. Stat. Ann. tit. 40, § 532.7 (1954).

46. N.Y. Ins. Law § 161(1)(f) provides that, if the insurer or employer cancels the policy, all employees who have been covered under such policy for a minimum of five years shall be entitled to a life insurance policy not to exceed \$2,000. See, e.g., Ariz. Rev. Stat. Ann. § 20-1267 (1956); Colo. Rev. Stat. Ann. § 72-6-2(9) (1953); Pa. Stat. Ann. tit. 40, § 532.6(9) (1954); Va. Code Ann. § 38.1-428.2 (Supp. 1964).

47. Because the conversion privilege is exercisable only upon the termination of employment or the cancellation of the policy by the employer, it could be classified as a future interest. It has been held that future interests are freely assignable. E.g., *Clowe v. Seavey*, 208 N.Y. 496, 102 N.E. 521 (1913); *In the Matter of Mfrs. & Traders Trust Co.*, 270 App. Div. 322, 59 N.Y.S.2d 519 (4th Dep't 1946); *In the Matter of Estate of Heye*, 149 Misc. 890, 269 N.Y. Supp. 530 (Surr. Ct. 1933), *aff'd mem.*, 241 App. Div. 907, 271 N.Y. Supp. 1042 (4th Dep't 1934).

48. McCarthy, *supra* note 40, at 439-40; see Yohlin, *New Tax Opportunities and Pitfalls in Assignments of Life and Group Insurance Benefits*, 13 *J. Taxation* 130 (1960). "[T]he privilege of conversion must be affirmatively exercised by the certificate holder himself, in the absence of a statutory rule to the contrary." 1 Richards, *Insurance*, § 15, at 57 (Freedman 5th ed. 1952). See N.Y. Ins. Law § 161(e).

49. 138 Misc. 710, 246 N.Y. Supp. 701 (Munic. Ct. N.Y. 1930).

50. *Id.* at 711, 246 N.Y. Supp. at 702-03.

51. *Id.* at 711-12, 246 N.Y. Supp. at 703-04.



the conversion privilege was attempted to be exercised.<sup>52</sup> And, in *Young v. General Am. Life Ins. Co.*,<sup>53</sup> where it was held that the beneficiary could not exercise the right of conversion after the insured employee's death, the court stated:

The decedent in the instant case failed to exercise the privilege for a conversion. The pertinent question now presented is whether or not the beneficiary had such right *after* the death of her husband. We are forced to the conclusion, upon principle as well as upon decided cases, that the beneficiary would have no such right. The very language of the policy relative to conversion demands affirmative action on the part of employee whose employment is discontinued.<sup>54</sup>

The language of the court in the *Young* case would seem to be the stronger authority of the two cases for concluding that the conversion privilege is personal to the employee and, hence, unassignable. The ruling of that court, however, is not on point despite the language used in dictum. It should be particularly noticed that, at the time of the insured's death, *no other party* had the right to exercise the conversion privilege. The policy had conferred the right on the insured employee, and no assignment or transfer of that right had been attempted. Hence, the effectiveness of such an attempt was not ruled upon. Furthermore, in both cases the attempted exercise of the conversion privilege by the beneficiary did not occur until after the death of the insured. Thus, their applicability, even by analogy, is at best tenuous.

It has been suggested that the requirement that group life insurance policies contain a conversion privilege<sup>55</sup> evidences a legislative intent that the privilege be one of which the insured cannot be divested.<sup>56</sup> However, it would seem that the purpose of this requirement is only to protect the insured by guaranteeing continued insurability. Therefore, assignment of this privilege would not be tantamount to a waiver since the conversion privilege could still be exercised by the assignee. As a result, there is no good reason why an assignment of the conversion privilege should not be effective to divest the insured employee of this incident of ownership.

### C. Power To Cancel by Terminating Employment

In the Regulations, the power to "surrender or cancel the policy" is specifically designated as an incident of ownership.<sup>57</sup> May it be said that the

52. *Id.* at 712, 246 N.Y. Supp. at 704.

