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ARTICLES

TESTAMENTARY SUBSTITUTES: RETAINED INTERESTS, CUSTODIAL ACCOUNTS AND CONTRACTUAL TRANSACTIONS—A NEW APPROACH*

SIDNEY KWESTEL**
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INTRODUCTION

Most legal systems have provided some degree of economic protection for a surviving spouse in the face of a decedent's efforts at disinheritance.¹ Virtually every noncommunity property state in the

1. Under Jewish law, at least as early as the Talmudic period, a widow had the indefeasible right to continued maintenance and payment of the amount provided in the "ketubah." See 16 ENCYCLOPAEDIA JUDAICA 491-95 (1972). The "ketubah" guaranteed a wife upon her husband's death a minimum of two hundred "zuz" if she had not been married previously and one hundred "zuz" if she had been widowed or divorced. See BABYLONIAN TALMUD, SEDER NASHIM II: TRACTATE KETHUBOTH 51a at 293 (Soncino ed. 1936); 10 ENCYCLOPAEDIA JUDAICA 927-28 (1972). Civil law systems generally protect the surviving spouse, as well as children and sometimes even parents from disinheritance. For example, in France, the doctrine of "legitime," which originated during the thirteenth century, gave the surviving spouse, issue, and parents an interest in inter vivos and testamentary transfers of property. 3 J. BRISSAUD, A HISTORY OF FRENCH PRIVATE LAW § 516 (1968). See Simes, *Protecting the Surviving Spouse by Restraints on the Dead Hand*, 26 U. CIN. L. REV. 1, 2 (1957) (noting similar German device for protecting widows and children called Pflichtteil). Dower, which provided some protection for the widow, is known to have existed in England in Anglo-Saxon times when it was considered a gift and developed into an estate arising by operation of law during the twelfth century. See generally W. MACDONALD, *FRAUD ON THE WIDOW'S SHARE* 279-89 (1960) (elaborating on civil law solutions to disinherited widow problem); Kurtz, *The Augmented Estate Concept Under the Uniform Probate Code: In Search of an Equitable Elective Share*, 62 IOWA L. REV. 981, 982-88 (1977) (providing historical background for augmented estate concept); Cox, *The Right of Election*, 32 ST. JOHN'S L. REV. 164, 164 (1958) (noting evidence of policy supporting widow's right of

United States has forced share or similar legislation² that guarantees a surviving spouse a share in the assets owned by a decedent at the time of his or her³ death.⁴ States enacted such legislation during the past century because they desired to provide greater financial security for the surviving spouse and to compensate the surviving spouse for her contribution to the marriage.⁵

election under Babylonian, Hebraic, Roman, and Saxon law); Cahn, *Restraints on Disinheritance*, 85 U. PA. L. REV. 139, 139-41 (1936) (tracing compulsory share history from ancient legal systems to present).

2. See, e.g., UNIF. PROB. CODE art. 2, pt. 2, 8 U.L.A. 73 general comment (1983) [hereinafter UPC] (describing system designed to protect surviving spouse from disinheritance by decedent's lifetime transfers); R. CAMPFIELD, *ESTATE PLANNING AND DRAFTING* ¶ 2525, at 85 (1984) (noting all separate property jurisdictions and at least one community property jurisdiction have form of spousal protection statute); E. CLARK, L. LUSKY & A. MURPHY, *GRATUITOUS TRANSFERS: WILLS, INTESTATE SUCCESSION, TRUSTS, GIFTS, FUTURE INTERESTS, AND ESTATE AND GIFT TAXATION* 122-24 (3d ed. 1985) (describing dower, elective share, community property, and marital property); Kurtz, *supra* note 1, at 988-90 (noting protections available under American statutes for disinherited widows). These statutes, as well as legislation in community property states, protect both husbands and wives. This article deals with the rights of the surviving spouse only in noncommunity property states.

3. Since women historically have been the focus of protection and statistically women survive men, we use the masculine pronoun in referring to the decedent and the feminine to refer to the surviving spouse.

4. The only jurisdiction that allows a decedent to disinherit a surviving spouse is Georgia, GA. CODE ANN. § 53-2-9 (1982 & Supp. 1988). Georgia law affords a surviving spouse only one year's maintenance. GA. CODE ANN. § 53-5-1 (1982 & Supp. 1988). See generally Note, *Preventing Spousal Disinheritance in Georgia*, 19 GA. L. REV. 427 (1985) (urging extension of equitable property division concept to Georgia probate law in order to recognize each spouse's presumed contribution to family wealth); Note, *The Protection of the Surviving Spouse Against Disinheritance: A Search for Georgia Reform*, 9 GA. L. REV. 946 (1975) (providing history and policy of disinheritance protection). The Supreme Court of South Carolina recently declared that state's dower statute unconstitutional in *Boan v. Watson*, 281 S.C. 516, 316 S.E.2d 401 (1984). The legislature subsequently repealed that provision, S.C. CODE ANN. §§ 21-5-110 to -190 (Law. Co-op. Supp. 1987) (repealed 1985), and enacted new legislation, effective July 1, 1987, which gives the surviving spouse a right to elect one-third of the decedent's probate estate which includes property passing under the decedent's will and by intestacy, although adoption of the relevant sections of the UPC had been recommended. S.C. CODE ANN. §§ 62-2-201, -202, -205 (Law. Co-op. Supp. 1987). See LeBlanc, *The Proposed South Carolina Probate Code*, 36 S.C.L. REV. 511 (1985) (urging adoption of modified version of UPC).

5. For example, in New York the forced share statute became effective on September 1, 1930 and replaced dower prospectively in order to provide greater protection for the widow. N.Y. DEC. EST. LAW § 18(1) (McKinney 1949), Act of April 1, 1929, ch. 229, § 21, 1929 N.Y. Laws 499, 519. As the report of the Foley Commission, which recommended the forced share legislation, stated: "There is a glaring inconsistency in our law which compels a man to support his wife during his lifetime and permits him to leave her practically penniless at his death." N.Y. LEGIS. DOC. NO. 70, COMBINED REPORTS OF THE COMM. TO INVESTIGATE DEFECTS IN THE LAWS OF ESTATES 12 (1928). Governor Franklin D. Roosevelt hailed section 18 as "a new charter of women's rights." See THIRD REPORT OF THE TEMPORARY STATE COMM. ON THE MODERNIZATION, REVISION AND SIMPLIFICATION OF THE LAW OF ESTATES N.Y. Report No. 1.5C, at 117 (1964) [hereinafter REPORT] (giving history of right of election in New York and reporting on need for statute to protect surviving spouses against disinheritance by certain inter vivos transfers). For a discussion of the background of the adoption of N.Y. DEC. EST. LAW § 18, see Barry, *Modernizing the Law of Decedents' Estates*, 16 VA. L. REV. 107 (1929) (praising modernization of New York probate law); Twyeffort, *The New Decedent Estate Law of New York*, 6 N.Y.U. L. REV. 377 (1929) (summarizing and praising changes effected by New York Decedent Estate Law). The REPORT, which recommended the replacement of N.Y. DEC. EST. LAW § 18, was "made upon the assumption that the policy of the State of New York continues to be to

As a general rule, however, a decedent can circumvent forced share legislation because an individual has the right until his death to transfer all of his property to a third person as a gift, usually free of any claim by the surviving spouse. Thus, through lifetime gift transfers of all of his assets, a person can disinherit his surviving spouse.⁶ Courts have attempted to deal with such evasion, under a variety of legal theories, by including certain lifetime transfers—such as Totten trusts, revocable trusts, and joint tenancies—in a decedent's estate for purposes of the surviving spouse's right of election.⁷ These judicial efforts, however, have proved to be

protect the surviving spouse—especially the surviving widow.” REPORT, *supra* at 118 n.13. Only recently, New York expanded the surviving spouse's forced share by granting a right to elect against foreign as well as New York real property. N.Y. EST. POWERS & TRUSTS LAW § 5-1.1(d) (8) (McKinney Supp. 1988) [hereinafter EPTL]. See also W. MACDONALD, *supra* note 1, at 24-25, 161-62 (indicating policy of supporting widows is based upon need to preserve family and historical moral claim); Langbein & Waggoner, *Redesigning the Spouse's Forced Share*, 22 REAL PROP. PROB. & TR. J. 303, 306-10 (1987) (noting need and contribution theories as rationales for forced share system). However, not all commentators agree that expansion of the surviving spouse's right of election is necessary or desirable. See, e.g., Clark, *The Recapture of Testamentary Substitutes to Preserve the Spouse's Elective Share: An Appraisal of Recent Statutory Reforms*, 2 CONN. L. REV. 513 (1970) (noting that legal intervention on behalf of widows is not responsive to demonstrated need); Plager, *The Spouse's Nonbarrable Share: A Solution in Search of a Problem*, 33 U. CHI. L. REV. 681 (1966) (finding small number of disinherited widows in United States and urging adoption of individual need-based system).

6. This was not true under common law dower which generally gave the widow a life interest in one-third of any real property of which her husband was seized at any time during their marriage. Thus, the husband had no power to transfer real property to a third party free of his wife's dower rights. See W. MACDONALD, *supra* note 1, at 59-64. Common law dower, however, provides the major form of protection in only seven states and has largely been replaced with forced or elective share legislation which gives the surviving spouse a right to a fractional share of the decedent's estate, both real and personal. Thirty-four states and the District of Columbia have enacted such forced share legislation. See 7 R. POWELL & P. ROHAN, *POWELL ON REAL PROPERTY* ¶ 971.9 (1988) (inclusion of South Carolina as state which provides dower appears to be erroneous since its dower law was declared unconstitutional and was subsequently repealed (*see supra* note 4)). Today, under the UPC some restrictions have been imposed on certain outright lifetime gifts of property that are viewed as transfers in contemplation of death. The surviving spouse has a right to elect against any transfers made by the decedent within two years of death “to the extent that the aggregate transfers to any one donee in either of the years exceeded \$3,000.00.” UPC § 2-202(1)(iv), 8 U.L.A. 76 (1983). Pennsylvania has an analogous provision except that it applies only to transfers made within one year of death. 20 PA. CONS. STAT. ANN. § 2203(a)(6) (Purdon Supp. 1988). In New York, the surviving spouse may elect against a lifetime gift only if it is a gift causa mortis. See EPTL § 5-1.1(b)(1)(A) (McKinney 1981).

7. The history of judicial attempts to protect the surviving spouse from disinheritance by lifetime transfers and the failure of the vast majority of these judicial efforts to accomplish the desired result have been discussed extensively. See, e.g., REPORT, *supra* note 5, at 119-30 (discussing case law on inter vivos transfers and how such transfers defeat elective right of surviving spouse); W. MACDONALD, *supra* note 1, at 67-144 (discussing different tests applied by courts to inter vivos transfers); Kurtz, *supra* note 1, at 993-1006 (discussing ad hoc judicial safeguards designed to protect surviving spouse from disinheritance that have resulted in inconsistent outcomes); Clark, *supra* note 5, at 518-22 (discussing unsuccessful judicial attempts to curb evasions as reason for statutory solutions); Powers, *Illusory Transfers and Section 18*, 32 ST. JOHN'S L. REV. 193 (1958) (discussing defects of New York Decedent Estate Law section 18 in protecting against disinheritance through inter vivos transfers).

unsatisfactory,⁸ as have similar legislative attempts based on subjective tests.⁹ As a result, some states enacted statutes that establish objective standards to determine whether a lifetime transfer will be deemed a testamentary substitute¹⁰ and, therefore, includible in the estate for purposes of the surviving spouse's right to elect a forced share.¹¹ Pennsylvania¹² and New York¹³ were among the earliest states to provide such statutory protection,¹⁴ and their legislation

8. The experience in New York is representative. The original forced share statutes, such as New York's Decedent Estate Law § 18 (the predecessor of EPTL § 5-1.1), provided for a right of election only against property in the decedent's probate estate—property to which the decedent alone held legal title—and not against any inter vivos transfers, such as revocable trusts or joint tenancies, over which the decedent retained certain powers or control. N.Y. DEC. EST. LAW § 18(1) (McKinney 1949). The dilemma often confronting the courts was how to extend the surviving spouse's right of election to such transfers without invalidating inter vivos dispositions which did not violate the Statute of Wills. *See* REPORT, *supra* note 5, at 118-22 (discussing need and attempt to create a statute balancing rights of surviving spouse with freedom of alienation); Arenson, *Surviving Spouse's Right of Election and Its Application to Testamentary Substitutes*, 20 N.Y.L.F. 1, 4-7 (1974) (discussing leading decisions construing Section 18); Schneider & Landesman, "Life, Liberty — and Dower" *Disharmon of the Spouse in New York*, 19 N.Y.U. L. REV. 343 (1941-42) (analyzing 1930 amendments to New York Decedent Estate Law). The courts in New York suggested three different tests to determine whether a lifetime transfer was subject to the right of election: (i) the retention of control test, *Newman v. Dore*, 275 N.Y. 371, 9 N.E.2d 966 (1937); (ii) the motive for the transfer test, *Bodner v. Feit*, 247 A.D. 119, 286 N.Y.S. 814 (1936); and (iii) the reality of the transfer test, *In re Halpern*, 303 N.Y. 33, 100 N.E.2d 120 (1951). Each test required a subjective evaluation of the facts to determine whether it was satisfied. The inconsistency of these approaches combined with frequently inequitable results spurred the New York legislature to seek statutory reform. *See* REPORT, *supra* note 5, at 122 (finding New York Decedent Estate law in state of confusion and inadequately protecting surviving spouse). As the Bennett Commission (the body appointed to propose a new statutory solution) stated: "The individual decision reached in the individual state is not important. What is important is . . . that the case law has been confusing and that the expectancy of the surviving spouse has not been adequately protected." *Id.* at 123.

9. REPORT, *supra* note 5, at 130-31. *See* Kurtz, *supra* note 1, at 1006-11.

10. We use the term "testamentary substitute" to refer to any lifetime transfer which is subject to the surviving spouse's right of election.

11. *See* REPORT, *supra* note 5, Recommendations to the Legislature, at 24 ("It [the proposed statute] is intended to substitute the objective standards of the provisions of section 18-a [enacted as EPTL § 5-1.1] for the vague and indefinite standards imposed by [case law].") and at 132-38 (noting specific statutes that establish objective standards to determine if lifetime transfers are testamentary substitutes).

12. 20 PA. CONS. STAT. ANN. § 2203(a)(2)-(a)(6) (Purdon Supp. 1988), the successor to 20 PA. STAT. ANN. § 6111 and 20 PA. STAT. ANN. § 301.11(a), was originally enacted in 1947 as section 11 of the Estates Act (hereinafter section 11) (quoted *infra* note 37). The full text of section 2203 is set forth in the Appendix. *See infra* pp. 67-68.

13. EPTL § 5-1.1, which became effective in 1967, applied to testamentary substitutes created on or after September 1, 1966, if the decedent and surviving spouse were married prior to their creation and the decedent executed a will or died intestate on or after that date. The relevant portion of the text of EPTL § 5-1.1 is set forth in the Appendix. *See infra* pp. 68-71.

14. For extensive writings on the historical background which led New York and other states to subject certain lifetime transfers to the surviving spouse's right of election, *see* REPORT, *supra* note 5, at 119-22 (discussing leading New York decisions); W. MACDONALD, *supra* note 1, at 3-19, 67-144 (providing background on need for restraints on alienation); Kurtz, *supra* note 1, at 993-1011 (analyzing history of judicial and legislative safeguards to protect against spousal disinheritance); Clark, *supra* note 5, at 516-22 (examining historical perspective of spousal disinheritance); Amend, *The Surviving Spouse and the Estates, Powers and Trusts*

served as models for the Uniform Probate Code (UPC).¹⁵

The UPC and the New York and Pennsylvania elective share statutes cover, at a minimum, lifetime transfers of property over which the decedent retained certain powers at the time of death.¹⁶ This article analyzes various aspects of such transfers under these statutory schemes and analogous federal estate tax statutes.¹⁷ At the out-

Law, 33 BROOKLYN L. REV. 530 (1966-67) (reviewing problem faced by temporary New York commission charged with recommending changes in New York estate law).

15. UPC § 2-202, 8 U.L.A. 79 (1983). The UPC was approved by the National Conference of Commissioners on Uniform State Laws and the American Bar Association in 1969. The Comment to UPC § 2-202 states that "[s]ome legislatures may wish to consider a simpler approach along the lines of the Pennsylvania Estates Act [§ 301.11(a)]" and that the EPTL "may be suggested as a model." *Id.* Nine states have enacted UPC § 2-202 into law in full or in significant part. *See* ALASKA STAT. § 13.11.075 (1985); COLO. REV. STAT. § 15-11-202 (1987); IDAHO CODE § 15-2-202 (1979); ME. REV. STAT. ANN. tit. 18-A, § 2-202 (1981 & Supp. 1987); MONT. CODE ANN. § 72-2-705 (1987); NEB. REV. STAT. § 30-2314 (1985); N.D. CENT. CODE § 30.1-05-02 (1976 & Supp. 1988); S.D. CODIFIED LAWS ANN. § 30-5A-2 (1984 & Supp. 1988); UTAH CODE ANN. § 75-2-202 (1978). The full text of UPC § 2-202 is set forth in the Appendix. *See infra* pp. 71-73.

16. *See, e.g.*, UPC § 2-202(1), 8 U.L.A. 75-76 (1983) (preventing complete disinheritance of surviving spouse via testamentary substitutes); EPTL § 5.1.1 (b)(1)(E) (McKinney 1981) (providing that property transferred by decedent who retains power to revoke or dispose of principal is subject to surviving spouse's right of election); 20 PA. CONS. STAT. ANN. § 2203(a)(3) (Purdon Supp. 1988) (subjecting property conveyed by decedent with retained power of revocation or right to enjoy the principal to surviving spouse's elective right).

17. Use of the federal estate tax statutes as a model for elective share statutes has been suggested. *See, e.g.*, REPORT, *supra* note 5, at 134 & n.142 (listing authors who argue for this analogy); Haskell, *The Power of Disinheritance: Proposal For Reform*, 52 GEO. L.J. 499, 518 (1964) (proposing that property includible in decedent's gross estate for federal estate tax purposes be subject to the surviving spouse's forced share); Garland, *The "Non-Barrable" Share: Some Comments Regarding a Reappraisal*, 32 ST. JOHN'S L. REV. 218, 224-27 (1958) (explaining logical relationship between federal estate tax statutes and elective share statutes); Simes, *supra* note 1, at 15-16 (arguing that elective share statutes should follow lead of estate tax statutes in reducing likelihood of spousal disinheritance by inter vivos transfers); Note, *Decedent's Estates — Aftermath of Halpern — Suggestions Concerning Statutory Reform*, 27 N.Y.U. L. REV. 306, 312-16 (1952) (showing that a federal estate tax model would reduce spousal disinheritance by making certain inter vivos transfers includible in the net estate for elective share purposes). Only Delaware has enacted forced share legislation providing for a right of election based upon the federal gross estate and apparently no cases have been reported under this provision. DEL. CODE ANN. tit. 12, §§ 901, 902 (1987). Parenthetically, the RESTATEMENT (SECOND) OF PROPERTY § 13.7 statutory note (1986) lists Maryland as also providing for a right of election based upon the federal gross estate, but this appears to be an error. *See* MD. EST. & TRUSTS CODE ANN. §§ 1-101(n), (p), 3-203 (1974 & Supp. 1987).

The drafters of the UPC rejected the "finespun tests of the Federal Estate Tax Law" because tax and UPC objectives are not the same. UPC § 2-202, 8 U.L.A. 78 comment (1983). The UPC is more limited and is "intended to reach the kinds of transfers readily usable to defeat an elective share in only the probate estate." *Id.* In New York, the Bennett Commission noted that the tax provisions could not "easily be lifted bodily" into the estates statute because of the detail and manner in which they were written and believed it would be difficult to obtain support for "such a detailed proposal." REPORT, *supra* note 5, at 134. In the Report's conclusion, the Commission rejected the federal tax approach in part because "it is too inclusive" (e.g., life insurance proceeds would be subject to inclusion) and "it would tend to generate additional litigation and delay the termination of the estate administration." REPORT, *supra* note 5, at 138. Macdonald also rejected the estate tax law as a model because its primary goal of minimizing "concentration of wealth" has "regard neither to the claimant's

set we discuss *In re Estate of Riefberg*,¹⁸ the most recent decision of New York's highest court arising under that state's Estates Powers and Trusts Law (EPTL), section 5-1.1(b)(1)(E), in which the issue was whether a buy-sell provision in a stockholders agreement was a "testamentary substitute" within the meaning of the statute.¹⁹ We consider the ramifications of that decision with respect to contractual arrangements and, more importantly, transfers in trust, where the decedent's power to terminate is retained by operation of law regardless of an express provision in the trust instrument reserving such power.²⁰ We next discuss *Helvering v. Helmholz*,²¹ a United States Supreme Court decision interpreting an analogous federal estate tax statute²² and analyze the effect of the Court's approach, as compared with the approach taken in *Riefberg*, on transfers pursuant to a contract and transfers in trust. The article then addresses several fundamental issues, which *Riefberg* did not raise, concerning the interpretation of elective share statutes that subject lifetime transfers in which the decedent retained certain powers to the surviving spouse's right of election. These issues include the meaning of the terms "transfer," "disposition" or "conveyance," and the treatment to be accorded transfers made for "consideration." Finally, we examine some basic questions concerning the retention of a power focusing particularly on the question of whether these elective share

need nor the equities of the donee" and "is the antithesis of the maintenance and contribution formula" which he proposed. W. MACDONALD, *supra* note 1, at 277.

