Federal Estate Tax: A Possible Exception in the Application of I.R.C. Section 2041 to Testamentary Powers of Appointment Held by Incompetent Decedents

Cheryl Bailey Preston

Follow this and additional works at: https://digitalcommons.law.byu.edu/lawreview

Part of the Taxation-Federal Estate and Gift Commons

Recommended Citation
Available at: https://digitalcommons.law.byu.edu/lawreview/vol1977/iss3/5
Federal Estate Tax: A Possible Exception in the Application of I.R.C. Section 2041 to Testamentary Powers of Appointment Held by Incompetent Decedents

INTRODUCTION

Under section 2041 of the Internal Revenue Code of 1954, property subject to a post-1942 power of appointment, exercisable in favor of a decedent or her estate, will be included—whether exercised or not—in the taxable estate of the decedent who "has" the power at death. Ambiguity in the terms of section 2041 opens a potential for inequitable results when the section is applied to tax the estates of passive donees of testamentary, general powers of appointment who are suffering from permanent mental incompetency which, under state law, prevents them from exercising the power. Where the donee of a testamentary power is incompetent throughout the duration of the power's existence, it is questionable whether the power is "exercisable" and whether the donee, in fact, possesses the power, as required by the section. A study of cases deciding related problems helps to define the issue, while a correlation of applicable legislative and administrative pronouncements with relevant constitutional language and policy considerations exposes the counterbalancing that will be necessary to finally resolve it.

I. THE SCOPE OF THE ISSUE

Although the specific issue under discussion has not been satisfactorily resolved by the courts, opinions related to peripheral problems have revealed the judiciary's limited sympathies for incompetent decedents. In the first of such cases, Hurd v.
POWERS OF APPOINTMENT

Commissioner, decided in 1947, the decedent created a trust and appointed himself cotrustee. As trustee, he had the power to eliminate the share of a beneficiary. The decedent did not resign, was not removed, and was not adjudicated insane, although he was incompetent for eighteen months prior to his death. The court held that the trust was properly included in his estate because “the power existed in his behalf . . . and he could have been removed” as trustee under the terms of the instrument.

Seventeen years later in Round v. Commissioner, the decedent had established three trusts and retained a taxable power in each. The instruments provided that upon the decedent’s incapacity, the corporate cotrustee would become the sole fiduciary. Although the decedent had had a conservator appointed to manage his affairs, the court refused to remove the trust property from his taxable estate. The court interpreted the instruments as requiring permanent incapacity and found that in the absence of a permanent removal — i.e., an adjudication of insanity — the appointment of a conservator “was not the definitive act called for” by Hurd and did not remove the possibility that the decedent could have recovered and resumed his duties as cotrustee.

The decedent in Commissioner v. Noel, the only related United States Supreme Court case, retained a taxable power to designate the beneficiaries of two insurance policies purchased just prior to takeoff on his fatal airplane flight. The Court admitted the practical impossibility of exercising the power while the decedent was in the air but declared it would not allow a decedent’s “fluctuating, day-by-day, hour-by-hour capacity” to determine his tax liability: “Estate tax liability . . . depends on

6. 160 F.2d 610 (1st Cir. 1947).
7. Taxation of the property subject to this power was predicated upon Int. Rev. Code of 1939, ch. 1, § 811(d)(2), 53 Stat. 121 (now I.R.C. § 2038(a)).
8. Under most state laws, a guardian can exercise an inter vivos power on behalf of a ward. See notes 40-41 infra.

The term “guardian” will be treated in this Comment as synonymous with the terms “conservator,” “curator,” “tutor,” and “approval of the court.” See generally F. Lindman & D. McIntyre, The Mentally Disabled and the Law 225 (1961).
9. 160 F.2d at 613.
10. 332 F.2d 590 (1st Cir. 1964).
11. Taxation of the property subject to this power was predicated upon I.R.C. §§ 2036(a) and 2038(a)(2). Id. at 595-96.
12. Id. at 591.
13. Id. at 593.
15. Taxation of the property subject to this power was predicated upon I.R.C. § 2042(2). Id. at 678.
a general, legal power to exercise ownership, without regard to the owner’s ability to exercise it at a particular moment.” 16

An inter vivos power of appointment was involved in Estate of Rebecca Edelman. 17 In this case, the Tax Court stressed the fact that the decedent had not been made a legal ward nor adjudicated incompetent. Under such circumstances, state case law provided that an exercise of an inter vivos power by an incompetent would only be voidable, not void. 18 As a result, Mrs. Edelman retained at death a “valuable property right” 19 which the court held was properly subject to taxation.