53. 35 Ohio L. Abs. 464, 41 N.E.2d 895 (Ct. App. 1941). In *Crutchfield v. Continental Assur. Co.*, 336 Ill. App. 411, 84 N.E.2d 333 (1949), the conversion privilege was again held to be coterminous with the life of the employee insured, despite the fact that, at the time the group insurance policy expired, the insured was totally incapacitated.

54. *Young v. General Am. Life Ins. Co.*, *supra* note 53, at 467, 41 N.E.2d at 897. (Emphasis added.)

55. The laws of some 37 states require a similar conversion privilege. E.g., Cal. Ins. Code § 10209(b); Ill. Rev. Stat. ch. 73, § 843(d) (1961); Pa. Stat. Ann. tit. 40, § 532.6 (1954); Va. Code Ann. § 38.1-428.1 (Supp. 1964); Wash. Rev. Code § 48.24.180 (1951).

56. Taft, Group Life Proceeds—A Taxing Problem, 9 J. Am. Soc'y C.L.U. 324, 330 (1955).

57. 26 C.F.R. § 20.2042-1(c)(2) (1961).

cancellation of the group policy through the exercise of the power to terminate employment is an incident of ownership? The Regulations state that "the term [incidents of ownership] has reference to the right of the insured or his estate to the economic benefits of the policy."<sup>58</sup> Since no cash surrender value attaches to a group term policy, neither the insured nor his estate would receive any economic benefit as a result of cancellation. The problem, however, may not be as simple as that.

In *Commissioner v. Treganowan*,<sup>59</sup> the insured's executor excluded 20,000 dollars from the gross estate. The deceased had been a member of the New York Stock Exchange, the constitution of which established a "Gratuity Fund" providing for the payment of 20,000 dollars by the surviving members to the families of the deceased members. No member had the right to name, select or designate any beneficiary other than the members of his family as prescribed by the constitution, nor could the proceeds be assigned or pledged for the payment of a debt.<sup>60</sup> The court held that, even though the deceased did not have the normal incidents of ownership, "an Exchange member does have the power to sell his seat, thus divesting his beneficiary of any right to payments, and entitling the purchaser to the same insurance which the seller has had."<sup>61</sup> It appears from the language used by the court that the cancellation of the *policy* by termination of employment was not the incident of ownership. Rather, the fact that the cancellation would result in divesting the beneficiary of the right to payment was the incident of ownership. In the case of an assigned group policy, cancellation by termination of employment will not divest the beneficiary of his right to payment. Although the specific group policy will be cancelled, the rights of the beneficiary will not be affected by that cancellation since apparently the assignee can exercise the conversion privilege. Hence, insurance coverage will be discontinued and the beneficiary will be divested of his right to payment only if the assignee elects not to exercise this privilege.<sup>62</sup>

Furthermore, the incidents of ownership, as enumerated in the Regulations, relate to the proceeds in one of two ways: either in the amount that will be distributed, or in the scheme of that distribution.<sup>63</sup> For example, a change in beneficiary will affect the scheme of distribution, whereas a pledge or loan may affect the amount of proceeds ultimately distributed.<sup>64</sup> However, the cancellation of the group policy by employment termination could not result in a disbursement change where the assignee exercises the conversion privilege,

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58. *Ibid.*

59. 183 F.2d 288 (2d Cir.), cert. denied, 340 U.S. 853 (1950).

60. 183 F.2d at 289.

61. *Id.* at 292.

62. Where the assignee is not the beneficiary, the rights of the beneficiary will again not be affected directly by the assignor's action. The beneficiary will be divested of his right to payment only if the assignee elects not to convert or if he changes the beneficiary.