The New York, Pennsylvania, and UPC statutory schemes are too restrictive and, unlike the federal estate tax scheme, unwisely exclude insurance and retirement plans that can be used to disinherit a surviving spouse. See, e.g., UPC § 2-202(1), 8 U.L.A. 75-76 (1983) (stating insurance proceeds payable to person other than surviving spouse are not subject to right of election); EPTL § 5-1.1(b)(2) (McKinney 1981) (stating insurance proceeds not subject to right of election); 20 PA. CONS. STAT. ANN. § 2203(b)(2) (Purdon Supp. 1988) (providing section analogous to New York's). This is true with respect to qualified employee benefit plans notwithstanding the "spousal annuity rules" adopted as part of the Retirement Equity Act of 1984 because the mandated annuity for a surviving spouse may not equal the value of an elective share in the participant spouse's benefit. See I.R.C. §§ 401(a)(11), 417(b), (c)(2) (1986). Furthermore, inclusion of insurance and employee death benefits, regardless of who is the beneficiary, would prevent the surviving spouse from receiving too much in an election situation if, as is often the case, the spouse is designated as the beneficiary. See *infra* notes 286-97 and accompanying text (supporting inclusion of life insurance and retirement benefits in elective share).

18. 58 N.Y.2d 134, 446 N.E.2d 424, 459 N.Y.S.2d 739 (1983).

19. *In re Estate of Riefberg*, 58 N.Y.2d 134, 139, 446 N.E.2d 424, 426, 459 N.Y.S.2d 739, 741 (1983). Whether a buy-sell provision in a stockholders agreement "can be a testamentary substitute" was a matter of first impression in New York's appellate courts. *Id.* at 136, 446 N.E.2d at 425, 459 N.Y.S.2d at 740.

20. EPTL § 5-1.1(b)(1)(E) (McKinney 1981) includes transfers in which the decedent retains a power to revoke "by the express provisions of the disposing instrument." See *infra* note 32 and accompanying text (quoting relevant EPTL section).

21. 296 U.S. 93 (1935).

22. Revenue Act of 1926, § 302(d), ch. 27, 44 Stat. 9 (predecessor of I.R.C. § 2038 (1986)).

statutes cover a transfer with a retained power, the exercise of which is mandatory or subject to an external standard.

As our analysis reveals, these statutes have neither produced predictable results nor eliminated confusion. Clarification, therefore, is needed. Accordingly, we propose guidelines to resolve the ambiguities and eliminate deficiencies in these elective share statutes.²³ Our guidelines,²⁴ if implemented, should result in enlarging the net estate subject to the right of election while diminishing a decedent's ability to disinherit his surviving spouse.²⁵ With the increasing use of testamentary substitutes and other lifetime conveyances and contractual devices in estate planning, the distinction, which the Internal Revenue Code has effectively abolished,²⁶ between the probate estate and other property passing outside the estate at death over which the decedent has retained a measure of control would appear to be artificial and unworkable in the elective share area.²⁷ While advocating greater financial security for the surviving spouse, our proposal would also ensure that the survivor does not receive an unjustified economic windfall.²⁸

23. Most recently, Professors Langbein and Waggoner have advocated that the UPC be modified to provide for, among other things, an elective share based upon the length of the marriage and the amount of property owned by the surviving spouse. Langbein & Waggoner, *supra* note 5, at 314-21. They do not, however, discuss the types of inter vivos transfers that should constitute testamentary substitutes. See also *Divorce and Death: Disparity in Economic Rights of Spouse*, N.Y.L.J., Jan. 28, 1988, at 1, col. 3 (advocating use of equitable distribution as model for elective share legislation); Comment, *Spousal Disinheritance: The New York Solution — A Critique of Forced Share Legislation*, 7 W. NEW ENG. L. REV. 881, 905-07 (1985) (arguing for equitable distribution in cases of disinheritance). Adjusting the fractional share of the surviving spouse based upon the length of the marriage may be more fair than the current scheme but an equitable distribution model, which entails a case-by-case approach based upon more subjective criteria, is not appropriate in the elective share area which has traditionally involved different concerns and where predictability and ease of administration are important goals. Furthermore, use of an equitable distribution model would significantly impede the development of a comprehensive estate plan and, more importantly, would probably provide no greater protection for the surviving spouse than do our guidelines. For a recent critique of the forced share and a proposal to base the right of election upon the length of the marriage, the extent of the surviving spouse's assets and property acquired during marriage, see Oldham, *Should the Surviving Spouse's Forced Share Be Retained?*, 38 CASE W. RES. L. REV. 223 (1987-88).

24. See *infra* notes 259-305 and accompanying text (discussing these guidelines).

25. The net estate, as used in EPTL § 5-1.1, includes the probate or intestate estate and the capital value, as of the date of death, of testamentary substitutes less debts, administration expenses, and reasonable funeral expenses. EPTL § 5-1.1(c) (McKinney 1981). The UPC uses the term "augmented estate" in place of net estate. UPC § 2-202, 8 U.L.A. 75 (1983).

26. See I.R.C. §§ 2031, 2033, 2036-38, 2040-42 (1986) (enumerating property and transfers that are includible in gross estate).

27. See Langbein, *The Nonprobate Revolution and the Future of the Law of Succession*, 97 HARV. L. REV. 1108 (1984) (arguing that wills and will substitutes should be unified for purposes of estates law).

28. See *infra* notes 286-97 and accompanying text (recommending inclusion of life insurance and retirement plans in the net estate regardless of who is the beneficiary to provide both financial security for the surviving spouse and prevent her from receiving a windfall).

I. THE RIEFBERG CASE

*In re Estate of Riefberg*²⁹ is the initial focus of our analysis. *Riefberg* held that a buy-sell provision in a shareholders agreement,³⁰ expressly reserving the stockholders' right to terminate the agreement by mutual consent, was a testamentary substitute.³¹ The pertinent statute, EPTL section 5-1.1(b)(1)(E), provides that:

[a]ny disposition of property made by the decedent . . . in trust or otherwise, to the extent that the decedent at the date of his death retained, either alone or in conjunction with another person, by the express provisions of the disposing instrument, a power to revoke such disposition or a power to consume, invade or dispose of the principal thereof is a testamentary substitute and its capital value, as of the decedent's death, is included in the net estate subject to the surviving spouse's elective right.³²

In *Riefberg*, the decedent's disinherited second wife elected to take her statutory share under EPTL section 5-1.1. She claimed that under EPTL section 5-1.1(b)(1)(E) the purchase price paid after the decedent's death for his stock interest in a family-owned corporation pursuant to a stockholders agreement should be included in the net estate for purposes of determining her elective share.³³ The decedent and his brother, each owning one-half of the corporation's stock, had entered into a stockholders agreement with the corporation that had initially provided that the corporation would purchase a deceased stockholder's shares and pay the purchase price to his

29. 58 N.Y.2d 134, 446 N.E.2d 424, 459 N.Y.S.2d 739 (1983). For comments on *Riefberg*, see Note, *Survey of New York Practice: Estate Powers & Trusts Law*, 58 ST. JOHN'S L. REV. 219, 222-27 (1983) (describing court's holding that stockholders agreement was testamentary substitute giving widow right to elect against it as part of net estate); *Corporate Buy-Sell Pacts — Testamentary Substitutes?*, N.Y.L.J., May 27, 1983, at 1, col. 3 (emphasizing that *Riefberg* was based upon interpretation of legislative history of EPTL § 5.1.1(b)(1)); Dean, *Estates and Trusts*, 33 SYRACUSE L. REV. 237, 242-43 (1982) (discussing lower court opinion).

30. Buy-sell provisions are commonly used in shareholders agreements in closely held corporations to prevent unwanted third parties from obtaining a stock interest in the corporation. See *In re Estate of Brown*, 446 Pa. 401, 409, 289 A.2d 77, 81 (1972) (expounding on use of buy-sell provisions as means of preventing outsider purchases). See generally 2 F. O'NEAL & R. THOMPSON, O'NEAL'S CLOSE CORPORATIONS § 7.02 (3d ed. 1987) (explaining that transfer restrictions in a closely held corporation safeguard intimacy and provide control over company personnel); Note, *Third Party Beneficiaries and the Intention Standard: A Search for Rational Contract Decision-Making*, 54 VA. L. REV. 1166, 1184 (1968) (elaborating on moral and competitive factors in transfer restrictions). Upon the death of a stockholder such provisions generally either (i) require the surviving shareholders or the corporation to purchase the shares; (ii) give the corporation or the surviving shareholders an option to purchase; or (iii) give the corporation or the surviving shareholders a right of first refusal. 2 F. O'NEAL & R. THOMPSON, *supra* at § 7.05.

31. *In re Estate of Riefberg*, 58 N.Y.2d 134, 142, 446 N.E.2d 424, 428, 459 N.Y.S.2d 739, 743 (1983).

32. EPTL § 5-1.1(b)(1)(E) (McKinney 1981).

33. *In re Estate of Riefberg*, 58 N.Y.2d 134, 137, 446 N.E.2d 424, 425-26, 459 N.Y.S.2d 739, 740-41 (1983).

personal representative.³⁴ One day before the decedent's death, however, the parties amended the agreement to obligate the corporation to pay the purchase price directly to specified individuals, including the decedent's first wife but not his surviving spouse.³⁵ In addition, the agreement provided that (i) either shareholder could transfer his stock by inter vivos gift to his wife or any member of his immediate family subject to the terms of the stockholders agreement; (ii) either shareholder could withdraw as a stockholder by offering his shares to the corporation which would then have a thirty-day option to purchase them; (iii) if the corporation did not purchase the shares, the remaining shareholder had a forty-five day option to do so; (iv) if neither the corporation nor the remaining shareholder purchased the shares, the corporation was to be liquidated; and (v) the agreement would remain in effect until "terminated by mutual agreement of the parties"³⁶

In concluding that the buy-sell provision in the stockholders agreement was covered by EPTL section 5-1.1(b)(1)(E), the *Riefberg* court relied on the Bennett Commission Report (the "Report")³⁷

34. *Riefberg*, 58 N.Y.2d at 137, 446 N.E.2d at 426, 459 N.Y.S.2d at 741.

35. *Id.*

36. *In re Estate of Riefberg*, 107 Misc. 2d 5, 9, 433 N.Y.S.2d 374, 377 (Nassau Co. Surr. Ct. 1980), *aff'd*, 86 A.D.2d 782, 449 N.Y.S.2d 371 (N.Y. App. Div. 1982), *aff'd*, 58 N.Y.2d 134, 446 N.E.2d 424, 459 N.Y.S.2d 739 (1983). Relying on all three provisions, the lower court held that the stockholders agreement was a testamentary substitute within the meaning of EPTL 5-1.1(b)(1)(E). *Id.* at 10, 433 N.Y.S.2d at 377. It equated the termination "by mutual agreement" provision with "an express power of revocation under the statute [EPTL 5-1.1(b)(1)(E)]," and it considered the gift and the withdrawal and sale provisions as "the equivalents of a power to dispose or consume the principal, both covered by the statute." *Id.* at 9-10, 433 N.Y.S.2d at 377.

37. See *supra* note 5 (citing Bennett Commission Report as background for EPTL). Inasmuch as the EPTL "reshape[d] principles," the Court of Appeals believed that "an historical survey would illumine its [the legislature's] intention" and therefore focused on the Report as "instructive." *In re Estate of Riefberg*, 58 N.Y.2d at 139-40, 446 N.E.2d at 427, 459 N.Y.S.2d at 742.

The court was also influenced by the decision in *In re Burk*, 37 Pa. D. & C.2d 528 (1965) which construed section 11 of the Pennsylvania Estates Act (quoted below) as permitting a right of election against a stock purchase agreement. *Id.* at 531-32. However, the court's reliance on *Burk* was misplaced. First, it is unclear whether *Burk* found for the surviving spouse based on section 8 of the Wills Act, which provided that a surviving spouse is entitled to one-half or one-third of the "real and personal estate of the testator," 20 PA. CONS. STAT. ANN. § 2508(b) (Purdon 1975)—in which event the case was entirely irrelevant—or on section 11 of the Estates Act, which provided in pertinent part:

A conveyance of assets by a person who retains a power of appointment by will, or a power of revocation or consumption over the principal thereof, shall at the election of his surviving spouse, be treated as a testamentary disposition so far as the surviving spouse is concerned to the extent to which the power has been reserved

20 PA. CONS. STAT. ANN. § 6111(a) (Purdon 1975) (repealed 1978). See *In re Estate of Brown*, 446 Pa. 401, 411, 289 A.2d 77, 82-83 (1972) (commenting on vague foundation of *Burk*). Furthermore, the court in *Burk* made no in-depth analysis of the issue under section 11. For example, it never addressed the basic question of whether the agreement constituted a "conveyance of assets" within the meaning of section 11. See *infra* notes 143 and 148 and accompanying text (describing Pennsylvania's statutory interpretations of "conveyance" and

which, the court said, analogized stock purchase agreements to trusts in which the decedent retained a life interest.³⁸ Insofar as EPTL 5-1.1(b)(1)(E) applies to any disposition “in trust or otherwise,”³⁹ the Report plainly supports the court’s view that the words “or otherwise” can, under certain circumstances, encompass contractual devices.⁴⁰ However, the court’s further observation that the Report concluded that stock purchase agreements should be regarded as testamentary substitutes because they are analogous to retained life interests is questionable.⁴¹ Moreover, the statute itself specifies transfers that constitute testamentary substitutes, but nowhere does EPTL section 5-1.1(b)(1)(E) mention or even hint at a transfer in which the decedent retained only a life interest.⁴²

“transfer”). More importantly, *Burk* was effectively overruled by the Pennsylvania Supreme Court in 1972, eleven years prior to *Riefberg*’s reliance on *Burk*. See *In re Estate of Brown*, 446 Pa. at 411-12, 289 A.2d at 82 (holding contractual rights under buy-sell agreement superior to widow’s competing claim of election rights). For comments on *Burk*, see Shaiman, *The Widow’s Election-Tax and Fiduciary Considerations*, 40 TEMP. L.Q. 1, 26-27 (1966) (criticizing reasoning but not result); Comment, *Buy and Sell Agreements and the Widow’s Rights*, 114 U. PA. L. REV. 1006 (1966) (criticizing reasoning and result insofar as right of election against shares of stock is allowed). Significantly, neither the parties nor the court in *Riefberg* made mention of *Brown*.

38. *In re Estate of Riefberg*, 58 N.Y.2d at 140, 446 N.E.2d at 427, 459 N.Y.S.2d at 742.

39. EPTL § 5-1.1(b)(1)(E) (McKinney 1981).

40. The Report analogizes contractual devices whereby the beneficiary received property from the decedent during the decedent’s lifetime but “where the decedent has retained a life estate or a power to control” to trusts “in which the decedent retained a life estate or control.” REPORT, *supra* note 5, at 129 n.97.

41. *In re Estate of Riefberg*, 58 N.Y.2d at 140, 446 N.E.2d at 427, 459 N.Y.S.2d at 742. The portion of the Report cited by the court simply asks: “[S]hould the surviving spouse have any right to elect [against contractual transactions] in which technical consideration is present and yet the decedent has not received his money’s worth.” REPORT, *supra* note 5, at 129. The Report provides no answer; it only indicates that the problem is multi-faceted and notes that another portion of the Report contains a discussion of some of the solutions to this question that have been offered in various jurisdictions. *Id.* at 129. Earlier in the Report, the Bennett Commission merely noted its concern “with the situation where . . . the settlor reserves to himself either a life estate or a power of revocation or power of control or any combination of these.” *Id.* at 124. The New York State Bar Association Committee on Trusts and Estates took the position that a transfer where “practical control of the beneficial enjoyment of the property has been retained during the transferor’s lifetime” should be “considered subject to the elective rights of the surviving spouse.” *Id.* at 138. However, without any discussion or analysis, the Bennett Commission rejected that position. *Id.* at 138-39 (emphasis supplied).

42. See *infra* Appendix, pp. 68-71 (quoting selected provisions of EPTL § 5-1.1). The court also implicitly assumed that the Report’s reference to “stock purchase agreements” is a reference to buy-sell provisions in a stockholders agreement such as the one involved in *Riefberg*. See *In re Estate of Riefberg*, 58 N.Y.2d at 140, 446 N.E.2d at 427, 459 N.Y.S.2d at 742 (indicating that Bennett Commission considered stock purchase agreements to be testamentary substitutes). From a fair reading of the Report, it would appear that in using the phrase “stock purchase agreement” the Report was *not* referring either to buy-sell agreements per se or to those included as part of an overall agreement between stockholders of a closely held corporation. See REPORT, *supra* note 5, at 129 n.96. Rather it was referring to a type of employee benefit plan under which an employee is permitted to purchase stock in the employer. Thus, in discussing “Other Contract Devices,” the Report states that most of the cases would involve a contract pursuant to which the “beneficiary . . . is to receive benefits after the death of the decedent.” *Id.* at 128-29. In a footnote to this statement, the Report quotes verbatim from Macdonald’s section on contractual devices. *Id.* at 129 n.96. This section, entitled “Employee Death Benefits,” reads, in pertinent part, as follows:

The real question presented in *Riefberg* was whether, by virtue of the stockholders agreement's express provision for termination by mutual consent,⁴³ the decedent "retained . . . by the express provisions of the disposing instrument, a power to revoke"⁴⁴ The court answered this question in the affirmative: "[B]y expressly providing for the manner of its termination," the agreement "fell squarely within the express statutory definition [EPTL section 5-1.1(b)(1)(E)] of the category of testamentary substitute[s]" concerning transfers in which the decedent retains certain powers.⁴⁵ Thus, in the court's view, the decedent at the time of his death retained, by the express terms of the agreement, a power to revoke the disposition, or more specifically, a power to revoke the stockholders agreement.⁴⁶

There is very little authority on the power of a surviving spouse to set aside or invade beneficiary rights under retirement plans, pension schemes, profit-sharing and stock-purchase agreements, and other types of employee benefits.

W. MACDONALD, *supra* note 1, at 244. Therefore, one can conclude that the Report did not consider stockholders agreements or buy-sell provisions of the type involved in *Riefberg* and commonly used by stockholders in closely held corporations.

To emphasize the point that the statute was intended to include "stockholders agreements," the court further notes that while section 5-1.1(b)(1)(E) was still in legislative committee, a proposal was adopted—EPTL § 5-1.1(b)(2)—that "excluded 'pension plans', 'insurance proceeds', 'profit sharing plans', 'stock options', 'stock bonuses', and 'deferred compensation plans'." *In re Estate of Riefberg*, 58 N.Y.2d 134, 140, 446 N.E.2d 424, 427, 459 N.Y.S.2d 739, 742 (1983). "[I]t is telling," the court says, "that, in stark contrast to this enumeration of exceptions to paragraph (1) [EPTL § 5-1.1(b)(1)(E)], none was made for stockholders agreements." *Id.* (citing Fourth Report of Temp. Comm. on Modernization, Revision and Simplification of the Law of Estates [Fourth Report], NY Legis. Doc., 1965, No. 19, pp. 148-50). However, it is only "telling" if, as the court assumes, paragraph (1) included stockholders agreements. Since such agreements were not included in paragraph (1) as explained above, their omission from paragraph (2) is not "telling." Furthermore, EPTL § 5-1.1(b)(2) does *not* mention stock options as the court states. Compare EPTL § 5-1.1(b)(2) (McKinney 1981) (enumerating transactions which are not testamentary substitutes) with *Riefberg*, 58 N.Y.2d at 140, 446 N.E.2d at 427, 459 N.Y.S.2d at 742 (naming "stock options" as one exclusion in EPTL § 5-1.1(b)(2)).

43. See *supra* note 36 and accompanying text (specifying terms of buy-sell provision in shareholders agreement at issue in *Riefberg*).

44. EPTL § 5-1.1(b)(1)(E) (McKinney 1981) (emphasis supplied).

45. *In re Estate of Riefberg*, 58 N.Y.2d 134, 142, 446 N.E.2d 424, 428, 459 N.Y.S.2d 739, 743 (1983). The opinion does not identify the precise "express provision" by which Riefberg retained a power to revoke, consume, invade or otherwise dispose of the stock. Thus, the court simply says:

[I]ts 'express provisions' enabled the decedent, in terms of an appropriate use of *ejusdem generis*, to retain a power to 'revoke', 'consume', 'invade', or otherwise 'dispose' of the corpus. Thus, the agreement itself, by expressly providing for the manner of its termination, fell squarely within the express statutory definition of the category of testamentary substitute which here has been our concern (EPTL 5-1.1, subd. [b], para [1], cl. [E]).