Townsend v. United States 20 also involved an inter vivos power of appointment. The decedent received the power in her husband’s will but was unable, physically and mentally, to exercise the power before her own death. The plaintiff contended that the decedent’s incompetency prevented her from “possessing” a taxable power. 21 The court, in dicta, rejected this argument by stating that “it is immaterial under the provisions of [section 2041(a)(2)] whether [the decedent] was...mentally capable of exercising such power.” 22 The court went on to exclude the property subject to the power from the estate because the donor’s will had not been probated before the donee’s death. 23

The Fifth Circuit in Estate of Bagley v. United States 24 refused to exclude a testamentary power of appointment from the taxable estate of a donee who died in a common disaster with the donor. The dissent vigorously opposed “[t]his inequitable result,” 25 alleging it was “not only inconsistent with the rationale of federal estate taxation, but unjust and a deprivation of property without due process of law.” 26

The clearest comments on the subject were made by the

16. Id. at 684.
17. 38 T.C. 972 (1962).
18. Id. at 978 (citing Finch v. Goldstein, 245 N.Y. 300, 157 N.E. 146 (1927)).
19. Id.
21. Id. at 221.
22. Id.
23. The court interpreted state law as requiring a devised estate to vest immediately upon death. It concluded, however, that a power of appointment was not an estate but a personal privilege that would not exist until probate. Id. at 222. State laws in other jurisdictions have not been interpreted to require this result. See, e.g., Estate of Bagley v. United States, 443 F.2d 1266 (5th Cir. 1971) (construing Florida law); Jenkins v. United States, 428 F.2d 538 (5th Cir.) (construing Georgia law), cert. denied, 400 U.S. 829 (1970).
24. 443 F.2d 1266 (5th Cir. 1971).
25. Id. at 1270 (Ainsworth, J., dissenting).
26. Id. at 1271 (Ainsworth, J., dissenting).
Ninth Circuit in *Fish v. United States*; the most direct discussion has been by a federal district court in *Finley v. United States*. These two cases, however, produced conflicting results. In *Fish*, the decedent had the power to demand on a yearly basis the income from a trust. She never exercised or released this power. The Internal Revenue Service included the value of the income in the taxable estate under the lapse provisions of section 2041. Although so urged by the plaintiff, the court refused to address itself to the questions of whether the decedent was incompetent or whether the power could have been exercised by a guardian. The court held that it was "immaterial whether the lapse occurred through a designed failure... or through indifference or incompetency of the decedent."30

In the startling 1975 *Finley* decision, the court declared that the decedent who was incompetent throughout the existence of the power, though never officially so adjudicated nor subjected to a guardian, could not be deemed to have possessed the testamentary power of appointment at her death.31 The opinion, unfortunately, reads as though the court were unaware that it had come to a novel conclusion. The court recognized its conflict with the Ninth Circuit as expressed in *Fish*, but it claimed that *Hurd, Noel, and Bagley* provided sufficient support. The court concluded that the decedent's incapacity was distinguishable from that of the decedents in *Hurd, Noel, and Bagley*. The decedent in *Finley* could not have validly exercised the power, either alone or through a guardian. Her incapacity was "legal,"33 not fluctuating, temporary, or brief; it was not merely physical or situational.34

The decision in *Finley* may not have been as contrary to precedent as it first appears. Although not specifically discussed