63. See note 27 *supra* and accompanying text.

64. Under a pledge agreement, the pledgee would require that he would be made a beneficiary up to the amount of the loan, thus temporarily divesting the original beneficiary of at least a portion of the expected proceeds. If the pledgor fails to repay the loan, however, there would be a permanent divestment.

and, even where this privilege is not exercised, it is not the scheme of distribution which is affected but, rather, the very fact of distribution. Affecting the very fact of distribution will be an incident of ownership, in the case of the cancellation of an individual policy, because in a sense there is an effect upon the scheme of distribution. The insured will receive the cash surrender value of the policy. However, when an employee cancels his group coverage by terminating employment, there is no cash surrender value.<sup>65</sup>

Finally, the dual inclusion clauses of section 2042 provide that the proceeds will be included in the decedent's gross estate if they are receivable by his executor, or if they were receivable by a beneficiary but were subject to the exercise of an incident of ownership retained by the decedent.<sup>66</sup> It would appear that the underlying rationale was to render taxable all proceeds which were in fact paid or payable to the estate, or which the insured had the power to make payable to his estate or to himself through the exercise of an incident of ownership. Neither result, however, is possible with respect to the proceeds of an assigned group policy. Even if the employee were to terminate his employment after the assignment, he would not have the power to direct the payment of the proceeds to himself or his estate, nor would he himself have the power to direct the proceeds away from the designated beneficiary.

Dictum in *Estate of John C. Whitworth*<sup>67</sup> would appear to support this view. There, it appeared that the decedent had made an inter vivos transfer of the proceeds of a pension plan. According to the employment contract, "no termination of the employment agreement, by any means whatsoever, would affect [decedent's] . . . rights under the company's pension plan . . ."<sup>68</sup> The Commissioner, in attempting to include the proceeds in the decedent's estate, contended that the decedent had the power to breach the employment contract and thereby terminate any rights thereunder which had been transferred to his wife.<sup>69</sup> The court held that the proceeds were not includible in the estate because of the very terms of the agreement.<sup>70</sup> In dictum, however, the court also stated that the termination of employment was not to be deemed a power of revocation:

To follow respondent's [Commissioner's] reasoning leads to an absurd result not required or permitted in the construction of a statute. To do so would be tantamount to holding that the value of all rights of widows to pension benefits arising under their husbands' employment contracts must be included in their deceased husbands' estates. All employees are able to cease their employment since the abolition of slavery . . . . Indeed, were decision to turn upon the latter point [cessation of employment being a sufficient power of revocation so as to include the proceeds in the gross estate], the value of no widow's right to pension arising

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65. Group life insurance policies usually contain a clause stating that the policy has no loan or cash value. 29 N.Y. Jur. Insurance § 521, at 513 (1963).

66. Int. Rev. Code of 1954, § 2042.

67. 22 CCH Tax Ct. Mem. 177 (1963).

68. Id. at 178.

69. Id. at 180-81.

70. Id. at 181.

under a . . . contract . . . wherein her husband was a party could escape inclusion in the deceased husband's estate.<sup>71</sup>

#### D. *Power To Cancel by Discontinuing Premiums*

An insured under a policy of contributory group insurance may exercise his power to "surrender or cancel" by defaulting in the periodic premium payments while remaining employed. If the insured has assigned the policy, the assignee would not have the right to exercise the conversion privilege since the privilege is exercisable only when the employee terminates his employment,<sup>72</sup> or when the employer terminates the group policy.<sup>73</sup> The assignee, however, will quite naturally seek to fortify his waning beneficial interest by attempting to tender the premium payments himself, in spite of the employee's seemingly contrary intentions. But the tender of these payments, to be effective, must be accepted by the employer. In view of the action of his employer, and in light of the increased cost and effort necessarily expended in receiving and transmitting premium payments from non-employees to the insurer, the employer would tend to discourage such arrangements. In any event, it appears doubtful that the assignee would be capable of compelling acceptance of the premiums by either the employer or the insurer.<sup>74</sup> Therefore, it would seem that the insured in a contributory plan, even though he had assigned the policy, could exercise such control over the policy so as to force a cancellation of the policy. This could be used by the assignor as a device to terminate or render worthless what would otherwise be an absolute assignment, and the power thus construed would constitute an incident of ownership.<sup>75</sup>

In an attempt to remove this stumbling block, an absolute assignment form, which would be signed by the employee, employer, and insurance company, should contain a clause that both the insurer and employer agree to accept tender, from the assignee, of any and all requisite contributions to maintain the insurance under the group policy.