Id. at 141-42, 446 N.E.2d at 428, 459 N.Y.S.2d at 743. A fair reading of the quotation leads to the conclusion that the only express term in the stockholders agreement to which the court was referring is the provision for termination by mutual agreement and not the additional provisions on which the lower court also relied. See *supra* note 36 (describing lower court conclusion that stockholders agreement was a testamentary substitute).

46. *In re Estate of Riefberg*, 58 N.Y.2d 134, 141-42, 446 N.E.2d 424, 428, 459 N.Y.S.2d 739, 743 (1983). Independent of its reliance on the express terms of the agreement, the *Riefberg* court emphasized that the stockholders agreement not only permitted the decedent to

In making this determination, the court brushed aside the argument that since every contract may be terminated by mutual consent, the express termination provision in the stockholders agreement added nothing to the rights conferred by law and, accordingly, the agreement did not meet the statutory requisites.⁴⁷ Logically, however, this argument has merit. If under local law the contracting parties have the right to terminate in the absence of an express termination provision, it can scarcely be said that the right to terminate was retained by an express provision of the contract. Rather, the power to revoke arose and was retained by virtue of local law, and the express termination provision in the contract is surplusage.

Acceptance of this argument, however, would not necessarily have led to a different conclusion in *Riefberg*. The *Riefberg* court did not consider, nor did the parties address, whether there were any third party beneficiaries of the stockholders agreement.⁴⁸ The persons to whom the proceeds from a sale of the decedent's stock were to be paid were not parties to the agreement; only the decedent and his brother were parties to the agreement.⁴⁹ If the beneficiaries of the

control the beneficial enjoyment of the stock interest but also "was the means by which the decedent . . . stripped the estate of assets which should have been subject to his surviving spouse's right to her elective share." *Id.* at 141, 446 N.E.2d at 428, 549 N.Y.S.2d at 743. Stated otherwise, the agreement should be deemed a testamentary substitute in part because such a lifetime transaction deprives the surviving spouse of having the decedent's stock included in the net estate for elective share purposes. *Id.* The court's emphasis on this point is reminiscent of pre-EPTL cases that employed the "motive" test—a subjective test that has no place under EPTL § 5-1.1(b)(1) and its objective criteria. See *Bodner v. Feit*, 247 A.D. 119, 121-22, 286 N.Y.S. 814, 817 (N.Y. App. Div. 1936) (ruling that inter vivos transfer by spouse subject to right of election if purpose was to disinherit surviving spouse). Cf. *supra* note 8 and accompanying text (discussing pre-EPTL tests utilized by New York courts in determining if transfer was subject to right of election). Indeed, it is implicit from the statute that unless the lifetime disposition falls within one of the specific and limited categories listed in section 5-1.1(b)(1), a person has every right to strip his estate of all of its assets through lifetime transfers. See *In re Estate of Zeigher*, 95 Misc. 2d 230, 231, 406 N.Y.S.2d 977, 978 (Nassau Co. Surr. Ct. 1978) (holding custodial accounts were not testamentary substitutes because they did not fall within statute's five limited categories); but see *infra* notes 234-37 and accompanying text; note 289.

47. See *Riefberg*, 58 N.Y.2d at 141, 446 N.E.2d at 428, 459 N.Y.S.2d at 743. This argument was predicated on, and discussed in, P. ROHAN, PRACTICE COMMENTARY TO EPTL § 5-1.1, Commentary at 3, 41-42 (McKinney 1981). In particular, Rohan was commenting on the lower court opinion which stated that the provision for termination by mutual agreement "is equivalent to an express power of revocation under the statute [EPTL § 5-1.1(b)(1)(E)]." *Id.* at 42 (quoting *In re Estate of Riefberg*, 107 Misc. 2d 5, 9, 433 N.Y.S.2d 374, 377 (Nassau Co. Surr. Ct. 1980), *aff'd*, 86 A.D.2d 782, 449 N.Y.S.2d 371 (N.Y. App. Div. 1982), *aff'd*, 58 N.Y.2d 134, 446 N.E.2d 424, 459 N.Y.S.2d 739 (1983)). This "reasoning," Rohan said, "is open to serious doubt" because "any contract can be abrogated by mutual consent of adverse parties." He concluded, without any explanation or citation of authority, that "this fact [an express provision for termination by mutual consent], without more, should not lead to classification as a 'testamentary substitute.'" EPTL § 5-1.1, at 42 (McKinney 1981).

48. *Corporate Buy-Sell Pacts — Testamentary Substitutes?*, *supra* note 29, at 2, col. 1.

49. See *Riefberg*, 58 N.Y.2d at 137, 446 N.E.2d at 426, 459 N.Y.S.2d at 741.

sale proceeds had been intended beneficiaries, however, then the power to revoke would not necessarily arise and be retained by local law, absent an express provision, and an express reservation of that power would not necessarily be surplusage.⁵⁰ Although the general rule is that the parties to an agreement have the power to modify or terminate it, even without a provision in the contract reserving such a power,⁵¹ the same is not true of a third party beneficiary contract if the rights of the beneficiary have vested.⁵² In such a case, the contracting parties may not terminate or modify the contract unless they have reserved such a power in the contract itself.⁵³ Thus, in *Riefberg*, if the beneficiaries' rights would have vested in the absence of the termination provision,⁵⁴ then the express termination clause

50. The Restatement (Second) of Contracts refers to beneficiaries who have rights under the contract as "intended beneficiaries" and avoids the use of the terms "donee" or "creditor" beneficiaries in the statement of its rules with respect to them. RESTATEMENT (SECOND) OF CONTRACTS § 302 (1981). New York has expressly adopted the Second Restatement's terminology and formulation regarding the classification of beneficiaries. See *Fourth Ocean Putnam Corp. v. Interstate Wrecking Co.*, 66 N.Y.2d 38, 44, 485 N.E.2d 208, 211-12, 495 N.Y.S.2d 1, 4-5 (1985) (decided after *Riefberg*) (holding property owner who is "incidental beneficiary" rather than "intended beneficiary" of contract is unable to maintain action).

51. RESTATEMENT (SECOND) OF CONTRACTS § 311 comment a (1981) (noting "[t]he parties to a contract cannot by agreement preclude themselves from varying their duties to each other by subsequent agreement"); J. CALAMARI & J. PERILLO, *THE LAW OF CONTRACTS* 863-64 (3d ed. 1987).

52. RESTATEMENT (SECOND) OF CONTRACTS § 311 (1981).

53. *Id.* The first Restatement of Contracts, which classified contract beneficiaries who have rights under a contract as either "donee" or "creditor" beneficiaries, RESTATEMENT OF CONTRACTS § 133 (1932), treats the rights of a donee beneficiary as being vested at the time the contract is made and these rights are thus indefeasible unless a power to modify them is reserved. *Id.* § 143. The rights of a creditor beneficiary, however, first vest when the beneficiary brings an action to enforce the contract or otherwise materially changes position before learning of a modification or termination. *Id.* Most courts have been opposed to discriminating between the rights of donee and creditor beneficiaries. RESTATEMENT (SECOND) OF CONTRACTS § 311 reporter's note at 469 (1981); Note, *The Third Party Beneficiary Concept: A Proposal*, 57 COLUM. L. REV. 406, 418-19 (1957).

RESTATEMENT (SECOND) OF CONTRACTS § 311 (1981) espouses the view that absent a contract term to the contrary, a duty to an intended beneficiary may be modified or discharged without the beneficiary's consent unless the intended beneficiary prior to "notification of the discharge or modification materially changes his position in justifiable reliance on the promise or brings suit on it or manifests assent to it at the request of the promisor or promisee." See *Detroit Bank & Trust Co. v. Chicago Flame Hardening Co.*, 541 F. Supp. 1278, 1283 (N.D. Ind. 1982) (applying Restatement (Second) formulation and holding that beneficiary's failure to accept, adopt, or act upon agreement extinguished any benefits that might have accrued).

54. See J. CALAMARI & J. PERILLO, *THE LAW OF CONTRACTS* 714-15 (3d ed. 1987); E. FARNSWORTH, *CONTRACTS* 740 (1982). Prior to the decision in *Riefberg*, New York had neither adopted nor rejected the position of the second Restatement. See *Salesky v. Hat Corp. of America*, 20 A.D.2d 114, 117, 244 N.Y.S.2d 965, 968 (N.Y. App. Div. 1963) (declining to decide whether to adopt Restatement (second) view because death benefits agreement at issue expressly permitted either of contracting parties to terminate upon notice). New York cases decided prior to *Riefberg* are consistent with the view of the first Restatement. See *Knowles v. Erwin*, 50 N.Y. Sup. Ct. 150, 153 (N.Y. App. Div. 1887), *aff'd mem.*, 124 N.Y. 633, 26 N.E. 759 (1891) (distinguished in *Salesky*, 20 A.D.2d at 116 n.*, 244 N.Y.S.2d at 967 n.*) (holding that rights of beneficiaries became fixed upon delivery of instrument); *In re Estate of Fairbairn*, 265 A.D. 431, 433, 40 N.Y.S.2d 280, 282 (N.Y. App. Div. 1943) (relying in part on *Knowles* and holding third party beneficiary's "rights accrued and were indefeasible upon the making of

in the stockholders agreement added something to the rights conferred by law and the decedent clearly retained an express power to revoke the disposition as required by EPTL section 5-1.1(b)(1). On the other hand, if absent the termination clause the beneficiaries' rights at the time of the decedent's death were subject to modification without their consent, then the termination clause in the stockholders agreement added nothing to the decedent's rights granted by local law. In such a case, the statutory requisite of a reservation of a power by the express provisions of the disposing instrument was not met.⁵⁵

II. IMPLICATIONS OF *RIEFBERG* FOR TRANSFERS IN TRUST

Most transfers with retained powers that constitute testamentary substitutes are transfers in trust. *Riefberg's* implications are most significant in this area because application of *Riefberg* to trusts produces anomalous results.⁵⁶ To illustrate, compare two hypothetical inter vivos trusts: Trust 1 that provides "this trust may be revoked or terminated by the settlor together with the consent of all living ben-

the . . . contract"). However, these cases were decided prior to the adoption of the Restatement (Second) and New York seems to be heading in the direction of adopting all the Restatement (Second) concepts regarding third party beneficiaries. See *Fourth Ocean Putnam Corp. v. Interstate Wrecking Co.*, 66 N.Y.2d 38, 44-45, 485 N.E.2d 208, 211-12, 495 N.Y.S.2d 1, 4-5 (1985) (applying Restatement (Second) formulations to conclude that plaintiff was incidental beneficiary and had no rights under contract).

55. As previously noted, under the Restatement (Second) of Contracts, unless there were a contrary contract term, the duty to these beneficiaries, who clearly are intended beneficiaries, could have been modified or discharged in the absence of assent, bringing an action or a material change in their position in justifiable reliance on the promise. See *supra* note 53 and accompanying text. There is no indication in *Riefberg* that prior to the decedent's death the beneficiaries either materially changed their position, brought an action, or assented to the promise. See *In re Estate of Riefberg*, 58 N.Y.2d 134, 446 N.E.2d 424, 459 N.Y.S.2d 739 (1983). Nor did the agreement apparently contain a provision precluding modification or discharge. But compare RESTATEMENT (SECOND) OF CONTRACTS § 311 comment b (1981). Thus, under the Restatement (Second) approach, it would appear that the express termination clause did not add to the right conferred by local law on the contracting parties to terminate under the circumstances existing at the time of decedent's death. Accordingly, it would follow that the decedent did not retain at death a power to revoke within the meaning of EPTL § 5-1.1(b)(1)(E). But see *Estate of Siegel v. Commissioner*, 74 T.C. 613 (1980) (holding that express reservation by parties to contract of power to modify it forecloses beneficiaries from taking the steps required by Restatement (Second) to vest their rights as third-party beneficiaries). Thus, the retained power to modify in *Siegel* "appears to be greater than the rights of the parties under local law." *Id.* at 630. This position seems untenable because under the Restatement (Second) if an intended beneficiary's rights have not vested, the parties to the contract may foreclose the vesting of these rights *even in the absence of an express provision to modify*. RESTATEMENT (SECOND) OF CONTRACTS § 311 (1981). Once these rights have vested, however, the original parties can modify them only if they reserved a right to do so. *Id.* Thus, an express provision adds to the rights of third parties under local law only if their rights have already vested. This was not the case in *Siegel*.

56. See *infra* notes 60-63 and accompanying text (discussing implications of *Riefberg* on transfers in trust).

eficiaries;"⁵⁷ and Trust 2 that does not contain a revocation or termination provision.⁵⁸

Trust 1 would be revocable even absent its express provision for termination by the settlor in conjunction with all the living beneficiaries because, by statute, any trust may be revoked by the settlor with the consent of all living beneficiaries.⁵⁹ The express provision in Trust 1 for termination, therefore, adds nothing to the decedent's power to revoke.⁶⁰ Applying *Riefberg*, however, Trust 1 should be deemed a testamentary substitute for purposes of EPTL section 5-1.1(b)(1) because the trust instrument contains an express provision for termination by the settlor in conjunction with another (the beneficiaries)—the precise situation presented in *Riefberg* in the context of a stockholders agreement. In other words, *Riefberg* compels the conclusion that the settlor retained the power to revoke Trust 1 "by the express terms of the disposing instrument" even though the law

57. Although this termination provision may not be too common, it is appropriate for illustration purposes because it is coextensive with New York's statutory power of termination, thus demonstrating the application of *Riefberg* in the trust area. See *infra* note 59 (noting New York courts have required consent of only living beneficiaries to revoke or terminate trust). If the consent of the unascertainable as well as the living beneficiaries were required, then under the majority rule the trust could not be terminated because their agreement could not be secured. See *infra* notes 59 and 80.

58. In most states, including New York, a trust is irrevocable unless a power of revocation has been reserved. See, e.g., RESTATEMENT (SECOND) OF TRUSTS § 330 (1959); G. BOGERT, TRUSTS § 148, at 527-30 (6th ed. 1987); 4 A. SCOTT, TRUSTS § 330 (3d ed. 1967); EPTL § 10-10.8 (McKinney 1967).

59. EPTL § 7-1.9(a) (McKinney 1967). Although the statute on its face refers to "persons beneficially interested," New York courts had held that the consent of only the *living* beneficiaries is necessary. See, e.g., *Roth v. Lipton*, 73 A.D.2d 560, 561, 423 N.Y.S.2d 25, 127 (N.Y. App. Div. 1979) (determining that consent of unborn children is not required to revoke trust). This does not comport with general law which requires the consent of *all* beneficiaries. See *infra* note 80 (noting settlor's consent is indispensable to terminate trust in certain circumstances); 4 A. SCOTT, *supra* note 58, at § 338; RESTATEMENT (SECOND) OF TRUSTS § 338 comment f (1959) (emphasizing termination or modification can only be accomplished through consent of all beneficiaries).

Under EPTL § 7-1.9(b), the settlor alone can revoke the trust without the consent of the beneficiaries if the beneficiaries are designated by such terms as "heirs" or "next of kin." This statutory codification of the doctrine of worthier title is limited in New York to the area of termination of trusts. See EPTL 6-5.9 (McKinney 1967); note 111 *infra* and accompanying text.

60. Other termination provisions in which the settlor retained a power in conjunction with another would render the general rule inapplicable. See 4 A. SCOTT, *supra* note 58, § 330.9 (providing for reservation of power to revoke only with consent of trustee); *id.* at § 330.10 (permitting reservation of power to revoke with consent of third person who is neither beneficiary nor trustee). See also *In re Dodge's Trust*, 25 N.Y.2d 273, 285, 250 N.E.2d 849, 856, 303 N.Y.S.2d 847, 857 (1969) (stating that terms of the trust requiring the trustee's consent to revocation "must be complied with before the statute [EPTL 7-1.9(a)] comes into play"). Cf. *In re Mordecai's Trust*, 24 Misc. 2d 668, 670, 201 N.Y.S.2d 899, 902 (N.Y. Sup. Ct.), *aff'd mem.*, 12 A.D.2d 449, 210 N.Y.S.2d 478 (N.Y. App. Div. 1960) (holding that when settlor who was sole beneficiary of trust reserved power to revoke with consent of trustees, trust could not be revoked without their consent despite statutory rule). The transfers subject to these termination provisions, however, should be includible in the net estate for elective share purposes.

confers such a right of revocation without a provision in the trust instrument. Thus, although the express provision for termination is superfluous, Trust 1 would be includible in the net estate for elective share purposes.⁶¹

On the other hand, Trust 2 would not be deemed a testamentary substitute for purposes of section 5-1.1(b)(1) because the settlor did not retain a power to revoke by the express terms of the trust instrument.⁶² Nevertheless, like Trust 1, under state law this trust—even in the absence of an express provision—may be revoked by the settlor in conjunction with all the living beneficiaries.⁶³ Therefore, despite the settlor's retained power to revoke each trust, *Riefberg* would appear to dictate different results in these two cases. The consequence that Trust 1 would be deemed a testamentary substitute, includible in the net estate, while Trust 2 would not, makes no sense.

III. LEGISLATIVE INTENT

Significantly, the *Riefberg* court did not ask why the legislature included the phrase “by the express provisions of the disposing instrument” in EPTL section 5-1.1(b)(1)(E). Was the phrase included to limit or expand the scope of the statute, and can legislative intent justify this dichotomous result?

In its Report, which the *Riefberg* court called instructive,⁶⁴ the Bennett Commission proposed that the legislation apply to “any transfer or conveyance . . . to the extent that the decedent at the date of his death retained . . . a power to revoke such transfer or conveyance.” Significantly, the Report did not use the phrase “by

61. EPTL § 5-1.1(b)(1)(E) (McKinney 1981).

62. In construing the phrase “arising by the express terms of the instrument of transfer and not by operation of law” contained in a predecessor of I.R.C. § 2037(a)(2) (1986) (I.R.C. § 811(c)(2) (1939), as amended, applicable to pre-October 8, 1949 transfers), the Court of Appeals for the Third Circuit, after noting that statutory language should be given its common meaning, stated that “[t]he word ‘express’ means ‘directly and distinctly stated; expressed, not merely implied or left to inference’ [citing WEBSTER'S NEW INTERNATIONAL DICTIONARY 803 (1945)]. . . .” *Commissioner v. Marshall's Estate*, 203 F.2d 534, 537 (3d Cir. 1953). See also *Estate of Keiffer v. Commissioner*, 44 B.T.A. 1265, 1267 (1941) (indicating no distinction exists between right of revocation under Louisiana law and one expressly retained by donee); *Longacre v. Hornblower & Weeks*, 83 Pa. D. 8 C. 259, 262 (1952) (ruling that declaration of joint tenancy gives joint tenants “by operation of law all the rights . . . and powers of joint tenants” which includes “power of revocation pro tanto” (emphasis added)). Cf. *Estate of Spiegel v. Commissioner*, 335 U.S. 701, 705-06, 731 (1949) (ruling that reversionary interest exists unless grantor effects complete transfer of all property rights); I.R.C. § 2037 (1986); 5 B. BITTKER, *FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS* § 126.7.6 (1984) (stating that pre-October 1949 transfer not subject to I.R.C. § 2037 (1986) unless decedent expressly reserves reversionary interest). However, one commentator has argued that the language “by the express provisions” in EPTL § 5-1.1(b)(1)(E) adds nothing to the statute and does not differentiate it from the U.P.C. See Kurtz, *supra* note 1, at 1027 n.224.

63. See EPTL § 7-1.9(a) (McKinney 1967).

64. See *supra* note 37 and accompanying text (discussing reasoning of *Riefberg* court).

the express provisions of the disposing instrument," which was eventually incorporated into the statute.⁶⁵ Moreover, the Report, without any explanation, hastened to add that "[a] trust which is irrevocable by its terms but subject to revocation under section 23 of the Personal Property Law [currently EPTL section 7-1.9(a)] would not be deemed a revocable trust for this purpose."⁶⁶ Thus, the Report made it clear that a transfer subject only to a section 7-1.9(a) power of termination by the settlor in conjunction with all living beneficiaries was not to be covered by the proposed testamentary substitute legislation of section 5-1.1(b)(1), even in the absence of a specific statutory requirement that the power be retained "*by the express provisions of the disposing instrument.*"⁶⁷

The Report, as noted, speaks of a trust that is "irrevocable by its terms."⁶⁸ It does not address a fact pattern like Trust 1 which expressly provides that the trust may be revoked by the settlor with the consent of all living beneficiaries, that is, it permits revocation to the same extent as provided by local law even absent the provision.⁶⁹ The Report, however, reasonably can be construed as conveying the idea that a power to terminate conferred by EPTL section 7-1.9(a) is not a retained power to revoke within the meaning of the proposed elective share statute. Thus, even if the legislators had not added the phrase "by the express provisions of the disposing instrument,"⁷⁰ the most reasonable interpretation of the statute, in light of the Report, is to exclude from its coverage a trust that expressly reserves no more than the same power to revoke conferred by EPTL section 7-1.9(a).⁷¹

In view of the Report's position that a power to revoke retained by operation of law should not be deemed a power to revoke for

65. REPORT, *supra* note 5, at 139.

66. *Id.*

67. EPTL § 5-1.1(b)(1)(E) (McKinney 1981) (emphasis added). See *supra* note 32 and accompanying text (quoting text of statute).