27. 432 F.2d 1278 (9th Cir. 1970).
29. 432 F.2d at 1279-80.
30. Id. at 1280.
31. 404 F. Supp. at 204.
32. Id. at 202-03 n.2.
33. By way of a footnote, the Tax Court in Estate of Freeman v. Commissioner, 67 T.C. 202 (1976), suggested that *Finley* could be distinguished from prior cases on the grounds that it involved a legal rather than some other disability. *Id.* at 208 n.9. Presumably, the court felt that the disability in *Finley* was not simply physical or even mental. The difference between a legal disability and a mere physical or mental one has never been fully explored. It could be that a physical disability, as well as one based upon situation, is both entirely an individual matter and one which theoretically could be overcome. On the other hand, a legal disability is imposed by law and is subject to uniform application.
34. 404 F. Supp. at 204.
by the court, the facts, as revealed by the briefs, approach the
fact situation suggested above in which taxation under the
terms of section 2041 would seem most unwarranted. The dece-
dent, Mrs. Whitlock, was mentally incompetent at all times dur-
ing the existence of the power. She had no opportunity, not even
a limited opportunity, to exercise the power. The decedents in
Hurd, Edelman, and Fish each had some time in which they
could have exercised the power. Even Mr. Noel had a few hours
on the plane and Mrs. Bagley a theoretical second in which his
or her power could have been exercised.

Not only was Mrs. Whitlock incompetent throughout the
duration of the power, but she also enjoyed no ownership rights
over the property prior to the creation of the power by her hus-
band's will. In Hurd and Round, the decedents themselves exe-
cuted the trust instruments creating their powers; moreover, the
property had been owned outright by them prior to its being
placed in trust.

Another distinguishing fact is that any attempt by Mrs. Whi-
tlock to exercise her power would have been void, not just voida-
ble. Her power was exercisable only by will, and lack of capacity
renders a will void. On the other hand, under most state laws
an inter vivos power can still be successfully exercised regardless
of capacity, assuming the exercise is not later disclaimed. It was
upon this distinction that the decision in Edelman was based.

Finally, Mrs. Whitlock's power, being testamentary, could
not have been exercised by a guardian acting in her behalf. A
guardian's function is to manage the ward's property during life,
not to control its disposition at death.

A case for the exclusion of the appointive property from a

35. See text accompanying notes 4-5 supra.
36. In Hurd, the decedent was competent for nearly four years during the existence
of the power. 160 F.2d at 611. In Edelman, the decedent was competent for three and one-
half years. 38 T.C. at 974. In Fish, the decedent was competent for two years during the
existence of the power. 432 F.2d at 1279-80.
37. R. Allen, E. Ferster, & H. Weihofen, Mental Impairment and Legal
Incompetency 286 (1968).
38. Finch v. Goldstein, 245 N.Y. 300, 157 N.E. 146 (1927); Restatement of Property
§ 345 (1936).
40. Equitable Trust Co. v. Union Nat'l Bank, 25 Del. Ch. 281, 18 A.2d 228 (1941);
Trust Co. v. McGowan, 323 U.S. 594 (1945) (dealing with guardian's ability to exercise
an inter vivos power); In re Houghton's Estate, 118 Vt. 228, 105 A.2d 257 (1954) (dealing
with guardian's ability to exercise an inter vivos power).
41. R. Allen, E. Ferster, & H. Weihofen, supra note 37, at 283.
decedent's estate would be even stronger if several additional facts could be established. For instance, if a decedent was incompetent at the time the donor's will which created the power was drawn, it could be argued that the donee (1) could not have agreed to the donor's plan for the property;\footnote{For the view that the fact a decedent did not request a gift of the property in question "in no way affects the outcome" of tax disputes, see Peoples Trust Co. v. United States, 412 F.2d 1156 n.5 (3d Cir. 1969). Presumably, a donee who has no capacity to exercise a power is also rendered unable to disclaim it. See I.R.C. § 2518(b)(2) (granting a minor nine months following his attainment of legal capacity to disclaim powers given to him). It may be possible for a guardian to disclaim a testamentary power if the facts establish that the disclaimer will not alter the succession of the property, see Minnehan v. Minnehan, 336 Mass. 668, 671, 147 N.E.2d 533, 535-36 (1958), and that the ward would have disclaimed the power himself if competent.} (2) could not have approved the donor's chosen takers-in-default, and (3) could not have changed her will to exercise the power. Before now, cases have just considered the decedent's incompetency after the power had been put into effect by the donor's death. Moreover, if such a decedent had attempted an inter vivos exercise of the power or had attempted to execute a will exercising it, a court may be more easily persuaded that taxation would be unwarranted. An official adjudication of insanity or the appointment of a guardian may also affect the result.\footnote{See Round v. Commissioner, 332 F.2d 590, 594 (1st Cir. 1964); Estate of Rebecca Edelman, 38 T.C. 972, 978 (1962); Rev. Rul. 55-518, 1955-2 C.B. 384, 385.}