As a result, the insured employee could not affect the rights of the assignee by failing to contribute to the plan since the assignee himself could tender payments to the insurer, which would have to be accepted.

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71. *Id.* at 181 (*dictum*).

72. N.Y. Ins. Law § 161(e).

73. As has been noted previously, the conversion privilege is exercisable only when the master policy is cancelled or where there is a cessation of employment. N.Y. Ins. Law § 161(f).

74. In *Magee v. Equitable Life Assur. Soc'y of the United States*, 62 N.D. 614, 622, 244 N.W. 518, 521 (1932), the court noted that the insurer was not obligated to notify the employee that no further premiums were paid for him by the employer, because the employee could not pay the premiums himself. See *Davis v. Metropolitan Life Ins. Co.*, 161 Tenn. 655, 32 S.W.2d 1034 (1930).

75. It may be said, however, that discontinuing premium payments is not an incident of ownership because the economic benefits could not be rendered payable, nor were they even capable of being rendered payable, to the insured's estate. See text accompanying note 58 *supra*.

E. *Reversionary Interest*

The only example given by the Code of an incident of ownership is a reversionary interest: "[T]he term 'reversionary interest' includes a possibility that the policy, or the proceeds of the policy, may return to the decedent or his estate, or may be subject to a power of disposition by him."<sup>76</sup> Such an incident of ownership may arise either from the express terms of the policy, from an assignment, or by operation of law.<sup>77</sup> The Code also provides that the proceeds will only be includible in the gross estate "if the value of such reversionary interest exceeded 5 percent of the value of the policy immediately before the death of the decedent."<sup>78</sup> The possibility of reversion is valued by the use of mortality tables and actuarial principles<sup>79</sup> and, if the potential reversion is to take effect after an estate for life, the value varies directly with the age of the transferee at the time of the transfer.<sup>80</sup> The decedent's estate will, therefore, include, for estate tax purposes, the entire proceeds of the policy regardless of whether these proceeds were *in fact* a part of his estate.<sup>81</sup>

There does not seem to be any doubt that the deceased will be said to have had a reversionary interest if the assignment or policy contains a provision that the proceeds will be payable to the insured's estate if the beneficiary predeceases him.<sup>82</sup> However, where there is a sufficient number of family members, the five-per-cent rule can be eliminated by sheer numbers. If there

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76. Int. Rev. Code of 1954, § 2042(2).

77. A reversion by operation of law results only from an incomplete vesting, as, for example, where the contingent interest of a beneficiary fails to become a vested one. A transfer of a reversionary interest, whether this interest has its roots in the policy or in an operation of law, will be taxable unless excepted by the five-per-cent rule. Dicus, *Some Implications of the 1954 Code for Estate Planning*, 32 *Taxes* 938, 939 (1954).

78. Int. Rev. Code of 1954, § 2042(2).

79. *Ibid.* For example, assume that the decedent assigned a \$50,000 individual policy to his wife, but retained a possibility of reverter in favor of his estate if she should predecease him. At the date of the decedent's death, his wife was forty-eight years old and the cash surrender value of the policy was \$37,500. (In determining the amount of the reversionary interest, the face amount of the policy is not relevant, but rather the value of the policy immediately before the insured's death, i.e., the cash surrender value. *Bank of New York v. United States*, 115 F. Supp. 375, 384 (S.D.N.Y. 1953).) The value of the reversion would be \$17,138.63, almost 46% of the cash surrender value. See 26 C.F.R. § 20.2031-7(d),(f) (1961).

80. 26 C.F.R. § 20.2031-7(d) (1961). If there is only one transferee, the lowest value of the reversionary interest would be 12.838%. 26 C.F.R. § 20.2031-7(d), (f) (1961). Therefore, successive life estates would have to be created to circumvent the five-per-cent rule. The value of the reversionary interest when there are successive life estates is computed on the basis of the Makehamized mortality table which appears as Table 38 of the United States Life Tables and Actuarial Tables 1939-41, published by the United States Department of Commerce, Bureau of Census. 26 C.F.R. 20.2031-7(e) (1961).