68. See REPORT, *supra* note 5, at 139. The Report's reference to a trust that is "irrevocable by its terms" is not very meaningful. In New York, every trust is irrevocable unless the trust expressly provides otherwise. EPTL § 10-10.8 (McKinney 1967). See *supra* note 58 (discussing New York State law). Is the Report referring only to a trust that expressly provides that it is irrevocable, thereby excluding any trust that does not so state? If it were making such a distinction, presumably it would have done so in clear language. Furthermore, the Bennett Commission had no reasonable basis on which to make such a distinction.

69. See *Helvering v. Helmholtz*, 296 U.S. 93 (1935) (presenting same situation). See also *infra* notes 71-78 and accompanying text (discussing *Helmholtz*).

70. EPTL § 7-1.9(a) (McKinney 1967).

71. As discussed in this article (see *infra* text accompanying notes 102-09), no logical reason exists to differentiate between a transfer in which a power to revoke is retained by the express provisions of the disposing instrument and a transfer in which a power to revoke is conferred by operation of law. In the guidelines, we propose that the New York statute be amended to cover both transfers. See *infra* text accompanying notes 267-72.

purposes of the elective share statute,⁷² the phrase “by the express provisions of the disposing instrument” probably was added only to underscore the intent that powers granted by operation of law be excluded. For absent that phrase, it could be argued that powers conferred by operation of local law were covered by the plain language of EPTL section 5-1.1(b)(1). By all accounts, the legislature apparently included the phrase to limit, not expand, the scope of the statute as proposed in the Report.

In contrast to *Riefberg*, therefore, the legislative history would not appear to justify treating Trusts 1 and 2 differently under the current language of EPTL section 5-1.1(b)(1)(E). Indeed, in light of the Report, neither trust should be included in the net estate under EPTL section 5-1.1(b)(1)(E). Had *Riefberg* considered the legislative history, it might have reached a different result.

IV. A FEDERAL ESTATE TAX ANALOGY

Significantly, the *Riefberg* court missed an opportunity to apply, or at least to consider applying, an entire body of federal estate tax law that appears to have a direct bearing on the interpretation of EPTL section 5-1.1, the UPC, and any similar elective share statutes. The language of these elective share statutes is similar to section 2038 of the Internal Revenue Code of 1986 (IRC)⁷³ which provides, in pertinent part:

The value of the gross estate shall include the value of all property . . . [t]o the extent of any interest therein of which the decedent has at any time made a transfer . . . by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power (in whatever capacity exercisable) by the decedent alone or by the decedent in conjunction with any other person (without regard to when or from what source the decedent acquired such power), to alter, amend, revoke, or terminate . . .⁷⁴

Although not binding, interpretations accorded this section may be instructive in interpreting the analogous elective share statutes.⁷⁵

The United States Supreme Court decision in *Helvering v. Helmholtz*⁷⁶ is a case in point. In *Helmholtz*, the decedent and others con-

72. REPORT, *supra* note 5, at 139.

73. I.R.C. § 2038 (1986).

74. I.R.C. § 2038(a)(1) (1986). All matter in parentheses applies only to transfers after June 22, 1936.

75. Section 2038(a)(1) does not require an expressly retained power, unlike EPTL § 5-1.1(b)(1)(E) or for that matter, I.R.C. § 2037(a)(2) (1986). See *supra* note 62 (discussing interpretations of term “express provisions”); *infra* note 78.

76. 296 U.S. 93 (1935).

veyed shares of stock to a trustee pursuant to a trust instrument, which named the decedent as a life beneficiary and expressly provided that the trust could be terminated upon written declaration of all the living beneficiaries.⁷⁷ The government claimed that the express termination provision was equivalent to a power to revoke or amend retained by the decedent in conjunction with the other beneficiaries—the precise argument accepted in *Riefberg*. The government, therefore, sought to include the trust principal (the value of the transferred stock) in the decedent's gross estate pursuant to the predecessor of current section 2038. That provision, like EPTL section 5-1.1(b)(1)(E), applied to any lifetime transfer subject at the decedent's death "to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend or revoke" ⁷⁸

In rejecting the government's argument, the Supreme Court concluded that the trust agreement contained "no such power" within the meaning of the tax statute;⁷⁹ and in words also directly applicable to the *Riefberg* situation, the Court stated:

This argument overlooks the essential difference between a power to revoke, alter or amend, and a condition which the law imposes. *The general rule is that all parties in interest may terminate the trust. The clause in question added nothing to the rights which the law conferred.* Congress cannot tax as a transfer intended to take effect in possession or enjoyment at the death of the settlor a trust created in a state whose law permits all the beneficiaries to terminate the trust.⁸⁰

77. *Helvering v. Helmholz*, 296 U.S. 93, 94-95 (1935).

78. Revenue Act of 1926, § 302(d) (predecessor of I.R.C. § 2038 (1986)). Like § 2038, 20 PA. CONS. STAT. ANN. § 2203 and UPC § 2-202—but unlike EPTL § 5-1.1(b)(1)(E)—section 302(d) does not provide that the power must be retained by the express provisions of the instrument.

79. *Helmholz*, 296 U.S. at 96. In so holding, the Court did not consider whether a power to terminate was the equivalent of a power to revoke. However, in a subsequent decision, the Court held that a power to terminate was included in the statutory words "alter, amend, or revoke." See *Commissioner v. Estate of Holmes*, 326 U.S. 480, 487-88 (1946) (concluding that 1936 amendment to Revenue Act of 1926 § 811(d) to add the word "terminate" to the phrase "alter, amend, or revoke" was only a codification of existing law). A power to terminate is the equivalent of a power to revoke if the property interest transferred will revert to the decedent; however, if a power to terminate is "exercisable as to effect a change in enjoyment," it is the equivalent of a power to alter. See Treas. Reg. 105, § 81.20 (predecessor of Treas. Reg. § 20.2038-1(a)(2) (as amended in 1962)).

80. *Id.* at 97 (emphasis added). The Court cited the Restatement of Trusts §§ 337 (allowing termination of trust by consent of beneficiaries) and 338 (permitting termination of trust by consent of settlor and beneficiaries). RESTATEMENT OF TRUSTS §§ 337, 338 (1935). See *Helmholz*, 296 U.S. at 97 n.3. As these sections make clear, the Court's reference to "all parties in interest" must include the settlor. Under the general rule, the settlor's consent is indispensable to terminate a trust if its continuance is necessary to carry out a material purpose of the trust. Thus, only if the settlor consents can all the beneficiaries (assuming they are not under an incapacity) compel a termination of the trust, "although the purposes of the

Accordingly, although a clause in the trust instrument expressly provided for termination by all the living beneficiaries (who included the settlor, a life beneficiary), the Court concluded that there was no reserved power to revoke within the meaning of the statute, because the termination clause "added nothing to the rights which the law conferred."⁸¹ Although the trust literally was subject to the exercise of a power to revoke in conjunction with the other benefi-

trust have not been accomplished." See RESTATEMENT OF TRUSTS § 337 comment a and § 338(1) (1935). See also RESTATEMENT (SECOND) OF TRUSTS §§ 337 and 338 (1959) (containing same provisions).

The Court may have overstated the general rule which applies only if all parties in interest are not under an incapacity. See RESTATEMENT OF TRUSTS § 337 (1935); RESTATEMENT (SECOND) OF TRUSTS § 337 (1959). The Court appears to have erred in equating the general rule with the trust provision in that the trust provision apparently permitted termination by all the then living beneficiaries without the consent of unborn beneficiaries. See 5 B. BITTKER, *supra* note 62, at 126-69 (arguing that Court erred because decision permits living beneficiaries to cut off rights of unborn ones); Note, 53 HARV. L. REV. 690, 691 (1940). If so, then the termination clause in *Helmholz* did add to the rights of the parties under local law. 5 B. BITTKER, *supra* note 62, at 126-69. New York does not follow the general rule. See *supra* note 59 and accompanying text (discussing New York State law). The fact that the decedent in *Helmholz* retained a life interest with a general testamentary power of appointment did not make her the equivalent of a sole beneficiary. See 2 A. SCOTT & W. FRATCHER, SCOTT ON TRUSTS § 127.1 (4th ed. 1987). For a discussion of when a settlor is the sole beneficiary of a trust, see *id.* at § 127.1.

81. 296 U.S. at 97. This interpretation of *Helmholz* appears to be the most reasonable and has wide support. See, e.g., Treas. Reg. § 20.2038-1(a) (2) (as amended in 1962) (codifying *Helmholz* decision and specifically providing that section 2038 does not apply "[i]f the decedent's power could be exercised only with the consent of all [interested parties,] . . . and if the power adds nothing to the rights of the parties under local law"); *Hauptfuhrer's Estate v. Commissioner*, 195 F.2d 548, 551 (3d Cir.), *cert. denied*, 344 U.S. 825, 826 (1952) (stating that *Helmholz* rule incorporated into Treasury Regulation 105, § 81.20 [predecessor of Treas. Reg. § 20.2038-1(a)(2) (as amended in 1962)]); *Estate of Siegel v. Commissioner*, 74 T.C. 613, 627-28 (1980) (stating that Treas. Reg. § 20.2038-1 embodies Supreme Court approach in *Helmholz*); *Houghteling v. Commissioner*, 40 B.T.A. 508, 513-14 (1939) (citing *Helmholz* as support for rule that all parties in interest may terminate trust if local law so provides); B. BITTKER & E. CLARK, FEDERAL ESTATE AND GIFT TAXATION 202 (5th ed. 1984) (arguing that Treas. Reg. § 20.2038-1(a) codifies *Helmholz* rationale that section 2038 does not apply); Wolk, *The Pure Death Benefit: An Estate and Gift Tax Anomaly*, 66 MINN. L. REV. 229, 260 n.167 (1982) (stating Treas. Reg. codified by *Helmholz* rule); 1 R. PAUL, FEDERAL ESTATE AND GIFT TAXATION 1078-79 (1942); R. PAUL, SELECTED STUDIES IN FEDERAL TAXATION 10 n.16 (2d ser. 1938). The meaning of *Helmholz* is not entirely free from doubt. In *Commissioner v. Allen*, the court interpreted *Helmholz* as holding that "the case was not within the intent of the statute" because the decedent-settlor's power to terminate in conjunction with others "came to her as one of the beneficiaries and not as the settlor." *Commissioner v. Allen*, 108 F.2d 961, 965 (3d Cir. 1939), *cert. denied*, 309 U.S. 680 (1940). *Id.* (citing *Helvering v. Helmholz*). The settlor in *Helmholz*, the *Allen* court explained, "had irrevocably parted in his [sic] lifetime, so far as any power, on his part as settlor, to terminate the trust was concerned." *Allen*, 108 F.2d at 965. The power in the beneficiaries as such, therefore, could not be a power contemplated by the statute because otherwise, the *Allen* court said, Congress, in these circumstances, would be "violating the Fifth Amendment. . . ." *Id.* In short, according to *Allen*, "[t]he thing of importance in the *Helmholz* case was that the power of revocation there rested with the beneficiaries and not with the settlor as such." *Id.* Viewing *Helmholz* in this light, *Allen* concluded that *Helmholz* did not distinguish "between a settlor's power to revoke when imposed by law and a settlor's like power when reserved by his trust indenture." *Id.* See also *Howard v. United States*, 125 F.2d 986, 989 (5th Cir. 1942) (apparently relying on *Allen*, the court refused to construe the *Helmholz* case as holding that "Section 302(d) distinguishes between a power to revoke derived from the donor's own act, and an identical power vested in him by state law;"

ciaries, the trust was considered irrevocable for estate tax purposes, because the decedent, together with the beneficiaries, possessed that power under state law.⁸²

Neither the parties nor the court in *Riefberg* cited *Helmholz*.⁸³ The court thus lost an opportunity to consider not only this specifically analogous case, but also the broader issue of whether federal estate tax decisions should be relied upon in interpreting elective share statutes. There is a legitimate basis for arguing that courts should extend decisions under the federal estate tax statutes, such as *Helmholz*, to similarly worded statutes governing a surviving spouse's right of election. To be sure, the overall objectives of the estate tax⁸⁴ (to raise revenue and prevent large accumulations of wealth) are different from elective share statutes (to protect the surviving

it simply stated that *Helmholz* involved a trust terminable by all beneficiaries, overlooking the point that the settlor was a beneficiary).

Allen's explanation of *Helmholz* appears to miss the mark. *Helmholz* never addressed the question of whether the decedent's power of termination in conjunction with the other beneficiaries was a power she retained in her capacity as a beneficiary and not in her capacity as settlor. Indeed, if the capacity in which the decedent retained the power of termination was decisive, the Court simply would have said that the statute required that the decedent retain the power in her capacity as settlor and does not apply to a power retained in any other capacity. But it did not do so. Instead, in responding to the government's argument, the Court implicitly assumed that the capacity in which the decedent held the power was irrelevant to the case. Furthermore, subsequent to the *Helmholz* decision, courts have indicated with respect to transfers covered by section 302(d) of the 1926 Revenue Act, that the capacity in which decedent has retained the power to terminate is immaterial. *See, e.g., Du Charmé's Estate v. Commissioner*, 164 F.2d 959, 963 (6th Cir. 1947), *modified*, 169 F.2d 76 (6th Cir. 1948) (decedent's reserved power exercisable in capacity as trustee); *Jennings v. Smith*, 161 F.2d 74, 77 (2d Cir. 1947) (same); *Union Trust Co. v. Driscoll*, 138 F.2d 152, 154 (3d Cir. 1943), *cert. denied*, 321 U.S. 764 (1944) (decedent's retained power to alter beneficiaries' interests exercisable in her capacity as trustee); *Welch v. Terhune*, 126 F.2d 695, 697 (1st Cir.) (stating that section 302(d) of Revenue Act of 1926 "refers to the existence of the power in the decedent, not to the capacity in which it is to be exercised"), *cert. denied*, 317 U.S. 644 (1942). *See also* Treas. Reg. 105, § 81.20(a)(2) (as amended in 1954) (the addition to section 302(d)(1) of the Revenue Act of 1926, as amended, "of the phrase to the effect that it is not material in what capacity the power was subject to exercise by the decedent or by the other person or persons in conjunction with the decedent . . . is considered merely declaratory of the meaning of the subdivision prior to the addition of the phrase"). *Accord* *Jennings v. Smith*, 161 F.2d 74, 77 (2d Cir. 1947) (holding that absence of language "in whatever capacity exercisable" in I.R.C. § 811(d)(2) (1936) is not significant); *Commissioner v. Newbold Estate*, 158 F.2d 694 (2d Cir. 1946) (same). *Cf.* Treas. Reg. § 20.2036-1(b)(3) (as amended in 1960) (absence of language "in whatever capacity exercisable" in section 2036 is immaterial and this provision reaches powers retained by the settlor in his capacity as trustee).

82. But when a trust is revocable under state law unless the settlor expressly provides that it is irrevocable, as, for example, in Texas, the corpus is includible under I.R.C. § 2038 (1986). Treas. Reg. § 20.2038-1(a) (as amended in 1962); *See Hill's Estate v. Commissioner*, 64 T.C. 867 (1975) (applying Texas law); TEX. REV. CIV. STAT. ANN. art. 7425b-41 (1960); *infra* note 137.

83. A second ground for the Court's decision in *Helmholz* not to apply section 302(d), and, in the words of Mr. Justice Roberts, the "more serious objection," was that any retroactive application of this section would violate the fifth amendment. Three Justices (Brandeis, Stone and Cardozo) concurred in the result only on this ground. 296 U.S. at 98.

84. Congress initially enacted the federal estate tax in 1916 to raise money to prepare the military for World War I. *See* 5 B. BITTKER, *supra* note 62, at 120-1 to 120-2 & n.1.

spouse and recognize the economic partnership aspects of marriage); consequently, depending on the issue involved the courts may have reasons not to utilize tax oriented approaches in the elective share area.⁸⁵ But to the extent the specific objective of tax and elective share statutes is the same (to capture transfers of property in which the settlor retains certain powers or interests), cases in one area are pertinent in the other. For example, the Tax Court has said that the objective of section 2038 "is to include in a decedent's gross estate the value of transferred property over which the decedent has retained a prohibited degree of control."⁸⁶ This is precisely the objective of EPTL section 5-1.1(b)(1)(E) and UPC section 2-202.⁸⁷ Thus, case law interpreting the federal estate tax statute should be relevant in interpreting similarly worded state elective share statutes.⁸⁸ Of course, the fact that certain lifetime transfers are not taxable for estate tax purposes because they are taxable as gifts⁸⁹ militates against wholesale acceptance of tax decisions in the elective share area.⁹⁰ Additionally, because of the public policy reflected by elective share statutes—protection of the surviving spouse and recognition of marriage as an economic partnership⁹¹—close cases should be resolved in favor of inclusion. This choice may not be as important in the tax area because of the interplay between the estate and gift taxes.

85. See, e.g., UPC § 2-202, 8 U.L.A. 77-79 comment (1983) (stating that objective of UPC is to protect against spousal disinheritance); *supra* note 17 (discussing correlation between federal estate tax statutes and elective share statutes).

86. Estate of Bell v. Commissioner, 66 T.C. 729, 736 (1976), *acq.*

87. See REPORT, *supra* note 5, at 117-18, 124 (stating that REPORT discusses transfers of property in which decedent has retained power of revocation); UPC § 2-202, 8 U.L.A. 75-78 comment (1983) (stating that purpose of UPC is to allow right of election against transfers readily usable to defeat elective share).

88. See Kurtz, *supra* note 1, at 1028 & n.229 (applying Treas. Reg. § 20.2038-1(a)(2) (as amended in 1962) and *Helmholz* to an analysis of UPC § 202(1)(ii)(1983)). It is noteworthy that New York also has followed *Helmholz* in interpreting New York's estate tax law which is patterned after the federal law. See *In re Falconer's Estate*, 47 N.Y.S.2d 35, 37 (N.Y. Surr. Ct. Co. 1944). The court, stating that *Helmholz* "is directly controlling," held that a trust that provided that it was revocable only upon consent of all the beneficiaries was not includible in the New York State gross estate under the section of New York's law that was derived from former I.R.C. § 302(d). *Id.*

89. Transfers by which a taxpayer relinquished sufficient control and did not retain certain prohibited powers normally are taxable as a gift. For example, had the trust in *Helmholz* been created after the enactment of the gift tax statute, the remainder interest in the beneficiaries would have been taxable as a gift.

90. Lifetime and testamentary transfers made after 1976 are now taxed at the same rate under the unified tax structure of I.R.C. § 2001 (West Supp. 1987). Prior to 1977, they were taxed at different rates. See I.R.C. § 2001 (1986).

91. See *supra* note 5 and accompanying text (discussing purpose of forced share statutes).

V. APPLICATION OF *HELMHOLZ* TO ELECTIVE SHARE STATUTES

A. Trusts

The rationale in *Helmholz*⁹² can be used to determine the scope of elective share statutes. For example, if the *Helmholz* approach were applied,⁹³ neither hypothetical trust would be includible under the New York statute, the UPC, or other similar state elective share statutes. Thus, unlike the *Riefberg* approach, the *Helmholz* rationale would not produce inconsistent results in our hypothetical trust cases. The relevant question, therefore, is whether the rationale of *Helmholz* should be applied in the elective share area.

The Supreme Court in *Helmholz* offered no explanation for its decision to exclude a transfer if the express power to terminate was coextensive with the power conferred by local law. After indicating that there is an essential difference between "a condition which the law imposes" and a "power to revoke," the Court simply stated that "Congress cannot tax as a transfer intended to take effect in possession or enjoyment at the death of the settlor a trust created in a state whose law permits all the beneficiaries to terminate the trust."⁹⁴ The Court seems to be saying that a power of the settlor with all the beneficiaries to terminate, granted by operation of local law, is not the type of power to which section 2038(a)(1) (or section 302(d) before it) is addressed. Rather, to cull from the *Helmholz* opinion, it is "a condition which the law imposes." Thus, if the settlor, by the trust instrument, has made what is, on its face, a complete and irrevocable transfer, the trust will not be treated as a revocable transfer merely because local law steps in and confers a power of termination. Implicit in the Court's decision appears to be the idea that the settlor is unable, by inserting language in the trust instrument or in any other way, to prevent such a power from being conferred. For if the settlor, by inserting appropriate language in the trust instrument, could preclude the law from conferring a power to terminate the trust, it would seem that the power is not "a condition which the law imposes."⁹⁵ Only if it is the settlor's deliberate choice of omitting language that would be effective to make the trust revocable without his participation should the corpus of the trust be included

92. See *supra* notes 76-83 and accompanying text (discussing Court's reasoning in *Helmholz*).

93. See *supra* text accompanying notes 57-58.

94. *Helvering v. Helmholz*, 296 U.S. 93, 97 (1935). See *supra* note 80 and accompanying text.