Although the present weight of precedent leans heavily in favor of taxation in the type of case here postulated, it is by no means clear that taxation is required in every instance.\footnote{The outcome of a pending case in the District Court of the Western District of Pennsylvania, Pennsylvania Bank & Trust v. United States, No. 76-155 (W.D. Pa., filed Feb. 2, 1976), may provide additional insight into the importance of various fact combinations. In that case the decedent, Mrs. Brice, was alleged to have been hopelessly and incurably incompetent beginning six years prior to the donor's death and continuing until her own death. Following the donor's death, she was adjudicated incompetent and a guardian was appointed. The plaintiff claims that this incompetency prevented the decedent from possessing a taxable power of appointment. A will executed by Mrs. Brice ten years before her death and two years before becoming incompetent, however, evidences a calculated release of the power. The will states: "It is not my intention to exercise by any of the provisions of this Will any Power of Appointment which I may have under the Will of my husband, James W. Brice, or any Power of Appointment which I may have." Further, it would appear that the decedent's guardian could have exercised the power during Mrs. Brice's lifetime since it included an inter vivos power to consume.} There

\footnote{A case subsequent to Finley dealing with an analogous problem has failed to resolve the Finley question whether there may be an exception to the application of § 2041.}
are gaps between the cases which have not been fully addressed. The contours of this unresolved issue are not yet defined.

II. THE RESOLUTION OF THE ISSUE

Specifically how the gaps in present law will be, or should be, filled is a matter of some dispute. Reference to the legislative history of section 2041, the interrelation of that section to other sections of the Code, applicable rulings and regulations, certain constitutional language, and policy considerations provide a basis for analysis of the conflicting views.

A. Legislative History

The 1942 amendments to the Internal Revenue Code of 1939 made it clear that Congress was not unaware of the problem of donees under legal disabilities. The amendments included, for the first time, unexercised powers of appointment in the taxable estate unless “the donee of such power is under a legal disability to release such power, until six months after the termination of such legal disability.”45 The Senate Report accompanying the Act summarized this provision, stating that the amendments would be “inapplicable to an existing general power held by a person under legal disability.”46 It is obvious from this language that incompetent donees can hold or possess powers of appointment; otherwise, the specific exclusion of these powers from the scope of the statute would not have been necessary. Since Congress could have excluded powers held by incompetent donees in the current version of the statute, the fact that it did not may indicate a present intent to tax these powers.

In 1951, Congress enacted the Powers of Appointment Act47 for the express purpose of simplifying the treatment of powers created prior to 1942. Under the old law, an unexercised pre-1942 power was subject to some complicated exceptions, including the
exception for persons under legal disability mentioned above. After the change, pre-1942 powers were only taxed if exercised, although post-1942 powers continued to be taxed whether exercised or not. The evils flowing from the old law were described in the Senate Report accompanying the Act: "[M]any such powers [were not] discovered until it [was] too late for the donees to do anything about them. . . . [Tax revenues came] from the unwary or those who [were] powerless to help themselves." The Report, however, went on to approve the treatment of post-1942 powers even though incompetent donees of post-1942 testamentary powers are by definition "unwary" and by state law "powerless to help themselves."

B. Marital Deduction

A thorough examination of the interplay between the marital deduction and powers of appointment is also useful in assessing the likely resolution of this issue. The purpose of the marital deduction was to equalize the incidence of estate tax in community property and common law jurisdictions. In community

48. The rationale for taxing an unexercised power was explained by the dissent in Bagley, 443 F.2d at 1271 (Ainsworth, J., dissenting): "A decedent who has knowingly permitted such a power to lapse at his death has exercised the privilege of directing the course of the property subject to it, as surely as if he had taken the formal steps necessary to exercise the power itself." Another commentator has described a taxable unexercised power as a power which the holder "refrains from exercising." Allen, supra note 3, at 17.