81. Doyle, *Life Insurance in Estate Planning*, 22 *Ohio St. L.J.* 258, 259-60 (1961).

82. Where there is no designated beneficiary at the death of the insured, the insurance company may have the option of paying the proceeds to certain members of the insured's family. N.Y. Ins. Law § 161(1)(d). Seemingly, such a provision would lessen the possibility that the proceeds of the policy would return to the decedent's estate.

are not enough contingent takers, the insured may make use of an exempt ultimate taker, such as a charity.<sup>83</sup>

#### V. TRANSFER IN CONTEMPLATION OF DEATH

The Regulations<sup>84</sup> point out that the insurance section of the Code<sup>85</sup> is not exclusive and that the proceeds of life insurance may be includible under other sections.<sup>86</sup> One such section concerns transactions made "in contemplation of death."<sup>87</sup>

Under section 2035, any interest in property gratuitously transferred "in contemplation of death" within three years of the transferor's death is included in his gross estate.<sup>88</sup> Whether the transfer is in fact "in contemplation of death" depends upon the principal motive<sup>89</sup> of the transferor at the time of such transfer.<sup>90</sup> If the motivating force is to reduce estate taxes, the transfer is "in contemplation of death."<sup>91</sup>

Any transfer made more than three years before death, regardless of intent, "shall [not] be treated as having been made in contemplation of death."<sup>92</sup> It should be noted that there exists a "rebuttable statutory presumption"<sup>93</sup> that the transfer was made "in contemplation of death"<sup>94</sup> if made within three

83. Gresham, *Estate Planning Under 1954 Internal Revenue Code*, 94 *Trusts & Estates* 1026 (1955).

84. 26 C.F.R. § 20.2042-1(a)(2) (1961).

85. *Int. Rev. Code of 1954*, § 2042.

86. See P-H *Fed. Est. & Gift Tax Rep.* ¶ 120420 (1964).

87. *Int. Rev. Code of 1954*, § 2035.

88. 26 C.F.R. § 20.2035-1(a) (1961).

89. *Allen v. Trust Co.*, 326 U.S. 630, 635-36 (1946); *Lockwood v. United States*, 181 F. Supp. 748 (S.D.N.Y. 1959); *Gross v. Rothensies*, 65 F. Supp. 92 (E.D. Pa. 1946).

90. "The phrase 'in contemplation of death' . . . does not have reference to that general expectation of death such as all persons entertain. On the other hand, its meaning is not restricted to an apprehension that death is imminent or near. A transfer in 'contemplation of death' is a disposition of property prompted by the thought of death [if] . . . (1) made with the purpose of avoiding death taxes, (2) made as a substitute for a testamentary disposition of the property, or (3) made for any other motive associated with death." 26 C.F.R. § 20.2035(1)(c) (1961). See *Estate of Hull v. Commissioner*, 325 F.2d 367, 369 (3d Cir. 1963); *Tait v. Safe Deposit & Trust Co.*, 74 F.2d 851, 854 (4th Cir. 1935).

91. *Vanderlip v. Commissioner*, 155 F.2d 152 (2d Cir.), cert. denied, 329 U.S. 728 (1946); 26 C.F.R. § 20.2035-1(c) (1961).

92. *Int. Rev. Code of 1954*, § 2035(b).

93. P-H *Fed. Est. & Gift Tax Rep.* ¶ 120350.

94. There have been provisions taxing transfers made in contemplation of death in each of the Revenue Acts since 1916, when an estate tax was first imposed. The United States Supreme Court, in *Heiner v. Donnan*, 285 U.S. 312 (1932), declared unconstitutional the provision in § 302(c) of the Revenue Act of 1926 that transfers made within two years of decedent's death were conclusively presumed to have been made in contemplation of death. Section 803(a) of the Revenue Act of 1932 restored the rebuttable presumption. The language used by the present Regulations is that any transfer made within such three year period "is deemed to have been made 'in contemplation of death', unless shown to the contrary." 26 C.F.R. § 20.2035-1(d) (1961).

years prior to death, thus placing the burden of coming forward with rebuttal evidence on the estate.