95. See *supra* note 80 and accompanying text (discussing *Helmholz* Court's analysis of power to revoke).

in the net estate for elective share purposes.⁹⁶

The relevant question, therefore, in determining whether Trusts 1 and 2 should be included in the net estate under an elective share statute, such as EPTL section 5-1.1(b)(1)(E) or UPC section 2-202(1), is whether the settlor can insert in the trust instrument an enforceable provision that prevents the termination of the trust under any circumstances or permits its termination with the consent of all beneficiaries but without the settlor's consent. One obvious possibility is that the settlor expressly provide that the trust is irrevocable. The law is well settled, however, that a provision stating that the trust is irrevocable will not suffice to strip the settlor of the right conferred by local law to terminate the trust with the trust beneficiaries' consent.⁹⁷ Another possibility is that the settlor include a provision in the trust instrument that, for purposes of terminating the trust, he should be regarded as deceased. At first blush, this might appear to render the trust irrevocable, because all trust beneficiaries cannot terminate a trust by their consent if the settlor is deceased and a material purpose of the trust remains to be accomplished.⁹⁸ However, because the settlor in fact is alive, his consent to terminate can still be secured. Accordingly, such a provision probably would not render the trust irrevocable, because courts have no interest in maintaining a trust where all interested parties wish to terminate it.⁹⁹

Another possibility is for the settlor to relinquish all control over the trust property by providing in the trust instrument that the trust may be terminated with the consent of only the beneficiaries. In such a case, the settlor would not retain a power to terminate in conjunction with the beneficiaries because, by the express terms of the trust, the beneficiaries would not need his consent to terminate. Stated otherwise, the settlor's consent to termination is superfluous and the general rule (or a statute such as EPTL § 7-1.9(a)) never

96. In such a case the corpus should also be includible in the settlor's gross estate for federal estate tax purposes under I.R.C. § 2038 (1986).

97. 4 A. SCOTT, *supra* note 58, at § 338 (stating that trust may be terminated upon agreement of settlor and beneficiaries); RESTATEMENT (SECOND) OF TRUSTS § 338 comment a (1959) (stating general rule applicable even if trust provides that it is irrevocable). See *In re Schroll*, 297 N.W.2d 282, 283-84 (Minn. 1980) (holding that when trust instrument provided that "[g]rantor has carefully considered the desirability of reserving the right to modify, amend or revoke . . . and now declares that such trust shall not be subject to revocation or amendment," trust could be "modified where the settlor and all beneficiaries agree") (citing *In re Warner's Trust*, 263 Minn. 459, 456-57, 117 N.W.2d 224, 229 (1962)).

98. 4 A. SCOTT, *supra* note 58, at § 337; RESTATEMENT (SECOND) OF TRUSTS § 338 comment a (1959). See *supra* note 80 (discussing conditions under which trust can be terminated).

99. See P. HASKELL, PREFACE TO WILLS, TRUSTS & ADMINISTRATION 227 & n.11 (1987) (stating that settlor can terminate trust with beneficiaries' consent); 4 A. SCOTT, *supra* note 58, at § 338 (stating same).

comes into play.¹⁰⁰ If this approach is available and the settlor *can* insert a provision in the trust that would preclude a power to terminate from arising by operation of law, the *Helmholz* rationale should not apply to either hypothetical trust.¹⁰¹ Indeed, if the settlor chooses to retain (by failing to negate the operation of local law) what amounts to a veto power over termination by the beneficiaries, there is no justification for applying the *Helmholz* approach to the elective share statutes. Thus, both Trusts 1 and 2 should be subject to inclusion.

Apart from the reasons discussed above, no logical explanation exists to differentiate between Trusts 1 and 2, because in both cases the settlor retains the *identical* power—the power in conjunction with the beneficiaries—to terminate the trust. In both cases the decedent has made the same lifetime disposition of his assets and the same result should obtain in each case.¹⁰² This is similar to the reasoning the Supreme Court used in *Estate of Spiegel v. Commissioner*¹⁰³ to interpret a federal estate tax statute, a predecessor of section 2037, that taxed transfers taking effect at death.¹⁰⁴ There, the Supreme Court treated a reversionary interest arising by operation of law the same as a reversionary interest that the decedent “deliberately reserves” by the express terms of the instrument.¹⁰⁵ “In either event,” as Justice Black stated, “the settlor has not parted with all of his . . . interests in the property transferred.”¹⁰⁶ As a consequence:

[O]ne can hardly quarrel with the conclusion that an interest arising by “operation of law” is no less significant than one expressly reserved. Both “types” of reversionary interests are created by the words used in the trust instrument and both are legally effective only by “operation of law,” i.e., because a court will attach legal consequences to the words used in the instrument and enforce the grantor’s claim. Restated, the distinction is between

100. If, as in *Helmholz*, the settlor is also a beneficiary, the trust instrument should expressly provide that it is revocable by all beneficiaries other than the settlor.

101. Based on this analysis, *Helmholz* should have been decided differently. For, it was the settlor’s failure to eliminate the power to terminate that arises by operation of law that resulted in the settlor’s retention of a power to terminate in concert with the beneficiaries. Under these circumstances, the power should have been considered a retained power to revoke within the meaning of the statute and not a “condition which the law imposes.” *Helvering v. Helmholz*, 296 U.S. 93, 97 (1935).

102. The same question can be posed regarding two contracts—one which contains a provision for termination by mutual consent (the *Riefberg* case)—and one which does not but, nevertheless, can be terminated by mutual consent because the law confers this right. See *supra* note 51 and accompanying text (citing RESTATEMENT (SECOND) OF CONTRACTS § 311 comment a (1981)).

103. 335 U.S. 701, 707 (1944).

104. Int. Rev. Act of 1939, § 811(c).

105. *Estate of Spiegel v. Commissioner*, 335 U.S. 701, 705 (1944).

106. *Id.*

rights which are conferred by a court because the grantor has used well-chosen words and those which are conferred because the grantor has combined well-chosen words with judicious silence. So restated, the distinction reflects no difference.¹⁰⁷

Because there appears to be no legitimate reason to differentiate between a transfer with a power to terminate retained by operation of local law and a transfer with a power to terminate retained by the express terms of the instrument, both transfers should produce identical results under an estate tax statute¹⁰⁸ or an elective share statute such as the UPC. The New York elective share statute, however, seems to require a different result,¹⁰⁹ because a power to terminate arising by operation of local law appears not to be a power retained "by the express provisions of the disposing instrument." This result, as explained, is inappropriate.¹¹⁰

Let us now examine a slightly different situation. Assume that A transfers property to B in trust to pay the income to A for life and the remainder to A's heirs under a trust instrument which provides that it is irrevocable. If A is considered the sole beneficiary,¹¹¹ most jurisdictions permit A to terminate the trust.¹¹² For reasons explained above, under the UPC and the Pennsylvania statute the de-

107. Bittker, *The Church and Spiegel Cases: Section 811(c) Gets a New Lease on Life*, 58 YALE L.J. 825, 834 (1949). Section 2037 no longer distinguishes—as it did for transfers made prior to October 8, 1949—between a transfer in which a reversionary interest is retained by operation of law or by the express terms of the instrument. Both are specifically included if the value of the reversionary interest immediately before death exceeds five percent of the property transferred.

108. If not for the fact that the *Helmholz* decision, limited to its facts, has been codified in Treasury Regulations since 1939, the decision should not be followed for the reasons explained in the text. Today, the *Helmholz* approach is not very meaningful in the tax area, because if *Helmholz* is followed, the transfer will be taxed under the gift tax statute and not under the estate tax statute. See *supra* note 89 and accompanying text. If *Helmholz* is not followed, then the transfer would be taxed under the estate tax statute and not under the gift tax statute. In either event, the transfer is taxed at some point and, were it not for the "tax exclusive" nature of the gift tax computation, at essentially the same rates. See *supra* note 90 and accompanying text. It should also be noted that the Regulations codifying *Helmholz* as to post-June 22, 1936 transfers are apparently in conflict with the express language of section 2038 as it applies to those transfers. As quoted above, section 2038(a)(1) applies to a power to terminate "without regard to when or from what source the decedent acquired such power" (emphasis supplied). See *supra* note 74 and accompanying text.

109. In our guidelines, we recommend that the New York statute be amended to cover all transfers in which the settlor retains a power to terminate either by the express terms of the instrument or by operation of law. See *infra* text accompanying notes 267-72.

110. See *supra* note 62.

111. This would be the case in jurisdictions that apply the doctrine of worthier title. See 2 A. SCOTT & W. FRATCHER, *supra* note 80, at § 127; RESTATEMENT (SECOND) OF TRUSTS § 127 (1959). Interestingly, New York has codified the doctrine with respect to termination of a trust under EPTL § 7-1.9(a). Thus, for purposes of such revocation a disposition to the settlor's "heirs" or "next of kin" does not create in those classes of persons a beneficial interest. EPTL § 7-1.9(b) (McKinney Supp. 1988). For all other purposes the "heirs" of the settlor take by purchase. EPTL § 6-5.9 (McKinney 1967).

112. 4 A. SCOTT, *supra* note 58, at § 339; RESTATEMENT (SECOND) OF TRUSTS § 339 (1959).

cedent is deemed to have retained a power of termination thereby subjecting the transfer to the surviving spouse's right of election.¹¹³ However, under the New York elective share statute, which requires the decedent to retain the power by the express terms of the disposing instrument, the opposite result would be reached. Such an outcome, of course, is senseless. To avoid that consequence, New York courts should take the position that in light of EPTL section 10-10.6¹¹⁴—which treats a settlor with a power to terminate as the owner of the transferred property for creditors' rights purposes—the decedent never disposed of the remainder interest for purposes of the elective share statute. Such a trust should not be viewed as a transfer with a retained power but instead, as a transfer with both a retained life estate and a retained reversion that is subject to the elective share statute.¹¹⁵

B. Contracts

Turning from transfers in trust, we now address the question of whether the *Helmholz* approach should apply to contractual transactions. Interestingly, this approach has not been employed in determining whether a contractual transaction creates an asset that is includible in a decedent's gross estate for federal estate tax purposes. *Estate of Tully v. United States*¹¹⁶ is illustrative. In that case, Tully and his employer entered into a contract that obligated the

113. See *supra* note 108 and accompanying text.

114. EPTL § 10-10.6 (McKinney 1967) applies when the settlor merely "reserved" a power to revoke, without requiring a reservation by the express terms of the disposing instrument. Thus, a power reserved by operation of local law may be deemed a power reserved by the settlor if the settlor, by appropriate language, could have precluded such a power. In the hypothetical trust, the settlor perhaps could avoid the effect of EPTL § 7-1.9(b) by providing that the "heirs" shall be deemed to have a beneficial interest for all purposes including revocation. Even if the settlor is powerless to make the disposition irrevocable, it can be argued that the settlor reserves a power to revoke anytime he makes a disposition in any manner as to give rise to such a power. See *infra* notes 137-38 and accompanying text.

115. One can argue that a surviving spouse should have at least the same rights as a creditor in any property which the decedent transferred during life. In Rohan's view a court might rule that "the right to revoke is contained in the agreement itself because the settlor is put on notice of the effect of such a provision [EPTL § 7-1.9(b)] and therefore the right to revoke is, in reality, an express provision in the disposing instrument; the latter would appear to be the better view." 9A P. ROHAN, NEW YORK CIVIL PRACTICE-EPTL § 5-1.1(7)(b), at 5-124 (1986). However, Rohan cites no support for "the better view" and in fact, his view would render ineffective the statutory words "by the express provisions of the disposing instrument." But compare P. ROHAN, PRACTICE COMMENTARY TO 17B MCKINNEY'S CONSOLIDATED LAWS OF NEW YORK ANNOTATED § 7-1.9, at 110 (Supp. 1988) ("The two sections [EPTL §§ 7-1.9(b) and 6-5.9], read together, then abolish the doctrine of Worthier Title and vest a remainder in the grantor or settlor's heirs, subject to the caveat that (if the interest created in them is equitable) the settlor can nevertheless revoke the trust without their consent, even without having reserved such power."). Indeed, the cases indicate that such a right to revoke would be characterized as arising by operation of law and not by the express provisions of the instrument. See *infra* notes 137-38 and accompanying text (discussing Massachusetts and Louisiana law).

116. 528 F.2d 1401 (Ct. Cl. 1976).

employer to pay certain death benefits to Tully's widow.¹¹⁷ Although there was no express reservation of a power to revoke this death benefit contract, the government claimed that the death benefits were includible in Tully's estate under I.R.C. section 2038.¹¹⁸ In rejecting the government's position, the court said that the possibility that Tully, in conjunction with his employer, "*might*" have revoked the death benefit contract was not determinative because the word "power" as used in section 2038(a)(1) "does not extend to *powers of persuasion*."¹¹⁹ The court, expressing what appears to be the true basis for its decision, also noted its concern that extending the statute to such a possibility would mean that all death benefit plans would be includible in the federal gross estate.¹²⁰ In light of the numerous cases excluding death benefit plans, the court concluded that "Congress did not intend the 'in conjunction' language of section 2038(a)(1) to extend to the mere possibility of bilateral contract modification."¹²¹

Tully's rationale should not be employed either for purposes of the right of election or section 2038. If that rationale were correct, then every trust situation in which the decedent reserved a power to revoke in conjunction with another person¹²² would fall beyond the reach of section 2038 and of the elective share statutes because it

117. *Estate of Tully v. United States*, 528 F.2d 1401, 1402 (Ct. Cl. 1976).

118. *Id.* at 1402. The court did not state the grounds for the government's claim, but apparently the government had argued that, as a matter of general contract law, Tully "kept a power" in conjunction with the employer to "'alter, amend, revoke or terminate' . . ." *Id.* at 1404-05. Nor did the court consider whether the general rule was inapplicable because Tully's widow might have been an intended beneficiary of the death benefits. *See Estate of Siegel v. Commissioner*, 74 T.C. 613, 616 (1980); *supra* notes 53 and 55 (discussing rights of beneficiaries under RESTATEMENT (SECOND) OF CONTRACTS). The government also argued that the death benefits were includible in Tully's gross estate under section 2033 as a general asset owned at death. *Estate of Tully*, 528 F.2d at 1406.

119. *Estate of Tully*, 528 F.2d at 1404 (emphasis in original). The court reasoned that if the word "power" included the possibility that Tully could convince his employer to change the contract, the statute would apply to "*speculative powers*." *Id.* at 1404-05 (emphasis in original).

120. *Estate of Tully v. United States*, 528 F.2d 1401, 1405 (Ct. Cl. 1976). This would have been contrary to the general exclusion of such benefits under section 2039 as it was then written.

121. *Id.* The court cited no legislative history to support its conclusions. *See also* Tech. Adv. Mem. 87-01-003 (Sept. 19, 1986).

Parenthetically, the death benefits contract was amended once by the parties. The court noted that there was no evidence to show that Tully had the power to coerce this modification but rather at best it seemed "that the parties were mutually convinced that the clarification was desirable." *Estate of Tully*, 528 F.2d at 1405 n.9.

122. The *Tully* reasoning should apply with equal force even if the death benefit plan expressly granted Tully a power to revoke the plan, exercisable only in conjunction with the employer. This was the case in Tech. Adv. Mem. 87-01-003 (Sept. 19, 1986). *But see Estate of Siegel v. Commissioner*, 74 T.C. 613 (1980). Applying the *Tully* rationale to *Riefberg* would mean that the stockholders agreement should not be includible in the net estate for elective share purposes because the reserved power was no more than a "power of persuasion." The *Riefberg* court did not consider this approach, nor was it called to its attention.

could be said that the decedent reserved only a "power of persuasion," whether or not the other person is an adverse party.¹²³ This result would fly in the face of the express language of section 2038 and the elective share statutes that cover transfers in which a power is retained "in conjunction with another."¹²⁴ Simply put, the *Tully* court's approach is untenable because section 2038 and the elective share statutes extend to powers that the *Tully* court calls "powers of persuasion" or "speculative powers," that is, the mere possibility of bilateral change.¹²⁵

Significantly, under section 2038, the phrase "in conjunction with another" applies even in cases in which the other person is an adverse party.¹²⁶ This approach should be utilized in the elective share area because, as in the estate tax area, adoption of an adverse party exception could easily lead to subterfuges which would frustrate the purposes of elective share statutes. For example, if an adverse party exception were applicable, a decedent could retain a power to revoke with a sympathetic beneficiary, such as a child or sibling, and insulate the transferred property from the surviving spouse's right of election. This approach was rejected in the estate tax area because of the possibility that "a beneficiary who was of the grantor's immediate family might be amenable to persuasion or be induced to consent to a revocation in consideration of other expected benefits from the grantor's estate."¹²⁷ This reasoning applies with equal force in the elective share area.

123. We are using the term "adverse party" as it is defined in I.R.C. section 672(a) (1986): "any person having a substantial beneficial interest in the trust which would be adversely affected by the exercise or nonexercise of the power which he possesses respecting the trust." I.R.C. § 672(a) (1976).

124. See, e.g., I.R.C. §§ 2036, 2038 (1986); EPTL § 5-1.1(b)(1)(E) (McKinney 1981); UPC § 2-202 (1983).

125. For example, a transfer in which the settlor, as a trustee, retains a power in conjunction with a cotrustee is clearly includible under section 2038. See *Wolk*, *supra* note 82, at 259-60 (noting that employee could use renegotiation power directly to affect interest of beneficiary); Treas. Reg. § 20.2038-1(a) (as amended in 1962) (stating that gross estate includes value of property transferred in trust, if decedent retained power to alter, amend, revoke or terminate); *Helvering v. City Bank Farmers Trust Co.*, 296 U.S. 85, 89-90 (1935) (decided under section 302(d) of the Revenue Act of 1926, predecessor of I.R.C. § 2038 (1986)) (holding that section 302(d) applied to transfer subject to revocation by settlor with consent of another who was beneficiary); *Estate of Farrel v. United States*, 553 F.2d 637, 642-43 (Ct. Cl. 1977) (stating trust property was includible in gross estate for estate tax purposes if settlor retained right to designate herself as trustee and to name beneficiaries). *Tully* has also been explained as involving "powers that become operational as a mere by-product of events of [independent significance], such as decedent's quitting his job or divorcing his wife." 5 B. BITTKER, *supra* note 62, at 126-67 and n.61. This explanation, however, focuses on actions the decedent could have taken unilaterally and overlooks the decedent's power to alter the death benefits contract by agreement with his employer.

126. This is also true in the case of a limitation of a power with a consent requirement, such as a power exercisable by a trustee only with the settlor's consent.

127. *Helvering v. City Bank Farmers Trust Co.*, 296 U.S. 85, 90 (1935).

The *Helmholz* Court's "operation of law" rationale provides a more persuasive justification for the result in *Tully*.¹²⁸ *Tully*'s power in conjunction with his employer to terminate the death benefit contract arose by operation of contract law which gives the contracting parties the right to terminate or modify their agreement.¹²⁹ Since the parties cannot, either in the contract or otherwise, divest themselves of that power, it can truly be characterized as a condition imposed by law and, accordingly, the *Helmholz* rationale should apply.¹³⁰ If such a power were within the scope of section 2038 or an elective share statute, then every contract would be deemed a transfer in which the decedent reserved a power to revoke in conjunction with another party,¹³¹ a result probably not contemplated under either the tax or elective share statutes.¹³²

An interesting estate tax decision, however, points to a different conclusion. In *Howard v. United States*,¹³³ the decedent made certain lifetime gifts to his wife prior to 1926 which, under then existing Louisiana state law, were revocable during the marriage, although the donor did not expressly reserve any power to revoke.¹³⁴ At the time of the husband's death in 1937, the estate tax law extended to all transfers if the enjoyment thereof, at the time of a decedent's death, was subject to change through the decedent's exercise of a power to revoke or terminate.¹³⁵ In holding that the transferred property was includible for estate tax purposes even though the power to revoke was conferred only by operation of local law, the court rejected the argument that exclusion was appropriate because the settlor was powerless to make the transfer truly irrevocable.¹³⁶ As the court stated:

We have been cited no authority, and we are aware of none, to the effect that the Revenue Act has no application to property other-

128. *Tully* neither mentioned *Helmholz* nor considered its rationale.

129. See *supra* note 51 (citing RESTATEMENT (SECOND) OF CONTRACTS § 311 comment a (1981)).

130. See *supra* text accompanying note 80.

131. See, e.g., text *supra* accompanying note 67.

132. Under an elective share statute (like EPTL § 5-1.1(b)(1)), if retention of the power by the express provisions of the instrument were required, the problem would most likely never arise.

133. 125 F.2d 986 (5th Cir. 1942).

134. *Howard v. United States*, 125 F.2d 986, 989 (5th Cir. 1942).

135. Revenue Act of 1926, § 302(d)(1) (as amended in 1934) (predecessor of I.R.C. § 2038 (1986)). The statute also applied to retained powers to alter or amend.