The degree of volition necessary is an interesting question. In a case concerning a pre-1942 power (where exercise is a prerequisite to taxation), the court refused to hold that the decedent had exercised the power when his attempt was a "complete nullity which from its very inception was devoid of legal significance." Estate of Edith Wilson Paul, 16 T.C. 743, 749 (1951). This is true, the court reasoned, especially when the attempt was nullified not just by a unique local law but also by the law in numerous common law jurisdictions. If an attempt by an incompetent or his guardian would not be an exercise of the power, it follows that inaction in such circumstances would not equal a forbearance from such exercising.


50. Courts have demonstrated a tendency to be unsympathetic with the "unwary," however. In Estate of Freeman v. Commissioner, 67 T.C. 202 (1976), the Tax Court refused to exempt from taxation the value of trust property even though the decedent was totally unaware of his power to terminate the trust and withdraw the property.

51. I.R.C. § 2056.

52. Northeastern Nat'l Bank v. United States, 387 U.S. 213, 219 (1967); United States v. Stapf, 375 U.S. 118, 128-29 (1963). Excluding testamentary powers qualifying for the marital deduction in the donor's estate from the taxable estates of incompetent donees will not create a benefit in common law states greater than that allowed in community property states. Since a surviving spouse receives community property outright and, if incompetent, may dispose of it in voidable transactions or through a guardian, there is no equivalent situation in community property states.
property states, the surviving spouse is entitled to one-half of the community property tax free. Using the marital deduction, a surviving spouse in a common law state can receive an amount of property equal to the larger of one-half of the decedent's estate or $250,000 without the imposition of a tax. To qualify for the marital deduction, property left to the spouse must be subject to her ultimate control. A general power of appointment trust is a device frequently used to qualify property for the marital deduction without thrusting the burden of managing the property on the surviving spouse. In creating a power of appointment trust with the marital deduction in mind, the parties are usually willing to accept an inevitable tax on the donee's estate in order to avoid a tax on the donor's estate. Generally, the husband dies first, and his estate is much larger; absent the marital deduction, the progressive estate tax would impose a greater burden upon his estate than upon his wife's estate. Deferment of the tax also means the use of tax dollars in the interim and, frequently, a reduction in tax caused by depletion of the taxable property.

The Internal Revenue Code does not state that section 2041 (governing general powers of appointment) and section 2056 (governing the marital deduction) are to be reciprocal in effect. However, "Congress' intent to afford a liberal 'estate-splitting' possibility to married couples, where the deductible half of the decedent's estate would ultimately—if not consumed—be taxable in the estate of the survivor, is unmistakable."
If powers otherwise qualifying for the marital deduction in the donor's estate would escape taxation in the donee's estate should the donee become incompetent, the Service would, no doubt, take an interest in foreclosing the use of the marital deduction in such circumstances. If the Service chose to deny the marital deduction in the donor's estate whenever the donee was incompetent—either unable to exercise the power at all or without the help of a guardian—it could do so under the literal language of existing regulations. One of the specific prerequisites for the marital deduction stated in the regulations is that the power of appointment be exercisable by the surviving spouse "alone and in all events." At least one court has interpreted this language as precluding the use of the marital deduction when a guardian would be required to effectively exercise the power.

An understanding of the marital deduction also provides useful insight into the intent of the parties in creating powers of appointment. This intent has significant bearing upon the equities of individual cases. When estate plans are the product of the mutual efforts of a husband and wife, the takers-in-default listed in the husband's will are probably the wife's choice as well. There is generally no incentive for her to exercise the power even if she were capable of doing so. If couples so intend, they should be able to plan for maximum tax benefit without fear that the use of the marital deduction would be foreclosed when a guardian would be required to exercise the power.

The Service has thus far refused to interpret the "alone and in all events" language of the regulation as precluding use of the marital deduction when the surviving spouse cannot exercise her power due to incompetency. Rev. Rul. 75-350, 1975-2 C.B. 367, states that "[t]he phrase in all events does not refer to those events that State law has determined to be sufficient to deprive a person of control of his or her property during a period of physical or mental incompetency." Id. at 368. The reason for this, as given by the ruling, is that anyone could possibly become incompetent at sometime; consequently, no power of appointment would ever qualify for the deduction. The allowance or denial of the marital deduction, however, must be predicated upon facts known at the donor's death. See Jackson v. United States, 376 U.S. 503, 508 (1964). Alternatively, a change in status of the donee within the statute of limitations could, if sufficiently permanent, be the basis for recomputing the tax. See, e.g., Finley v. United States, 404 F. Supp. 200, 201 (S.D. Fla. 1975), appeal dismissed, No. 76-1459 (5th Cir. May 24, 1976).