#### A. *Assignment of the Policy*

Any transfer made more than three years before death, regardless of intent, "shall [not] be treated as having been made in contemplation of death."<sup>95</sup> Given such a transfer, the question arises whether group insurance is inherently includible in the gross estate of the insured. At least one author is of the opinion that, since group term coverage is usually of a one year nature, the assignment would have to be annually renewed, and, hence, the assignment would always come within the three year restriction.<sup>96</sup>

Term insurance has been defined as insurance which will pay a benefit for only a stipulated period of time.<sup>97</sup> At the end of the agreed term, a new contract of insurance would be required to continue the coverage. It is submitted that group insurance has been incorrectly categorized as term insurance.

In *Frey v. Feller*,<sup>98</sup> the insured employee irrevocably designated the plaintiff as beneficiary under a policy issued by the Travelers Insurance Company. The employer terminated its contract with Travelers and entered into a new group contract with Metropolitan Life Insurance Company.<sup>99</sup> The employee filed a change of beneficiary request under the new contract.<sup>100</sup> The court, in holding for the newly designated beneficiary, stated that

the insurance was . . . term insurance of one year duration renewable each year. The premium paid for no more than the coverage afforded for the one year period. At the end of the year the only interest which remained to the Employee or the Company [employer] was the right to renew, upon a premium which could be newly computed.<sup>101</sup>

It appears that the court was correct in its decision, but for the wrong reason. With the substitution of insurers, there was a cancellation of the Travelers contract, thus terminating all of the plaintiff's rights as an irrevocable beneficiary. The court, however, overlooked this fact and also the fact that a group insurance contract had previously been held not to be of a one year renewable nature.<sup>102</sup> Rather, it is a *continuing contract* conditioned upon the payment of the yearly adjusted premium and upon the maintenance of a minimum number of employees in the group.<sup>103</sup> Excluding the latter, it would

95. Int. Rev. Code of 1954, § 2035(b).

96. McCarthy, *Personal Life Insurance: Transfers of Ownership of Life Policies; Application of Federal Tax Liens to Life Insurance*, N.Y.U. 18th Inst. on Fed. Tax 435, 443 (1960).

97. *Doty v. American Nat'l Ins. Co.*, 350 Mo. 192, 203, 165 S.W.2d 862, 869 (1942).

98. 127 N.Y.S.2d 302 (Sup. Ct. 1953).

99. *Id.* at 304.

100. *Ibid.*

101. *Id.* at 305.

102. *Mulligan v. Travelers Ins. Co.*, 280 App. Div. 764, 113 N.Y.S.2d 659 (1st Dep't), reversing mem. 113 N.Y.S.2d 77 (App. T. 1952) (per curiam), aff'd mem., 306 N.Y. 805, 118 N.E.2d 820 (1954).

103. "[T]here was created a conditional but indeterminate contract of insurance for life [and] . . . this is true for the reason that . . . the employer, just as in any other policy

seem that group insurance, covering an employee during the period of employment, differs from individual insurance only in that the amount of premiums is subject to change reflecting the group's prior history. Consequently, both individual and group insurance are continuing contracts with the condition precedent of the payment of the established premium.

In *Mulligan v. Travelers Ins. Co.*,<sup>104</sup> the plaintiff attempted to apply Section 161 of the New York Insurance Law to a master policy issued in 1931.<sup>105</sup> The policy provided that, if the beneficiary died before payment of the proceeds to him, the proceeds would become payable to a blood relative. Section 161, which took effect on January 1, 1940, provided that the proceeds would be payable to the designated beneficiary. The insured died in 1945 and the beneficiary died in 1946, before a disbursement of the proceeds had been made.<sup>106</sup> The appellate term held that the statute was binding on the policy, thus giving section 161 an apparent retroactive effect. The inference is that the court considered the master policy to be of a renewable term nature and, therefore, section 161 became applicable to the master policy as of its yearly renewable date in 1940.