136. The court considered *Helmholz* to be irrelevant. *Howard*, 125 F.2d at 989. It refused to construe *Helmholz* as holding that section 302(d)(1) distinguished between a power derived from the settlor's own act and the same power conferred by state law. *Id.* The only "explanation" it offered was that "[t]he *Helmholz* case involved a gift in trust that, under the state law and the provisions of the trust indenture, was terminable by the joint act of all the beneficiaries." *Id.*

wise subject to the tax because the taxpayer is powerless to deal therewith in a manner that will place it beyond the coverage of the Act.¹³⁷

Nevertheless, in the contract area the *Howard* court approach is not feasible because by operation of law each party to a contract automatically possesses a power to amend or terminate in conjunction with the other party.¹³⁸ Under *Howard*, no contract would be exempt unless the elective share statute contained a phrase such as that in New York ("retained . . . by the express provisions of the disposing instrument").¹³⁹ Naturally, it is fair and reasonable to construe the statute to cover the *Howard* transfer in trust even though the decedent was powerless to make it irrevocable, because the decedent in *Howard* retained total and absolute control over recapturing the transferred property—the decedent required no consent to revoke the transfer. In the contract area, however, the decedent does not retain by operation of law a *unilateral* power to terminate; the consent of another party is necessary to terminate the contract. Under these circumstances, it is neither fair nor reasonable to include property subject to a contract in the net estate if the decedent, for all practical purposes, is powerless to make the transfer irrevocable.¹⁴⁰ Thus, if property subject to a contract is to be

137. *Id.* at 990. *Accord* *Vaccaro v. United States*, 149 F.2d 1014 (5th Cir. 1945) (holding that under Louisiana law, repealed in 1942, decedent's inter vivos gifts to his wife were automatically revocable by husband and thus includible in his gross estate under section 302(d) of the Revenue Act of 1926, as amended by section 811(d) (predecessor of section 2038)); *Estate of Keiffer v. Commissioner*, 44 B.T.A. 1265, 1266 (1941) (holding that under Louisiana law, decedent had "absolute right to revoke" gift she made to her husband in 1930 and thus transfer was includible under "Section 302(d)(1) of the Revenue Act of 1926, as amended . . ."; *but cf.* *Newhall v. Casey*, 18 F.2d 447, 447 (D. Mass. 1927) (holding that under Massachusetts law, husband's absolute gift was revocable; "[t]he mere fact that by operation of [the] law [then in effect] the gift might be revoked by the husband during his lifetime would not be sufficient . . . to bring the gift within section 202(b) [of Revenue Act of 1916], as a transfer intended to take effect in possession or enjoyment after death").

138. Even with a third party beneficiary contract under the First Restatement of Contracts or under the Restatement (Second), if the rights of the third parties have vested, each party would have the power to terminate in conjunction with the other party and the beneficiaries. *See supra* notes 52-53.

139. *See* EPTL § 5-1.1(b)(1)(E) (McKinney 1981). Even if a contract such as a stockholders agreement provided that it may be terminated only by the other party—and assuming that such party's promises were supported by consideration or otherwise enforceable—the contract could be amended by mutual consent of decedent and the other party. *See supra* note 51. Such a power to amend may be treated as a power to dispose retained by the decedent in conjunction with another. However, it is less than realistic to require either party to a contract—particularly one that is part of a business transaction—to give the other party *carte blanche* to terminate or amend the terms of a contract to avoid including property subject to a contract in the net estate. In our guidelines, we advocate that all contracts should be subject to the elective share except to the extent they are made for full and adequate consideration. *See infra* notes 264-66.

140. *See supra* note 137. If the *Howard* rationale were applied to contracts, it might be argued that it also would apply to an absolute gift of property, on the theory that the donor retains a power to revoke the gift in conjunction with the donee. This theory seems untenable.

included in the net estate for elective share purposes, it should not be based solely on the unavoidable power to terminate held by the contracting parties in conjunction with each other.

VI. UNANSWERED FUNDAMENTAL QUESTIONS OF ELECTIVE SHARE STATUTES

Several questions relating to the scope of the elective share statutes have not previously been addressed. In analyzing these unanswered questions, we draw upon interpretations of analogous provisions and concepts in other areas of law.

A. *The Required Transfer, Disposition, or Conveyance*

The first question involves the meaning of the words “transfer” in the UPC, “disposition” in the EPTL, and “conveyance” in the Pennsylvania statute. *Riefberg* did not address the threshold issue of whether the decedent, by entering into the stockholders agreement, made a “disposition of property” within the meaning of EPTL 5-1.1(b)(1)(E).¹⁴¹ The only definition of the word “disposition” is found in the general provisions of the EPTL which defines it as “a transfer of property by a person during his lifetime or by will.”¹⁴² However, no definition is given for the word “transfer.” The same definitional problem exists under the UPC, which uses the word

ble. A contract involves an ongoing relationship in which each party has a degree of control over the other—each needs the other to consent to any change in their relationship with respect to the subject matter of the contract. In contrast, once an absolute gift is made, the donor has no relationship to the property and no control over the donee’s disposition of it. Indeed, the donor’s relationship to the property after the gift is made is no different from any stranger’s relationship to the property. It therefore seems inappropriate to speak of a retained right of revocation in conjunction with the donee. If the donee decides to give the property to the donor, this transaction should properly be characterized as a new gift, not as a revocation of the donor’s gift. Thus, even if the *Howard* rationale were applied to contracts—and it seems that it should not, as discussed in the text—there appears to be no real justification to apply it to absolute gifts.

141. See *supra* note 32 and accompanying text (citing EPTL § 5-1.1(b)(1)(E) (McKinney 1981)).

142. EPTL § 1-2.4 (McKinney 1981). This definition is applicable to section 5-1.1 “unless the context otherwise requires . . .” EPTL art. 1, part 2, at 8. The Practice Commentary and the Revisers’ notes to EPTL § 1-2.4 add nothing to an understanding of the definition, stating only that the term “disposition” is a comprehensive one and includes any transfer whether testamentary or lifetime. P. ROHAN, PRACTICE COMMENTARY TO 17B, MCKINNEY’S CONSOLIDATED LAWS OF NEW YORK ANNOTATED, at 12-13 (1981), and Revisers’ notes, *id.* at 13. Nor does the REPORT shed any light on the definition of “disposition.” And although it uses the terms “conveyance” and “transfer” it does not define them. See REPORT, *supra* note 5, at 110, 139.

Interestingly, the section on renunciation of property interests, EPTL § 2-1.11, contains, for purposes of that section, a statement illustrating the types of transactions included in the term “disposition.” EPTL § 2-1.11, at 248 (McKinney 1981). However, those illustrations are not enlightening for purposes of EPTL § 5-1.1(b)(1)(E).

“transfer” without defining it.¹⁴³

The Restatement of Property defines “transfer” as “the extinguishment of such interests [in land or in a thing other than land] existing in one person and the creation of such interests in another person.”¹⁴⁴ If this definition were applied to the words “transfer” and “disposition” in the UPC and EPTL, these elective share statutes would cover lifetime transactions that extinguish a decedent’s existing interest in property and create the identical interest in that property in the transferee.¹⁴⁵

This requirement is readily satisfied by any transfer in trust, because such a transaction involves existing property in which the decedent’s interest is extinguished and the identical interest is created in others—legal title in the trustee and equitable title in the beneficiary.¹⁴⁶ If the transaction, however, does not involve existing property but the creation of new property interests,¹⁴⁷ would such a transaction fall within this definition of “transfer”? For example, if the decedent entered into a contract, can that act constitute a “disposition” of property under EPTL section 5-1.1(b)(1)(E), a “conveyance” under the Pennsylvania statute,¹⁴⁸ or a transfer under

143. See UPC § 2-202 (1983), 8 U.L.A. 75-77 (1983). Pennsylvania’s statute, which covers “property conveyed by the decedent,” does not present this definitional issue to the same extent because the word “conveyance” is expressly defined to mean “unless the context clearly indicates otherwise an act . . . which . . . is intended to create an interest in real or personal property whether the act is intended to have inter vivos or testamentary operation.” 20 PA. CONS. STAT. ANN. § 2201 (Purdon Supp. 1988). This definition was adopted from section 1 of the UNIFORM PROPERTY ACT and section 11 of the RESTATEMENT OF PROPERTY. See section 11 of the Estates Act, Commissioners Comments; P. BREGY, PENNSYLVANIA INTESTATE, WILLS AND ESTATES ACTS OF 1947, 5051-52 (1949). Bregy states that the word “conveyance” is used in the Estates Act for the same reason it was utilized by the Restatement and the Uniform Property Act. He explains that the Restatement arbitrarily chose this word because at the time “there was need for a term which could be used as to both real and personal property and would include inter vivos transfers as well as devises and bequests” and there was “no such generic legal term with a long-settled artistic meaning.” *Id.* at 5051. The SUGGESTED MODEL DECEDENT’S FAMILY MAINTENANCE ACT contains the following definition of the word “transfer”:

‘Transfer’ includes, but is not restricted to, a transmission of the decedent’s property effected by such methods as gift, gift causa mortis, revocable or irrevocable trust, creation of any joint interest, contract to make a will, and any contract, such as life insurance, under which the decedent purchased benefits payable at his death.

REPORT, *supra* note 5, at 161.

144. RESTATEMENT OF PROPERTY § 13(1) (1936).

145. This seems to be the plain import of the phrase, “any disposition of property made by the decedent,” which appears to contemplate any transaction by which the decedent transfers ownership of existing property. EPTL § 5-1.1(b)(1)(E).

146. See RESTATEMENT (SECOND) OF TRUSTS § 2 comment h and § 17 (1959) (noting that creation of trust involves original property owner, trustee and beneficiary).

147. This occurs when parties enter into a contract—each party creating a contract right—which constitutes property. See *infra* note 156.

148. It is unclear whether the Pennsylvania statute applies to contracts. Section 2201 does not expressly include contracts in the definition of the word “conveyances.” Section 2203 refers only to “property conveyed” and does not mention contracts. Additionally, the

UPC section 2-202¹⁴⁹

Let us examine, for example, a contract for the sale of land. Such a contract extinguishes an interest of the seller and creates that identical interest in the purchaser.¹⁵⁰ Thus, the party who enters into a contract to purchase a piece of land acquires from the seller an equitable interest in the land from the moment the contract becomes effective.¹⁵¹ Since a contract for the sale of land creates an

language of section 2205 provides that "conveyances and *contracts* made by the decedent [for money value] are *excluded* from the provisions of section 2203," 20 PA. CONS. STAT. ANN. § 2205 (Purdon Supp. 1988) (emphasis added), implying that conveyances and contracts are two different things. Nevertheless, if the phrase "property conveyed" in section 2203 is construed literally to exclude contracts then the language of section 2205 excluding contracts for value from the provisions of section 2203 is meaningless. Parenthetically, in *In re Estate of Brown*, the Pennsylvania Supreme Court assumed *arguendo* that the "buy-sell" agreement involved was a "'conveyance' within the meaning of Section 11 . . ." *In re Estate of Brown*, 446 Pa. 401, 412, 289 A.2d 77, 82 (1972) (footnote omitted). See also *In re Estate of Korn*, 332 Pa. Super. 154, 480 A.2d 1233 (1984) (holding that deferred compensation plan that gave employee right to change beneficiary was not a "conveyance" within the meaning of 20 PA. CONS. STAT. ANN. § 2201). The court narrowly construed this section as requiring "either an inter vivos or testamentary operation in the creation of the property interest . . ." *Id.* at 164, 480 A.2d at 1238. The majority reasoned that because the beneficiary designation was revocable, the designation "did not create an inter vivos or testamentary interest." *Id.* (citation omitted). This reasoning is unsound, because if it were accepted, then every conveyance in which the decedent reserved a power to revoke would not constitute a "conveyance" under section 2201—a result precluded by section 2203(a)(3) which plainly contemplates that the word "conveyance" includes conveyances with a reserved power to revoke. Interestingly, the concurring and dissenting opinion took the position that the designation "could only give rise to an expectancy." *Id.* at 166, 480 A.2d at 1239 (Spaeth, J., concurring and dissenting). See P. BREGY, *supra* note 143, at 5864-65; Comment, *Buy and Sell Agreements and the Widow's Rights*, 114 U. PA. L. REV. 1006 (1966) (arguing that shareholder's interest in retaining control of corporation under a buy-sell provision should be balanced against interests of widow); *Spouse's Election-Stock Subject to Buy-Sell Agreement*, FIDUCIARY REV., Sept. 1965, at 3.

149. UPC § 2-202 appears to distinguish between "transfer" and "transfer[] by contract." Compare UPC § 2-202(1), 8 U.L.A. 75-78 (1983) with UPC § 2-202(2)(i). Neither the Code nor the Comments indicate whether the term "transfer" includes a "transfer by contract." Parenthetically, the first tentative draft of the UPC included "property transferred by the decedent . . . by . . . contract or other device under which the transfer became effective at or after decedent's death." Fratcher, *Toward Uniform Succession Legislation*, 41 N.Y.U. L. REV. 1037, 1059 (1966). In addition, Article VI, part 2 of the UPC, entitled "Non-Probate Transfers, Provisions Relating to Effect of Death," which does not mention shareholders agreements or buy-sell provisions, is designed to "authorize[] a variety of contractual arrangements which have in the past been treated as testamentary . . . [and] does not invalidate other arrangements by negative implication." UPC § 6-201, 8 U.L.A. comment at 534-35 (1983).

150. RESTATEMENT OF PROPERTY § 6 comment b, illustration 3 (1936) (explaining that contract for sale of land gives purchaser equitable, but not legal, title immediately after agreement is made). The illustration is somewhat confusing because it states that the contract buyer "immediately acquires an equitable interest but does not acquire a legal interest [in the land] until [the land] is *transferred* to him." *Id.* (emphasis added). Most probably it should have said that the buyer does not acquire the legal interest until the deed is *delivered* to him.

151. This assumes that the contract is specifically enforceable. If it is, and generally land contracts are specifically enforceable (see 6A R. POWELL & P. ROHAN, *supra* note 6, ¶ 925[1]), then an equitable conversion occurs. Thus, in equity, the buyer is considered the owner of the land—holding the purchase price for the seller—and the seller is viewed as holding legal title for the buyer with a claim for the purchase price secured by a lien. See, e.g., *Panushka v. Panushka*, 221 Or. 145, 149-52, 349 P.2d 450, 452-53 (1960) (holding that when equitable conversion occurs purchaser holds equitable title to land and seller holds legal title); *In re*

equitable interest in the purchaser and simultaneously extinguishes that interest in the seller, it should constitute a conveyance under section 2201 of the Pennsylvania statute¹⁵² and, utilizing the Restatement's definition, a disposition under the EPTL and a transfer under the UPC.

Turning now to a buy-sell provision in a stockholders agreement, does each party to the agreement acquire an equitable interest in the stock of the other party from the moment the parties enter into the agreement? First, consider a buy-sell provision in a stockholders agreement that gives each party only an option—as distinguished from a contract to purchase which imposes a duty—to purchase the stock of a deceased stockholder.¹⁵³ Here, no definitive answer can be given. Option contracts relating to land may create an equitable interest in the holder for one purpose, such as the application of the statute of frauds,¹⁵⁴ but not for another, such as the application of the Rule Against Perpetuities¹⁵⁵ or the devolution of property.¹⁵⁶

Governor Mifflin Joint School Auth., 401 Pa. 387, 164 A.2d 221 (1960) (same); S. SIMPSON, J. MALONEY, R. PATTON, 3 AMERICAN LAW OF PROPERTY § 11.22 (A. Casner ed. 1952); Stone, *Equitable Conversion by Contract*, 13 COLUM. L. REV. 369 (1913) (arguing equitable conversion is legal fiction burdening purchaser of land). This result is generally assumed to be based on the maxim that equity regards as done that which ought to be done.

152. See *supra* note 148 (discussing meaning of word "conveyance").

153. Until the purchaser exercises the option by accepting the offer, no contract to purchase exists. See *Lord Ranelagh v. Melton*, 2 Drewyr & Smale 278, 281, 62 Eng. Rep. 627, 628 (V.C. 1864) (stating that until option is exercised, option to lease does not give rise to relation of vendor and purchaser); E. FARNSWORTH, CONTRACTS § 8.7, at 572 (1982).

154. 2 A. CORBIN, CONTRACTS § 418 (1950 & Supp. 1984).

155. *Id.* In order to avoid holding that a long term lease with an option to buy does not violate the Rule Against Perpetuities, at least one court has held that the option creates no interest in the land. See *Keogh v. Peck*, 316 Ill. 318, 333, 147 N.E. 266, 271 (1925) (holding lease with option to buy did not violate Rule Against Perpetuities because options did not create interest in land). But cf. *Morgan v. Griffith Realty Co.*, 192 F.2d 597, 599-600 (10th Cir. 1951) (holding that although option to purchase or repurchase property only "creates rights in personam" it encumbered land, and general rule is that such an option which extends beyond the perpetuities period is void for remoteness), *cert. denied*, 343 U.S. 934 (1952); *Gange v. Hayes*, 193 Or. 51, 64-66, 237 P.2d 196, 201-02 (1951) (same). The result in *Keogh* can also be explained by the Restatement of Property § 395 which excludes an option to purchase the lease premises from the Rule Against Perpetuities as long as the option is exercisable prior to or at the end of the lease term. Such options are not subject to the Rule Against Perpetuities in order to enable the lessee "so to plan for the future as to get the benefits of the full utilization of the land during his lease-term." RESTATEMENT OF PROPERTY § 395 comment a (1944). Accord 6 AMERICAN LAW OF PROPERTY § 24.57 (A. Casner ed. 1952 & Supp. 1977). The general rule stated by § 393 of the Restatement is that options which "would create an interest in land, or in some unique thing other than land" are subject to the Rule. RESTATEMENT OF PROPERTY § 393(b) (1944). The rationale for excluding transactions that are "exclusively contractual" is that they do not involve the "fettering of any property." RESTATEMENT OF PROPERTY § 401, comment a (1944).

156. Many courts have held that an option contract relating to land does not result in an equitable conversion prior to the time the option is exercised. See, e.g., *Brooks v. Yawkey*, 200 F.2d 663, 665 (1st Cir. 1953) (stating option is contract to enter purchase and sale contract in future and does not create interest in real property); *Eddington v. Turner*, 27 Del. Ch. 411,

Nor is there a simple answer where the stockholders agreement contains a buy-sell provision that *requires* the sale of the deceased stockholder's stock. Here, notwithstanding the duty to sell, it is impossible to know during the parties' joint lives who will die first and, thus, who will be the seller and who will be the buyer. Because the obligation to purchase is conditional during the parties' joint lives, arguably no equitable interest is created despite the fact that—in contrast to the option contract—the obligation to sell ultimately becomes unconditional when one stockholder predeceases another. Alternatively, perhaps it can be argued that each party should be deemed to have an equitable interest in the stock of the other party, subject to defeasance of that interest upon death. These different questions can be resolved by amending the statutes to define conveyance, disposition, and transfer as including contracts¹⁵⁷ or giving broad judicial interpretation to such statutory terms.¹⁵⁸

419, 38 A.2d 738, 742 (1944) (holding that equitable conversion does not apply because until option is exercised "no duty rested on anyone in connection with the land"); *Rockland-Rockport Lime Co. v. Leary*, 203 N.Y. 469, 480, 97 N.E. 43, 46 (1911) (stating that since owner did not intend conversion unless option exercised, conversion should not be assumed any earlier than date option exercised); Simpson, *Legislative Changes in the Law of Equitable Conversion by Contract*, 44 YALE L.J. 559, 564 (1935) (noting that unlike England, all American jurisdictions except Rhode Island hold no conversion occurs where option contract is not exercised until after optionee's death). *But cf.* *Cobb v. Commissioner*, 49 T.C.M. (CCH) 1364, 1369, 1372 (1985) (holding that although option agreement between decedent and Cobb for purchase of decedent's farm gave Cobb no interest in land under state law, contract right to purchase was property within meaning of gift tax statute, sections 2501 and 2511 of Internal Revenue Code of [1986] and could be taxable gift when transferred). The gift tax regulations, which were cited by the court, provided that the tax was "applicable only to a transfer of a beneficial interest in property." Treas. Reg. § 25.2511-1(g)(1) (as amended in 1986). In essence, the court said that the conferring of a contract right on another or the creation of a contract right in another is a "transfer of property by gift" under section 2501(a). The Senate Hearings concerning the 1932 Act indicate that the gift tax statute covers "transactions . . . whereby . . . property or a property right is donatively passed to or conferred upon another, regardless of the means or the device employed in its accomplishments." S. Rep. No. 665, 72d Cong., 1st Sess. (1932), reprinted in 1939-1 (Part 2) C.B. 496, 524 (emphasis added).

Both *In re Burk*, 37 Pa. D. & C.2d 528 (1965), which was relied on by *In re Estate of Riefberg*, 58 N.Y.2d 134, 140, 446 N.E.2d 424, 427, 549 N.Y.S.2d 739 (1983), and *In re Estate of Brown*, 446 Pa. 401, 289 A.2d 77 (1972), involved shareholders agreements in which each shareholder had only an option to purchase the deceased shareholder's stock. Neither case passed on the question of whether the agreement was a conveyance within the meaning of section 11 (see *supra* notes 37 and 148). *Brown* noted that specific performance was a proper remedy to enforce buy-sell agreements for shares in closely held corporations. *Id.* at 408-09, 289 A.2d at 81. However, in view of the decisions mentioned above concerning option contracts relating to land, an equitable conversion would most likely not occur prior to exercise of the option in a shareholders agreement.