"Takers-in-default" are the persons designated by the donor to receive the property after the donee's death if the power is not exercised by the donee.
of the marital deduction will be automatically precluded by the incompetency of the survivor.\footnote{61}

\section*{C. Administrative Pronouncements}

\subsection*{1. Rulings}

Though congressional intent may be variously construed, the Service has left no doubt as to its view of when a decedent's estate should be taxed. In Revenue Ruling 55-518,\footnote{62} the Service first announced its position that a decedent possessed a taxable power of appointment even though she was incompetent "at all times" during the existence of the power.\footnote{63} The ruling, however, dealt with an inter vivos power that was exercisable by the decedent with approval of the court. Although the ruling declared that taxation was predicated upon the existence of the power distinguishable from the capacity to exercise it,\footnote{64} the particular facts of the ruling imply a relationship to capacity because the power was still exercisable with approval of a court.\footnote{65}

Revenue Ruling 75-350\footnote{66} is particularly on point. There the Service concluded that a testamentary power of appointment created in the husband's will is included in the wife's estate notwithstanding both her incompetency at all times during the existence of the power and her legal inability under state law to exercise it: "In the absence of a stated condition in the instrument requiring termination of the power of appointment, the practical inability of the wife to exercise it (due to her legal incapacity) did not affect the existence of the power at her death."\footnote{67}

The Service suggests in Revenue Ruling 75-350 the comparison between appointive property and property owned outright. The ruling correctly asserts that no form of incapacity exempts property owned outright from the throes of estate tax.\footnote{68} It is, however, possible to distinguish property held outright and prop-
property subject to a testamentary power of appointment. First, the identity of the ultimate takers of the property owned outright is determined, if there is no valid testamentary document, by the laws of intestate succession. The decedent's blood relatives will generally receive the property. In the case of appointive property, however, the donor's will which created the power will frequently designate takers-in-default who might not bear the remotest relationship to the decedent. Second, disposal of property owned outright is not limited to testamentary disposition. Inter vivos transactions entered into by incompetents, such as contracts to sell or gifts, are generally only voidable. Further, such transactions can be validly completed by a guardian. Any attempted exercise of a testamentary power of appointment by or on behalf of an incompetent would be totally ineffectual.

2. Regulations

While the regulations make no direct statement on the issue, they do provide useful insight into the necessary prerequisites for taxation. Although not readily apparent on an initial reading of the statute, not every general, vested, post-1942 power of appointment "exists" for tax purposes. For instance, a power "by its terms" conditioned upon an event or contingency that did not in fact occur is not included in the taxable estate under the regulations. Powers subject to a binding agreement prohibiting their exercise are also not included. Consequently, the broad sweeping language of the statute cannot be taken literally.

Of even greater significance is the fact that the statute has been interpreted not to tax a power invalidated by certain state laws. The courts as well as the regulations recognize that in some contexts an interest must be valid under state law before it can be subjected to federal estate tax. Although invalidation by state testamentary capacity and guardianship laws has never suf-

69. See notes 37-41 supra.
faced to remove a power from taxation, it is arguable that it should. The dissenting opinion in Bagley somewhat reflected this analysis. In distinguishing a prior case, the dissent asserted:

If, as a matter of state law, any document executed [by the donee] could have had no present or future legal effect, the Court would have had to conclude that [she] died without ever having had the privilege of disposing of the property, and hence that the value of the property could not be taxed to her estate.74

D. Constitutional Language

A constitutional look at the problem, framed in both direct tax and due process terms, has been suggested in several cases.75 The Constitution prohibits a direct property tax levied without apportionment.76 The estate tax is said to avoid this prohibition because it is an excise tax levied on an action, privilege, or event rather than directly on the property. It has been argued that when the decedent is deprived of any possibility of control, the estate tax loses its excise quality and becomes a prohibited direct tax upon the appointive property.78 In recent times, courts have consistently rejected this direct tax argument.79 They have had no problem conceptualizing the estate tax as a levy upon the hap-

73. The important question, under the current state of the law, is whether testamentary capacity and guardianship laws wipe a power out of existence or just prohibit its exercise. If it is the latter, the power is not invalidated, though nullified and, as such, could still be a taxable interest. Taxation would then be predicated on whether the federal statute is interpreted as taxing only viable powers.