In reversing, the appellate division<sup>107</sup> made specific reference to the dissent of Justice Hofstadter of the appellate term<sup>108</sup> who, maintaining that section 161 was not applicable to the 1931 policy, stated: "Nor is the master policy a new policy issued annually because renewed each year by payment of an adjusted premium."<sup>109</sup>

The court of appeals, in affirming, did not alter the established law of New York that a group policy is a continuing contract.<sup>110</sup> As early as 1925, it had been decided that, "although the [group] policy is renewable from year to year, the original policy is continued in force by the payment of the premiums."<sup>111</sup> Therefore, an absolute assignment of a group policy does not require a yearly renewal of the transfer and is not made "in contemplation of death" if three years have elapsed since the assignment.

#### B. *Payment of Premiums*

Despite the fact that it is made more than three years prior to death, the transfer may still have to hurdle the "contemplation of death" obstacle if the insured continues to pay premiums after assignment. Generally, the pre-

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of life insurance, was clothed with the absolute right to maintain the insurance from year to year upon payment by it of the rates as annually fixed by the insurance company." *Johnson v. Metropolitan Life Ins. Co.*, 52 Ga. App. 759, 762, 184 S.E. 392, 394 (1936).

104. 280 App. Div. 764, 113 N.Y.S.2d 659 (1st Dep't), reversing mem. 113 N.Y.S.2d 77 (App. T. 1952) (per curiam), aff'd mem., 306 N.Y. 805, 118 N.E.2d 820 (1954).

105. 113 N.Y.S.2d at 79 (dissenting opinion).

106. *Id.* at 79-80 (dissenting opinion).

107. 280 App. Div. 764, 113 N.Y.S.2d 659 (1st Dep't 1952) (memorandum decision).

108. *Ibid.*

109. 113 N.Y.S.2d at 80 (dissenting opinion).

110. 306 N.Y. 805, 118 N.E.2d 820 (1954) (memorandum decision).

111. In the Matter of Estate of Johnson, 124 Misc. 493, 501, 203 N.Y. Supp. 655, 658 (Surr. Ct. 1925). Accord, *Franklin v. Northern Life Ins. Co.*, 4 Wash. 2d 541, 555, 104 P.2d 310, 318 (1940).



mium payment test was eliminated by the 1954 Code.<sup>112</sup> It has been suggested, however, that the test is still applicable since payments made after assignment and within three years of the decedent's death may be considered by the Commissioner to have been made "in contemplation of death."<sup>113</sup> If the payment of premiums by decedent three years after assignment and yet within three years of death are "in contemplation of death," it is not clear what amount will be included in the estate. It has been suggested that the amount included will equal: (a) the amount of the premiums; or (b) the entire proceeds of the policy; or (c) a proportionate amount of the proceeds attributable to such premiums.<sup>114</sup>

The sole authority for raising this question is *Liebmann v. Hassett*.<sup>115</sup> In that case, decedent assigned a policy to his wife two years before his death, thus raising an inference of a transfer "in contemplation of death." Since the assignee had paid the two premiums during the period between assignment and death, it was held that the face value of the policy *less the proportionate amount of the insurance purchased with the two premiums paid by the assignee* was to be included in the gross estate.<sup>116</sup> The first application of this case would clearly warn that, for three years immediately after an assignment, the transferee should make the premium payments so that, if the assignor should die within the three year restrictive period, some portion of the proceeds will be excluded from the gross estate even though the transfer is deemed to have been made "in contemplation of death."<sup>117</sup>

The converse reasoning of the *Liebmann* case would seem to be authority for concluding that the Commissioner would attempt to include the proportionate amount of the proceeds purchased by the assignor within three years of his death.<sup>118</sup>