157. This is the approach suggested in the guidelines. See *infra* notes 264-65 and accompanying text.

158. This is what *Riefberg* implicitly did when it held that the stockholders agreement was covered by EPTL § 5-1.1(b)(1)(E). Similarly, in considering whether the execution of a buy-sell agreement resulted in a taxable "transfer of property by gift" under section 2501, a revenue ruling, without analysis, stated that the mutual promises of the stockholders constitute a transfer of legally enforceable contract rights. Tech. Adv. Mem. 86-12-001 (Sept. 19, 1985). Compare *Cobb*, 49 T.C.M. (CCH) 1364.

Regardless of whether a stockholders agreement technically constitutes a transfer, disposition, or conveyance of property, it is possible to take the approach used in *Brodrick v. Gore* in the estate tax area¹⁵⁹ that a shareholders agreement is still not a transfer, disposition, or conveyance within the meaning of the elective share statutes.¹⁶⁰ In *Brodrick* a partnership agreement for the conduct of an oil and gas business provided that, upon the death of a partner, his interest in the partnership should be sold to the surviving partners for the book value of the interest.¹⁶¹ The court rejected the concept that by entering into the agreement, each partner made a transfer of his interest within the meaning of Internal Revenue Code section 811¹⁶² other than by a bona fide sale for an adequate and full consideration. The court explained that the parties made the agreement to provide for the operation of the business and not to "make any transfer of property in contemplation of death, revocable, or otherwise, within the intent and meaning of the statute."¹⁶³

Although the *Brodrick* court said that no "transfer of property in contemplation of death" was made, as distinguished from no "transfer," the meaning is clear. In the court's view, such an agreement is not the type of transfer encompassed within the statute, because the stockholders entered into it in order to regulate the conduct of a business. A similar approach can be used under an elective share statute which is aimed at transfers designed to defeat the rights of a surviving spouse. Thus, it could be argued that even if a technical transfer of an equitable interest occurs when the parties enter into a stockholders agreement, such an agreement may not constitute a disposition—to quote from *Brodrick*—"within the intent and meaning of the statute."¹⁶⁴ The buy-sell provision should not be viewed as independent of the stockholders agreement but rather as an integral part of an overall agreement for the operation of a business¹⁶⁵ and, therefore, the stock—or its value—would not be includible in the net estate for elective share purposes.

159. 224 F.2d 892 (10th Cir. 1955).

160. The word "transfer" is not defined in the Internal Revenue Code although it is used throughout the Code and most importantly for the purposes of this article in I.R.C. §§ 2036, 2038 (1986).

161. *Brodrick v. Gore*, 224 F.2d 892, 894 (10th Cir. 1955).

162. The predecessor of I.R.C. §§ 2035-38 (1986).

163. *Brodrick*, 224 F.2d at 897. *Accord* Estate of Littick v. Commissioner, 31 T.C. 181, 186 (1958), *acq.*, 1959-2 C.B. 5 (holding that stockholders agreement containing buy-sell provision requiring decedent stockholder's stock to be sold to corporation did not effectuate a "transfer" within the meaning of section 811"). The *Brodrick* court further stated that the agreement "was supported by an adequate and full consideration, within the intent and meaning of the statute." *Brodrick*, 224 F.2d at 897.

164. *Brodrick*, 224 F.2d at 897.

165. See *supra* note 26.

Regardless of the approach taken, however, it is obvious that clarification of elective share statutes concerning contracts is necessary. If protection of the surviving spouse is not to be whittled away, technical definitions should not be employed in those instances where the benefits, such as the proceeds from sale of stock, are derived from a contract right created by the decedent during his lifetime.¹⁶⁶ Similarly, the underlying business reasons for the contract should be irrelevant. Creation of a contract right in another ought to be considered the same as a transfer of existing property for elective share purposes. In both situations, the decedent has granted a property right to another—in the case of the transfer of property by extinguishing rights in the property and in the case of the contract by creating an obligation to another. Nevertheless, even if a contract is considered a transfer or disposition of existing property, the other conditions of an elective share statute must be satisfied before a contract is considered a testamentary substitute for elective share purposes.

B. Transfers for Value

In determining the size of the net estate for elective share purposes, both the UPC¹⁶⁷ and the Pennsylvania statute¹⁶⁸ exclude

166. The courts have generally avoided a technical approach in the tax area in determining whether a given transaction constitutes a transfer of property. This issue has arisen in several contexts. See *Chase Nat'l Bank v. United States*, 278 U.S. 327, 337 (1929); *Estate of Porter v. Commissioner*, 442 F.2d 915, 919 (1st Cir. 1971) (holding that agreement for employer to pay employee's widow upon his death constituted a transfer of property under section 2035); *Kramer v. United States*, 406 F.2d 1363, 1369 (Ct. Cl. 1969) (holding same was transfer under section 2036); *Worthen v. United States*, 192 F. Supp. 727, 733-34 (D. Mass. 1961) (holding same was transfer under section 811(c)(3)). But cf. *Hinze v. United States*, 29 A.F.T.R.2d (P-H) 72-1553, 72-1557 (C.D. Cal. 1972) (finding decedent agreed with corporation to provide annuity to his widow; court concluded that decedent never had property interest and thus "could not make a transfer as contemplated by sections 2036 and 2038").

167. UPC § 2-202(1), 8 U.L.A. 75, 76 (1983 & Supp. 1986) includes in the augmented estate: "[t]he value of property transferred to anyone other than a bona fide purchaser . . . to the extent that the decedent did not receive adequate and full consideration in money or money's worth for the transfer . . ." Interestingly, the UPC excludes any transfer to a bona fide purchaser even if made for less than adequate and full consideration. See UPC § 2-202 (1) comment (discussing purpose for augmenting probate estate in computing elective share).

168. 20 PA. CONS. STAT. ANN. § 2205 (Purdon Supp. 1988) provides in pertinent part as follows: "Conveyances and contracts made by the decedent are excluded from the provisions of section 2203 (relating to right of election. . .) . . . to the extent that the decedent received adequate consideration therefore in money or money's worth." In contrast, section 11 of the Pennsylvania Estates Act as enacted in 1947 (quoted *supra* in note 37), did not expressly exclude transfers for value. One commentator believes that this section "is not limited to voluntary transfers." See P. BREGY, *supra* note 143, at 5861. According to Bregy, the inclusion of transfers for value would not cause hardship except in unusual cases, because no one would give value for property subject to one of the enumerated powers. *Id.* at 5861-62. The mere fact that a statute does not expressly exclude transfers for value, he says, should not automatically mean they are included. This is a matter of statutory interpretation. *Id.* at 5864-65.

transfers for a full consideration in money or money's worth.¹⁶⁹ In contrast, EPTL section 5-1.1(b)(1)(E) simply refers to "any disposition." The New York statute does not expressly limit its coverage to transfers that are not for full consideration (and then only to the extent they are for less than *full* consideration). It is reasonable to construe the term "disposition of property" in the New York statute as excluding any transfer to the extent value in money or money's worth is received. For example, if the decedent disposed of \$300 in assets for which he received \$200 from the transferee, it could be argued that the decedent only disposed of \$100 worth of property; the word "disposition" would then be construed to mean the "net disposition."¹⁷⁰ Such a construction (i) would comport with the Report, which concludes that any transaction " 'made for full consideration in money or money's worth' " is not subject to the right of election,¹⁷¹ and (ii) would be consistent with the federal estate tax scheme,¹⁷² and the UPC and Pennsylvania elective share statutory schemes.¹⁷³

Interestingly, neither the *Riefberg* court nor the parties addressed this issue with respect to the stockholders agreement. If the court had considered the issue and determined that the statute did not apply to transfers for value, it might have concluded that such an agreement was supported by adequate and full consideration¹⁷⁴ and, thus, would not have been includible in the net estate for elec-

169. Presumably "adequate consideration," the term used in the Pennsylvania statute, and "adequate and full consideration," the term used in UPC § 202(1), have the same meaning, notwithstanding that the word "adequate" may connote something less than "full" consideration.

170. *But cf.* P. BREGY, *supra* note 143.

171. REPORT, *supra* note 5, at 138. There is no indication why an express provision to this effect was not included in the draft or final legislation. Parenthetically, there are statutory models such as a North Carolina statute which only cover a "gratuitous transfer." Such statutes, however, should also extend to transfers for nominal consideration, at least in non-business contexts. Otherwise, as pointed out in the Report, virtually every transfer could be excluded simply by providing minimal consideration regardless of its adequacy. *Id.* at 128-29. Additionally, authority exists for the proposition that no consideration exists "where the purported consideration is merely nominal." RESTATEMENT (SECOND) OF CONTRACTS § 71 comment b, illustration 5 (1981).

172. I.R.C. §§ 2036, 2038 (1986). Both sections exclude "a bona fide sale for an adequate and full consideration in money or money's worth." *Id.*

173. Unlike the federal estate tax and the Pennsylvania statute, the UPC does not include a bona fide sale even if made for less than adequate and full consideration. UPC § 2-202(1) (1983) (stating that augmented estate includes "value of property transferred to anyone *other than a bona fide purchaser* . . . to the extent that the decedent did not receive adequate and full consideration . . .") (emphasis added). See also UPC § 2-202 comment (1983) (discussing purpose behind augmented estate approach).

174. See *supra* notes 34-36 and accompanying text (discussing *In re Estate of Riefberg* in which court held stockholders agreement was testamentary substitute within meaning of EPTL § 5-1.1(b)(1)(E)). Cf. *Brodrick v. Gore*, 224 F.2d 892, 897 (10th Cir. 1955) (stating that partnership agreement "was supported by an adequate and full consideration" for federal estate tax purposes).

tive share purposes.¹⁷⁵

Such a conclusion would not be justifiable, however, unless the overall transaction were examined. Generally, in entering into a stockholders agreement containing a buy-sell provision, each party receives valuable contract rights. But, this type of transaction also anticipates the future sale of a deceased shareholder's stock and the payment of the purchase price for that stock by the surviving shareholders. In determining whether the decedent made a transfer for full consideration under an elective share statute, which excludes (expressly or otherwise) transfers made for a full and adequate consideration, a court should focus on the value to be received by the decedent shareholder for the ultimate sale of decedent's stock and not simply on the value of the contract rights that the decedent shareholder received from the other shareholder under the agreement.

Indeed, any transfer of property by contract in which a decedent has a life interest or a reserved power should be deemed made for full and adequate consideration under an elective share statute¹⁷⁶ only if full value is received for the underlying property transferred and not simply for the retained interests or powers.¹⁷⁷ In the area of contracts, full consideration should be interpreted to mean that the decedent receive full consideration for any property actually transferred pursuant to the contract rights and not just for the contract rights alone.¹⁷⁸

175. This conclusion has been reached in the gift tax area. See Tech. Adv. Mem. 86-12-001 (Sept. 19, 1985) (stating stockholders agreement was not subject to gift tax statute, because each stockholder owned one-half of shares in corporation and thus contract rights transferred by each stockholder to other were deemed to equal in value). *Id.*

176. This assumes that the statute reaches the value of the property transferred if the decedent reserved a life interest such as under the UPC. See UPC § 2-202(1)(i) (1983) (stating that estate augmented by transfer in which decedent retains possession or enjoyment of, or right to income from, property).

177. Although addressing a different issue, the concurring opinion in *United States v. Allen*, 293 F.2d 916 (10th Cir.), *cert. denied*, 368 U.S. 944 (1961), is instructive. The court held that the principal of a trust was includible in the decedent's gross estate under I.R.C. § 811(c) (1939) (predecessor of I.R.C. § 2036(a)(1) (1986)) as a relinquishment of a retained life interest in contemplation of death even though the decedent as settlor of the trust made a bona fide sale of her reserved life estate for the full value of that life interest. The concurring opinion explained:

The fact that full and adequate consideration was paid for the transfer of the retained life estate is immaterial. To remove the trust property from inclusion in decedent's estate there must be full and adequate consideration paid for the interest which would be taxed. That interest is not the right to income for life but the right to the property which was placed in the trust and from which the income is produced.

Allen, 293 F.2d at 918 (Breitenstein, J. concurring). Similarly, to remove the shares from inclusion in the decedent's estate for elective share purposes, full and adequate consideration should be paid not only for the retained life interest but also for the shares that were the subject of the agreement.

178. Relinquishment of a retained interest or power in contemplation of death presents a

C. Retention of a Power

Another unanswered fundamental question concerning the scope of the elective share statutes under discussion is the meaning of the word "power" as used in the phrases "*power* to revoke" or "*power* to consume, invade or dispose."¹⁷⁹ Does the word "power" include a mandatory power, a discretionary power,¹⁸⁰ or does it cover both? *Estate of Twersky* addressed this question under the EPTL.¹⁸¹ There, decedent Twersky created an irrevocable trust, naming himself and two others as trustees. Pursuant to the trust instrument, Twersky was to receive each year of his life a \$50,000 annuity, payable quarterly from income and if the quarterly income was less than \$12,500, the trust instrument *required* the trustees to invade principal to make up the deficiency.¹⁸² The court was "convinced" that the word "power" implies "control or authority" and concluded that the non-discretionary quarterly payments of the fixed annuity was not a power to invade the principal within the scope of EPTL section 5-1.1(b)(1)(E).¹⁸³

Although the court's reasoning may be subject to question,¹⁸⁴ the

somewhat similar situation. Thus, in determining whether the relinquishment was made for full and adequate consideration, should the value received for the transfer of the underlying property be considered in addition to the value received for the relinquishment of the power or interest? It can be argued that unless full consideration is received for the property in which the decedent reserved that interest or power, the decedent could, after enjoying the benefits of the property almost until death, sell the reserved interest or power for a full consideration measured against only the short remaining term of that interest, or the period during which the power may be exercised, and thereby deprive the surviving spouse of an opportunity to share in that property. The underlying property might nevertheless be includible if the statute also covers transfers in contemplation of death. *See infra* note 300. *Cf. Allen*, 293 F.2d at 917-18 (holding that corpus of trust or amount equal in value should be includible in federal gross estate).

179. *See* UPC § 2-202(1)(ii); EPTL § 5-1.1(b)(1)(E); 20 PA. CONS. STAT. ANN. § 2203(a)(3).

180. A mandatory power refers to a purely ministerial duty, such as the obligation of a trustee to pay \$10,000 per year to a beneficiary. A discretionary power involves the exercise of some judgment, such as a trustee's power to invade principal as the trustee deems desirable.

181. N.Y.L.J., Sept. 16, 1982, at 10, col.7 (N.Y. Co. Surr. Ct. 1982), *aff'd mem.* No. 178-83 slip op. (N.Y. App. Div. 1983). In this litigation, the Twersky Estate was represented by Kaye, Scholer, Fierman, Hays & Handler, and Professor Kwestel, a former partner in the firm, handled the litigation in the Surrogate's Court. Professor Sepowitz participated in the appeal when she was associated with the firm.

182. At decedent's death, the principal was to be paid to a charitable foundation. *Estate of Twersky*, N.Y.L.J., Sept. 16, 1982, at 10, col.7 (N.Y. Co. Surr. Ct. 1982), *aff'd mem.* No. 178-83 slip op. (N.Y. App. Div. 1983).

183. *Id.*

184. After noting that neither the case law nor the legislative history was illuminating, the court stated that the REPORT defines the word "power" as "'the ability possessed by any person to extinguish legal relations in property, real or personal, and to create new relations therein [REPORT, *supra* note 5, at 129-30].'" *Id.* This definition, according to the court, seemed "to import a requirement that some authority or control be retained by the possessor of the power." *Id.* However, the definition appears in the REPORT under the heading "Powers of Appointment," a section which addresses elective share rights against property subject to a

conclusion in *Twersky* is sound.¹⁸⁵ Absent an unequivocal expression to the contrary, the word “power” in an elective share statute should not extend to a trust provision directing a trustee to invade principal under an objective standard that grants the trustee absolutely no room for discretion.¹⁸⁶ In such a case, no matter who is trustee, the decedent or anyone else, the trustee must exercise the power in the same manner. Accordingly, if the element of discretion or control is completely absent, it can scarcely be said that the settlor retains a “power,”¹⁸⁷ unless the statute makes it clear that the legislature intended to cover both discretionary and mandatory powers.

This approach is consistent with the estate tax law. Under IRC section 2038, if the exercise of the settlor-trustee’s power to “alter, amend, revoke, or terminate” the enjoyment of the property transferred is governed by an “external standard,” that is, a standard capable of enforcement by a court of equity, then the transferred property is not includible in the gross estate under IRC section 2038.¹⁸⁸ In such a case, enjoyment of the property is deemed to be

power of appointment. REPORT, *supra* note 5, at 129-30. It has nothing to do with EPTL § 5-1.1(b)(1)(E) and more importantly a person can have the requisite ability to extinguish or create relations without the kind of authority or control the court envisioned (for example, through the exercise of a mandatory nondiscretionary power).

Parenthetically, *Twersky* did not refer to EPTL § 10-2.1 (McKinney 1967), which defines the word “power” as “an authority to do any act in relation to property.” However, this definition implicitly seems to relate only to Article 10 which deals in part with powers of appointment, including imperative powers of appointment. See EPTL § 10-3.4(b) (McKinney 1967) (stating that power of appointment is imperative when donee has duty to exercise it).

185. If the power to invade principal for the benefit of the settlor were regarded as discretionary, the settlor, in his capacity as trustee, still should not be deemed to have retained a power because under New York law a trustee is prohibited from participating in the exercise of a discretionary power to distribute principal (or income) to himself as beneficiary. EPTL § 10-10.1 (McKinney 1967).

186. This presents a slightly different situation from a power to invade governed by an external standard under which the trustee still has some degree of discretion in the extent to which he exercises the power. See *infra* note 188 and accompanying text.

187. Analysis of the EPTL and its history confirms that the New York concept of a “testamentary substitute” is designed to encompass property transfers as to which the decedent retained a “string” during his lifetime to recapture or dispose of the property. The key under this statutory scheme and UPC § 2-202 is the decedent’s retention of control, a “string” over the property until his death. In essence, the property is disposed of upon the decedent’s death and not during life. Thus, each of the testamentary substitutes enumerated in EPTL § 5-1.1(b)(1)(A)-(D) involves transfers over which the decedent retained some control during his lifetime. Apart from gifts causa mortis and Totten trusts which are revocable, the statute covers tenancies by the entirety and joint tenancies. In such joint ownership, each joint tenant enjoys the power to sever the tenancy either alone or in conjunction with the other joint tenant. Although the decedent would have control over only one-half the property jointly held, the statute includes the value of the jointly held property to the extent of the decedent’s capital contribution. I.R.C. § 2040(a) (1986) also includes in the gross estate that portion of the property contributed by the decedent where property is held jointly with a nonspouse.

188. See, e.g., *Old Colony Trust Co. v. United States*, 423 F.2d 601, 603 (1st Cir. 1970); *Jennings v. Smith*, 161 F.2d 74 (2d Cir. 1947); *Estate of Budlong v. Commissioner*, 7 T.C. 756, 762 (1946), *aff’d in part and rev’d in part sub nom Industrial Trust Co. v. Commissioner*, 165

controlled by the external standard—which imposes on the decedent-trustee a *duty* to exercise the power—rather than the discretion of the decedent-trustee.

Pennsylvania's elective share statute, however, takes a different approach. First, the statute expressly applies to transfers where the retained power to withdraw principal or income is subject to an external standard, such as a power that may be exercised "only for support or other particular purpose or only in limited periodic amounts."¹⁸⁹ Second, a transfer with a retained power to revoke, consume, invade or dispose is includible only if the retained power is for the decedent's "own benefit."¹⁹⁰ The key to the Pennsylvania statute is the decedent's enjoyment or possibility of enjoyment of the transferred property and not merely the exercise of some degree of control over such property.¹⁹¹

The UPC also includes transferred property only if the retained

F.2d 142 (1st Cir. 1947). Although *Jennings* is cited repeatedly for this proposition, the decision is not clear. In this case, the settlor-trustee's power to invade was exercisable only if the decedent's son suffered prolonged illness or financial misfortune deemed extraordinary by the trustees, a standard considered "sufficiently definite to be capable of determination by a court of equity." *Id.* at 77. Neither contingency had occurred, however, prior to the decedent's death. The court concluded that the trustee's power to invade, "conditioned on contingencies which had not happened," was insufficient to make the transfer subject to section 811(d)(2) (predecessor of section 2038). *Id.* at 78. Similarly, in discussing the settlor-trustee's power to disburse income if he and his co-trustees determined it was necessary to enable the beneficiary to maintain himself in accordance with his "station in life," the court reasoned that since the contingency that would justify exercise of the power had not occurred, the trust was not subject to any change through the exercise of a power and thus was not includible under section 811(d). *Id.* Thus, insofar as section 2038 is concerned, the non-occurrence of the contingency appears to have been the determining factor, not the fact that the exercise of the power was subject to "determinable standards." Indeed, in *Estate of Yawkey v. Commissioner*, the court cited *Jennings* for the proposition that "a power based on such a future contingency [the beneficiary's reaching 30] does not suffice to bring the situation within section 811(d)." *Estate of Yawkey v. Commissioner*, 12 T.C. 1164, 1170 (1949), *acq.*, 1949-2 C.B. Nevertheless, the *Jennings* court emphasized the external standard concept in its discussion of whether the trustee's powers constituted a right under section 811(c) (predecessor of section 2036) to designate the persons who will enjoy the trust principal or income:

But for the reasons that moved us when considering the applicability of § 811(d) we think the decedent effectively put that "right" beyond his own control or retention by imposing conditions upon the exercise of it. A "right" so qualified that it becomes a duty enforceable in a court of equity on petition by the beneficiaries does not circumvent the obvious purpose of § 811(c) to prevent transfers akin to testamentary dispositions from escaping taxation.