74. 443 F.2d 1266, 1271 (5th Cir. 1971) (Ainsworth, J., dissenting).

75. In Finley, the court's holding obviated any need to address the constitutional argument raised by the plaintiff. 404 F. Supp. at 204 n.3. The plaintiff's failure to raise constitutional objections in a timely manner precluded judicial determination of them in Edelman, 38 T.C. at 978-79, and in Freeman, 67 T.C. at 206 n.3. The majority in Bagley ignored the constitutional implications raised by the dissent. See 443 F.2d at 1271 (Ainsworth, J., dissenting).

76. U.S. CONST. art. 1, § 9, cl. 2.


79. For a recent and clear denunciation of this argument, see Estate of Freeman v. Commissioner, 67 T.C. 202, 206-07 (1976).
pening of an event, namely death, or upon the receipt of the property by the survivor.80

Another constitutional argument is that the donee’s estate is, in effect, improperly taxed for the exercise of the donor’s privilege. When the takers-in-default are designated in the donor’s will and the donee cannot effectively appoint others, the donor is never divested of control over the property. The Supreme Court has invalidated a state income tax law that included a wife’s income with the husband’s for tax purposes, holding that “any attempt . . . to measure the tax on one person’s property . . . by reference to the property . . . of another is contrary to due process of law.”81 This argument again assumes that the basis of the estate tax is control by the decedent. If, however, the event of death or the maturation of the beneficiaries’ interest accrues the tax, the argument fails. It would seem, though, that in such instances the tax should be extracted from the value of the property and not from the residual of the donee’s estate.82

E. Policy Considerations

When, as in this instance, the cases have left doubt as to what result would be required by law and that doubt is not eliminated by an examination of legislative history, related sections of the Code, rulings, regulations, or constitutional language, it is helpful to reduce the problem to policy terms. Considerations of judicial economy, ease of application, and fairness are especially relevant here.

Courts are particularly sensitive to the administrative burdens suggested by making taxation turn on the competence of the decedent. In a footnote, the Fish court commented, “We note parenthetically that if the position contended for by the taxpayer were adopted, the result would be an open invitation to contest

80. United States v. Manufacturers Nat’l Bank, 363 U.S. 194, 198 (1960); Estate of Sanford v. Commissioner, 308 U.S. 39, 43 (1939); Tyler v. United States, 281 U.S. 497, 502-04 (1930); Knowlton v. Moore, 178 U.S. 41, 57 (1900); Commissioner v. Clise, 122 F.2d 998, 1001 (9th Cir. 1941). The tendency in these cases is to evaluate the tax from the point of view of the ultimate takers of the property. Their interest ripens at the death of the previous owner regardless of her competency or her control over the property. Evaluating the tax from the position of the takers is not inappropriate. It is they who can be made liable for the amount of the tax under I.R.C. § 2207; the decedent is beyond the reach of the Internal Revenue Service at last.


82. I.R.C. § 2207 allows the executor to require the takers of the property to pay the tax thereon “[u]nless the decedent directs otherwise in his will. . . .” Unfortunately, clauses providing for the payment of the estate taxes out of the residuary of the estate or some other fund are very common.
the competency of the decedent in every similar case. . . . "83 Similarly, in Noel, the Supreme Court shunned the suggestion that tax law should be based on tenuous and fluctuating circumstances,84 possibly because such criteria would require extensive litigation. In Bagley, the court refused to tie taxation to the probate of the donor's will possibly because the court interpreted congressional intent to mean that the delays and inconsistencies of probate also render it "so tenuous"85 a basis for taxation.