Such premium payments might, however, be subject to a different judicial opinion. In *Estate of Achille F. Israel*,<sup>119</sup> the decedent established an unfunded insurance trust into which he paid all the premiums until his death in 1939. The Commissioner attempted to include the premiums paid by the deceased in the gross estate as payments made "in contemplation of death," but the court rejected this theory, stating:

We conclude that in paying the premiums here involved, the decedent was actuated solely by the intention of preserving the integrity of the trust corpus, and not by

112. See notes 23-27 *supra* and accompanying text.

113. E.g., Brown & Sherman, *Payment of Premiums as Transfers in Contemplation of Death*, 101 *Trusts & Estates* 790 (1962). See Gresham, *supra* note 83.

114. Moses, *Irrevocable Life Insurance Trusts Can Be Attractive Estate Planning Tool*, 18 *J. Taxation* 206, 211 (1963).

115. 148 F.2d 247 (1st Cir. 1945).

116. *Id.* at 251.

117. Casner, *The Internal Revenue Code of 1954: Estate Planning*, 68 *Harv. L. Rev.* 222, 255 (1954).

118. Casner, *supra* note 117, at 255; Dicus, *supra* note 77, at 941-42; Mannheimer, Wheeler & Friedman, *Gifts of Life Insurance by the Insured*, N.Y.U. 13th *Inst. on Fed. Tax* 247, 260 (1955).

119. 3 CCH *Tax Ct. Mem.* 1301 (1944).

any intention or purpose to make such payments as transfers 'in contemplation of death' . . . .<sup>120</sup>

Therefore, whatever else may be included in the gross estate, the premiums themselves will not be.

In *Allen v. Trust Co.*,<sup>121</sup> decedent established two trusts in 1925 to which he assigned property. Learning that the assignment was subject to estate tax because of his power to amend, he released this reserved power in 1937, two years prior to his death. The Supreme Court refused to include the trust in the gross estate, stating that the release in 1937 was merely to perfect the transfer made in 1925.<sup>122</sup> Thus, the inference that the release within three years of death was made "in contemplation of death" was rebutted by a finding that the primary motivation of the settlor was to perfect the prior transfer. Analogously, premium payments within three years of death should also be regarded as relating to, and perfecting the prior assignment of, the insurance policy. It would also seem inconsistent and unfounded to say that the proportionate amount of the proceeds are taxable when the *entire* proceeds are not taxable.

It has been suggested, however, that the use of a funded trust would render the payment of premiums question moot.<sup>123</sup> Where there is a contributory group plan or where the group policy has been converted, the premiums would be paid by income-producing property assigned to the trust at the time of the assignment of the insurance policies. Three years after such dual assignment, neither the policies nor the income-producing property would be within the purview of the "contemplation of death" statute.

In the event that the group policies are not contributory, the use of a funded trust prior to conversion would also be beneficial. With the simultaneous assignment of the policies and property to the trust, and with the ever present possibility that the conversion privilege will be exercised and hence will necessitate the payment of premiums at some date in the future, at least some part, if not the entire three year statutory presumptive period, would have elapsed, thus rendering both the income-producing property and the policies themselves transferred not "in contemplation of death." Therefore, at the time of conversion, section 2035 would have no applicability. In addition, another consequence of the use of the funded trust would be that the proceeds would also be excluded from the wife's estate since she would have neither incidents of ownership nor the ability to transfer any of them.

## VI. CONCLUSION

Before an attempt is made to assign a group policy, there are a number of considerations to be weighed regarding the advisability and feasibility of assigning *any* insurance policy. These include, but are not limited to: the

120. *Id.* at 1307. See *Estate of Hull v. Commissioner*, 325 F.2d 367 (3d Cir. 1963); *Liebmann v. Hassett*, 148 F.2d 247 (1st Cir. 1945); *Estate of Wilbur B. Ruthrauff*, 9 T.C. 418 (1947).

121. 326 U.S. 630 (1946).

122. *Id.* at 633.

123. *Moses*, *supra* note 114, at 211.