One response to the argument of administrative convenience would be to limit special treatment to estates of decedents whose disability was not fluctuating but permanent throughout the period in question. Practical disability may well be too variable, short-term, and temporary to be the basis of taxation; legal disability would be a more easily administered criterion. Of course, posthumously proving the lack of capacity necessary to establish legal disability could be most challenging.86

Another policy concern is that of simplicity of application. When it changed the treatment of pre-1942 powers, Congress stated that the treatment of post-1942 powers was already simple, clear-cut, and easy to apply.87 Although special treatment for incompetent decedents caught in the certain pattern of circumstances described in this Comment would add one more complication to the law, it would be far from the only complication that has been allowed under existing law. As discussed above,88 there are exceptions carved out for powers expressly subjected to contingencies, restricted by binding agreements, or invalidated by state law.

Finally, it runs amiss of our sense of justice to tax the estate

83. 432 F.2d at 1280 n.3.
86. In the past, the Commissioner has been willing to stipulate to the decedent's incompetency, thus avoiding the problem of proving capacity. If the decision of the court could turn upon the decedent's competency, this spirit of cooperation would be dispelled. Some of the problems involved in proving capacity are illustrated in R. ALLEN, E. FERSTER, & H. WEIHOFEN, supra note 37. Appointment of a guardian, involuntary hospitalization, and determination of a contractual incapacity during the decedent's life are not conclusive of a lack of testamentary capacity. Id. at 253-54, 291. In recognition of these problems perhaps, the Louisiana Civil Code, art. 403, provides that the validity of acts cannot be contested after death on grounds of insanity unless the decedent's condition (1) was pronounced or an adjudication thereof petitioned while he lived, (2) was not manifest until ten days before his death, or (3) can be proved by the act itself. LA. CIV. CODE ANN. art. 403 (West 1952).
88. See text accompanying notes 71-72 supra.
of a decedent for property from which she received no prior enjoyment\textsuperscript{89} and over which she could exercise no control. The dissent in \textit{Bagley} found it inequitable to tax property when there was no opportunity for the decedent to alter its disposition.\textsuperscript{90} The true injustice, however, does not lend itself to remedy through the tax laws. The husband's takers-in-default, not the persons desired by the decedent, obtain the property whether the decedent's estate is taxed for the property or not. If the tax amount is extracted from the value of the appointive property, the passage of the property through the estate causes little harm, particularly to the decedent.

\section*{III. Conclusion}

An exception to the strict application of section 2041 in cases involving permanently incompetent donees of testamentary powers is arguably justified and may find acceptance in the courts. The weight of precedent favors taxation regardless of circumstances, but no case besides \textit{Finley} directly addresses these exceptional facts. Congressional statements intimate a sympathy for unwary decedents and those under legal disabilities, but the wording of the statute contains no clear protection for them. The rulings insist upon taxation while the regulations, on the other hand, open a slim possibility for exception. Such an exception's appealing sense of fairness and justice is not well supported by specific constitutional mandates and must be weighed against the policies of administrative convenience and simplicity of application. The greatest concern of estate planners, though, is probably the effect such an exception would have on the use of the marital deduction. There is the chance that exclusion of appointive property in donees' taxable estates will automatically trigger denial of the marital deduction in donors' estates, even though the use of the marital deduction would obtain a greater tax savings overall. Most importantly, though, those involved in the planning stages of estates should be aware of the possibility that an exception exists, the exact parameters of which are unknown.\textsuperscript{91}

\textsuperscript{89} Of course, a power of appointment trust that qualifies for the marital deduction will include a right to the income of the trust payable at least annually. Unless the right to the income is allowed to lapse, the donee definitely receives a benefit from the property during her life.

\textsuperscript{90} 443 F.2d at 1270-71 (Ainsworth, J., dissenting).

\textsuperscript{91} Rev. Rul. 75-351, 1975-2 C.B. 369, discusses the parallel problem of a minor donee of a power of appointment. According to the ruling, a minor's estate includes a testamen-
tary power of appointment although, by reason of local law, the minor was precluded from executing a valid will and thereby from exercising the power. The incapacity of a minor can only be distinguished from the facts treated by this Comment on the basis of permanence. In the rare but possible situation where the donor of the power had reason to know at the time the power was drafted that the minor donee would never gain capacity—*i.e.*, if he were suffering from a terminal illness—the equities bearing upon a decision to tax the minor's estate for the appointive property would follow those discussed herein.