Jennings, 161 F.2d at 78-79.

189. 20 PA. CONS. STAT. ANN. § 2203(a) and official comment (Purdon Supp. 1988). Since the statute appears to equate "beneficial powers" with "beneficial interests," it is likely that such a statute would be construed to reach mandatory invasions for the decedent's benefit. *See id.*

190. *Id.*

191. Thus, unlike the UPC and EPTL it is not surprising that the Pennsylvania statute, which focuses on decedent's benefit, provides that a power to withdraw "in any person whose interest is not adverse to the decedent" is deemed a power in the decedent. *Id.* This concept is found in the federal income tax laws concerning the taxability of trust income. *See* I.R.C. §§ 674(a), 675(1),(2),(4), 676(a), 677(a) (1986).

power is for the decedent's benefit.¹⁹² However, unlike the Pennsylvania statute, it does not expressly include property transferred with a retained power subject to an external standard. Nevertheless, the failure expressly to cover such transfers does not mean that they are not includible under UPC section 2-202. The UPC simply does not address the issue.¹⁹³

In this connection, the estate tax cases under IRC section 2038 provide no useful guidance. Significantly, these cases, which exclude from the scope of section 2038 transfers with a retained power to invade subject to an external standard, involve a power exercisable by the settlor in any capacity but only for the benefit of another person. Thus, the estate tax cases under section 2038 do not answer the question of whether a transfer with a retained power to invade subject to an external standard is includible under UPC section 2-202, which includes the transferred property only if the retained power is for the decedent's own benefit.

Given the rationale of the estate tax cases for excluding transfers subject to an external standard, the person for whose benefit the power is exercisable should be irrelevant. In focusing on the settlor as trustee, the external standard imposes a *duty* to invade which is enforceable in equity. In such a case, the settlor-trustee's *power* to invade is in reality only a *duty*. In focusing on a decedent who is also a beneficiary of the power to invade, one may argue that in his capacity as a beneficiary, the decedent retained a power to invade through the right to enforce the trustee's duty to exercise the power and, thus, the transfer should be includible under UPC section 2-202.¹⁹⁴ This argument, however, makes a distinction without a dif-

192. UPC § 2-202(1)(ii) (1983).

193. In our guidelines, we recommend that transfers subject to an external standard should be includible under elective share statutes. See *infra* notes 273-79 and accompanying text (discussing guidelines).

194. This argument is equally applicable to an elective share statute based on the federal estate tax statute, such as the Delaware elective share statute. See *supra* note 17. In fact, two commentators have asked whether a power, the exercise of which is subject to an external standard, would be covered by section 2038 if the decedent is the beneficiary on the ground that the decedent's "power to compel the third person to distribute income or corpus to him when the contingency occurs is a power to 'alter, amend or revoke.'" B. BITTKER & E. CLARK, *FEDERAL ESTATE AND GIFT TAXATION* 204 (5th ed. 1984).

Interestingly, under section 811(c) of the Internal Revenue Code of 1939, which taxed transfers intended to take effect in possession or enjoyment at or after the transferor's death, a transfer in trust by which the "trustees were under an enforceable fiduciary obligation, in the exercise of their discretion, to pay the principal of the trusts to the grantors according to fixed standards" was includible in the gross estate. *Estate of Rosenwasser v. Commissioner*, 5 T.C. 1043, 1046 (1945). See also *Blunt v. Kelly*, 131 F.2d 632, 633-35 (3d Cir. 1942) (including trust in gross estate under section 302(c) of Revenue Act of 1926, predecessor of section 811(c)); B. BITTKER & E. CLARK, *supra*, at 204 (reviewing cases including trust property in gross estate). Presumably, this argument is not applicable to EPTL § 5-1.1(b)(1)(E), because

ference. In the final analysis, the power to compel distributions—which could only exist to the extent that the trustee has failed to exercise the invasion power—is no more extensive than—and is governed by—the trustee’s correlative duty. In short, exercise of both powers is circumscribed by the same external standard. Thus, the power of a decedent as beneficiary to enforce the trustee’s duty is no more of a “power” than is the trustee’s duty itself and should be treated the same as any power that is subject to an external standard.¹⁹⁵

D. Gifts to Minors

Transfers under a state’s Uniform Gifts to Minors Act (UGMA)¹⁹⁶ or Uniform Transfers to Minors Act (UTMA)¹⁹⁷ present an interesting situation under all elective share statutes that cover lifetime transfers with certain reserved powers. Assume that Parent transfers funds into a bank account, naming Parent as custodian for Child, a minor, under the state’s UGMA. The gift is irrevocable and legal title is “indefeasibly vested” in Child.¹⁹⁸ However, Parent as custodian has the power to pay to Child or expend for Child’s benefit so much of the property as Parent “deems advisable for the support, maintenance, education and benefit of the minor.”¹⁹⁹ Under these circumstances, if Parent died before the custodianship terminated, would the custodial funds be included in Parent’s estate for

a power to enforce the duty of the trustee is not a power retained by the express provisions of the trust instrument.

195. Under our guidelines, such a power would render the property includible in the net estate. See *infra* notes 273-76 and accompanying text (reviewing arguments for including property in net estate).

196. UNIF. GIFTS TO MINORS ACT (1966 UGMA), 8A U.L.A. 328 (1966); UNIF. GIFTS TO MINORS ACT (1956 UGMA), 8A U.L.A. 412 (1956) (revised 1966). The 1956 UGMA is currently in effect in two states and the Virgin Islands (8A U.L.A. 90 (Supp. 1988)). The 1966 UGMA is currently in effect in twenty-one states. *Id.* at 75.

197. UNIF. TRANSFERS TO MINORS ACT (UTMA), 8A U.L.A. 176 (Supp. 1988). Twenty-seven states and the District of Columbia have adopted the UTMA which revised and restated the UTMA and which the National Conference of Commissioners on Uniform State Laws approved in 1983. 8A U.L.A. 75 (Supp. 1988).

198. See 1966 UGMA § 3(a), 8A U.L.A. 366 (1983); 1956 UGMA § 3(a), 8A U.L.A. 421 (1983); EPTL § 7-4.3(a) (McKinney Supp. 1988) (all three statutes contain this rule).

199. UGMA § 4(b), 8A U.L.A. 369 (1966), provides as follows:

The custodian shall pay over to the minor for expenditure by him, or expend for the minor’s benefit, so much of or all the custodial property as the custodian deems advisable for the support, maintenance, education and benefit of the minor in the manner, at the time or times, and to the extent that the custodian in his discretion deems suitable and proper, with or without court order, with or without regard to the duty of himself or of any other person to support the minor or his ability to do so, and with or without regard to any other income or property of the minor which may be applicable or available for any such purpose.

Any unexpended funds must be paid to the minor no later than the age of 21 or if the minor dies prior to such age, to his estate. UGMA § 4(d), 8A U.L.A. 369 (1966).

elective share purposes? More specifically, under UPC section 2-202(1) and the Pennsylvania elective share statute, would such a gift constitute a transfer in which Parent retained, to any extent, a power exercisable “for his own benefit”?²⁰⁰ And under EPTL section 5-1.1(b)(1)(E) can it be said that Parent’s powers as custodian were retained by the express provisions of the disposing instrument? Finally, is exercise of Parent’s power as custodian subject to an external standard? Based on existing authority, it is difficult to give definitive answers.

1. *Retained power for parent’s benefit*

In *Estate of Schwartz*,²⁰¹ the Pennsylvania Supreme Court held that a corporate bond, which decedent purchased for his son (by a prior marriage) under Pennsylvania’s UGMA,²⁰² was not subject to his surviving spouse’s right of election under section 11, which reached transfers with a retained testamentary power of appointment or a power to revoke or consume. The court noted that under Pennsylvania’s UGMA the gift was irrevocable and indefeasibly vested title in the minor. Consequently, the court concluded that the custodian “cannot consume the principal for his own benefit.”²⁰³ It rejected the surviving spouse’s argument that a limited power of consumption was retained because application of the custodial property might have relieved the decedent of his parental support obligation. The court explained:

[T]his argument presupposes the existence of a support obligation on the part of the custodian that can be met by payments from the custodial fund and falls apart whenever a custodian owes no duty of support to the minor. Additionally, we believe the advantage to the present decedent, if there was any advantage, was too indirect and remote and cannot be classified as a power of consumption under Section 11. It appears to be impossible for the custodian to have used his statutory authority to his own advantage; his power of consumption could *only* be exercised to benefit the minor and the existence of such power of consumption has

200. Both statutes require that the power be exercisable for the decedent’s benefit. UPC § 2-202(1)(ii) (1983); 20 PA. CONS. STAT. ANN. § 2203(a)(3) (Purdon Supp. 1988).

201. 449 Pa. 112, 295 A.2d 600 (1972) (plurality opinion).

202. 20 PA. CONS. STAT. ANN. §§ 5301-10 (Purdon Supp. 1988).

203. *Estate of Schwartz*, 449 Pa. 112, 116, 295 A.2d 600, 603 (1972) (plurality opinion). The court interpreted the words “power of consumption” in section 11 (quoted *supra* in note 37) to mean a power to consume in favor of the decedent. It based its interpretation on the fact that prior decisions under section 11 “involved situations where the interest retained by the decedent could be exercised to his own advantage.” *Id.* (footnote omitted). See also *Longacre v. Hornblower & Weeks*, 83 Pa. D. & C. 259, 262 (1952), where the court concluded that in using the phrase “power of consumption” the legislature intended to cover transfers that were subject to the transferor’s power “to reacquire beneficially the property conveyed.”

not been demonstrated on this record to have relieved, actually or potentially, the donor-decedent of his support obligation.²⁰⁴

This explanation is difficult to understand in light of the court's basic premises. The court had already acknowledged that the donee's father had a pre-existing duty of support,²⁰⁵ and assumed for purposes of the decision that "the donor-custodian could in fact substitute custodial funds for his legal obligation to support."²⁰⁶ Therefore, why did the court say that the surviving spouse did not demonstrate that the donor-decedent was relieved either "actually or *potentially*"²⁰⁷ of his support obligation?²⁰⁸ If, as the court explicitly assumed for purposes of the decision, the decedent-parent had retained a power to substitute custodial funds for his legal obligation to support his child, what additional showing could have been made? It seems that under these circumstances the decedent was at least "potentially" relieved of his support obligation, and thus benefited by virtue of the power the court assumed he had as a UGMA custodian.²⁰⁹ Indeed, the dissent took the position that once a parent designates himself as custodian "he *could* utilize the custodial proceeds, *instead* of his personal assets, to satisfy *his* parental obligation to support his minor son."²¹⁰ Accordingly, the dissent ob-

204. Estate of Schwartz, 449 Pa. 112, 117, 295 A.2d 600, 603-04 (1972) (plurality opinion) (emphasis in original).

205. *Id.* at 114, 295 A.2d at 602.

206. *Id.* at 115 n.2, 295 A.2d at 603 n.2. Although the court made this assumption, it explained in note 2 that the conclusion does not necessarily follow from the UGMA. *Id.* See *infra* note 210.

207. *Schwartz*, 449 Pa. at 117, 295 A.2d at 604 (emphasis added).

208. The most plausible explanation is that the court ignored—and reached a conclusion that is irreconcilable with—the premises it had assumed for purposes of the decision. *But see* Sutliff v. Sutliff, 515 Pa. 393, 404, 528 A.2d 1318, 1323 (1987) ("We have stated that a custodian may not use UGMA property to benefit himself [citing *Schwartz*] and suggested that a custodian may not use it to fulfill an existing support obligation.").

209. The Pennsylvania Superior Court explained that the majority in *Schwartz* believed that even if it were permissible for a parent as custodian to use custodial funds to satisfy his legal obligation to support his minor child such a right would not constitute a power of consumption. *Sutliff v. Sutliff*, 339 Pa. Super. 523, 535-36, 489 A.2d 764, 770 (1985), *aff'd in part and remanded in part*, 515 Pa. 393, 528 A.2d 1318 (1987). This is probably a correct interpretation. Unfortunately, the plurality opinion in *Schwartz* did not make this clear but rather provided a confusing and questionable explanation for its decision. But even if *Sutliff* correctly states the conclusion of the *Schwartz* plurality, the underpinnings for that conclusion remain obscure. Logically the retention of a power to use income or principal to discharge a legal obligation seems to be the equivalent of retaining to some extent a power to consume for the decedent's benefit. Perhaps the *Schwartz* plurality recognized this possibility and accordingly added the comment that such an "advantage [i.e. relief of support obligation] was too indirect and remote and cannot be classified as a power of consumption under Section 11." Estate of Schwartz, 449 Pa. 112, 117, 295 A.2d 600, 603 (1972) (plurality opinion).

210. *Schwartz*, 449 Pa. at 122-23, 295 A.2d at 606 (Roberts, J. dissenting) (emphasis in original). The plurality opinion assumed for purposes of the decision that the custodian had a right to use custodial funds to satisfy his legal obligation of support. See *supra* note 206 and accompanying text (outlining court's assumptions). However, the author of the plurality opinion thought that it was "less than clear" that UGMA § 5(b) conferred such a right.

served, the decedent-parent retained “the exclusive right to decide whether to satisfy his support obligation from his personal assets *or* from the custodial assets”—a right that, according to the dissent, constituted a power of consumption under section 11.²¹¹

Tax cases under section 2036(a) of the Internal Revenue Code support the dissent in *Schwartz*. In *Estate of Chrysler v. Commissioner*,²¹² the decedent made a gift to his daughter under New York’s Model Gifts of Securities to Minors Act.²¹³ Because the Tax Court construed the Act as giving the decedent the right, as custodian, to apply so much of the income as he deemed advisable for the support, maintenance, education, and benefit of the minor, the court concluded that “he had made a transfer under which he had in effect retained the right to use the income from the property to discharge his legal obligation to support [his daughter].”²¹⁴ This right, the court held,²¹⁵ required that the custodial property be included in the gross estate under section 2036(a).²¹⁶ Thus, the reason for the Tax Court’s holding, to quote from a subsequent Tax Court case, “was that the decedent had a legal obligation to support his daughter and as custodian he retained the right to use the income from the custodial property to discharge his legal obligation to support

Schwartz, 449 Pa. at 115 n.2, 295 A.2d at 603 n.2. The concurring opinion stated that the parent as custodian only had the right to “claim” that the use of the custodial funds extinguished his obligation to support his son. *Id.* at 119, 295 A.2d at 608 (Manderino, J., concurring). But, in fact, such use could not satisfy the parent’s obligation of support. *Id.* at 119-20, 295 A.2d at 608 (Manderino, J., concurring).

211. *Schwartz*, 449 Pa. at 123, 295 A.2d at 606 (Roberts, J., dissenting) (emphasis in original).

212. 44 T.C. 55 (1965), *rev’d on other grounds*, 361 F.2d 508 (2d Cir. 1966).

213. *Estate of Chrysler v. Commissioner*, 44 T.C. 55, 56-60 (1965), *rev’d on other grounds*, 361 F.2d 508 (2d Cir. 1966). The Model Gifts of Securities to Minors Act was originally enacted in 1956 as an amendment to the Personal Property Law. N.Y. PERS. PROP. LAW § 265-71 (McKinney 1976). In 1959, this act was replaced by the UGMA which in turn was replaced by the revised UGMA in 1967 and was subsequently amended. EPTL §§ 7-4.1 to 7-4.13 (McKinney Supp. 1988).

214. *Estate of Chrysler*, 44 T.C. at 68.

215. Alternatively, the court held that the transfer was includible under section 2038(a)(1). *Id.*

216. *Id.* The relevant part of section 2036 provides:

Transfers with Retained Life Estate.

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

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

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

I.R.C. § 2036(a) (1986).

her."²¹⁷

In contrast to the federal estate tax decisions, state cases that construed the UGMA in the context of court ordered support generally concluded that the UGMA does not permit a parent as custodian to use custodial funds to satisfy any legal obligation to a minor child.²¹⁸ The effect of these cases is somewhat unclear. Absent explicit language as contained in *Sutliff v. Sutliff*,²¹⁹ they should not be construed as prohibiting a parent as custodian who is not subject to a court order from exercising the power to use custodial funds for the support of a minor child, because UGMA section 4(b) expressly authorizes such a use.²²⁰ Although the parent as custodian may have the power under UGMA section 4(b) to use custodial funds for

217. *Stuit v. Commissioner*, 54 T.C. 580, 581 (1970) (reviewing *Estate of Chrysler*), *aff'd*, 452 F.2d 190 (7th Cir. 1971)). *Accord* *Estate of Prudowsky v. Commissioner*, 55 T.C. 890, 894-95 (1971) (holding gift includible in decedent's estate under Wisconsin UGMA), *aff'd*, 465 F.2d 62 (7th Cir. 1972); *Crocker Citizens Nat'l Bank v. United States*, 75-2 U.S.T.C. ¶ 13,106 (N.D. Cal. 1975) (holding gifts of stock to daughters includible in decedent's estate). *See also* *Korschun v. Clayton*, 13 N.C. App. 273, 277, 185 S.E.2d 417, 419-20 (N.C. Ct. App. 1971) (in holding custodial funds taxable under inheritance tax statute comparable to section 2036(a), the court said: "[t]he Uniform Act permits him [the parent-custodian] in his discretion to use the principal and income of the custodial gift for that purpose [his duty of support] and thereby retain the full possession and enjoyment of his own estate without diminution by expenditures of funds for the support of his child, the donee"); *cf.* *Commissioner v. Dwight's Estate*, 205 F.2d 298, 301 (2d Cir.) (holding that because settlor-husband had power to use 40% of the trust income for his wife's support and maintenance, which "had in part at least discharged his legal obligation of supporting her," 40% of trust corpus was includible in husband's gross estate under I.R.C. § 811(c)(1)(b), predecessor of I.R.C. § 2036(a)(1) (1986)), *cert. denied*, 346 U.S. 871 (1953); *Helvering v. Mercantile-Commerce Bank & Trust Co.*, 111 F.2d 224, 226-27 (8th Cir. 1940) (including trust used to discharge obligation of support for wife in settlor-husband's gross estate); *Estate of Gokey v. Commissioner*, 72 T.C. 721, 728 (1979) (finding support trust for children includible in parent-settlor's estate under section 2036).

218. *See Sutliff v. Sutliff*, 515 Pa. 393, 528 A.2d 1318, 1320 (1987) (footnote omitted). In an action to remove and surcharge custodian-parent for using custodial funds to make court ordered support payments for his minor children, the court held that "on the merits, . . . a parent's obligation to support minor children is independent of the minor's assets. UGMA funds may not be used to fulfill the parent's support obligation where the parent has sufficient means to discharge it himself." *Id.* *See In re Marriage of Wolfert*, 42 Colo. App. 433, 435-36, 598 P.2d 524, 526 (Colo. Ct. App. 1979) (indicating that Colorado UGMA does not relieve parent of obligation to support child); *Gold v. Gold*, 96 Misc. 2d 481, 483, 409 N.Y.S.2d 114, 116 (N.Y. Co. Sup. Ct. 1978) (barring custodian from using children's money for their support, because by reducing her child care obligations, she received indirect financial advantage); *Erdmann v. Erdmann*, 67 Wis. 2d 116, 124, 226 N.W.2d 439, 443 (1975) (holding that parent-custodian could not use court-created fund established under divorce decree for support and maintenance of children). *Cf.* *Tharp v. Blackwell*, 570 S.W.2d 154, 159 (Tex. Civ. App. 1978). The court stated that "[t]he law of this state imposes upon a parent who has resources of his own sufficient to maintain his children, and who is also guardian of their estates, to support them out of his own means and he may not have recourse to the estates of the wards." *Id.*

219. *See supra* note 218; *infra* note 222. *Sutliff*, however, does not explain how its decision squares with the express language of UGMA § 4(b).

220. Section 4(b) authorizes the custodian to pay or expend funds to or for the minor's support "with or without regard to the duty of himself or of any other person to support the minor." *See supra* note 199 (quoting UGMA).

such support, it can plausibly be argued that such use does not discharge the parent's primary duty of support of the child to whom title to the custodial funds is indefeasibly vested²²¹ and that the minor should be permitted to enforce this obligation and recover the expended custodial funds.²²² Under these circumstances, the custodial funds might not be includible in the custodian-parent's estate for elective share purposes under the UPC or the current Pennsylvania statute.²²³

It is even less likely that under the UTMA a court would hold that a custodian-parent retained a power that could be exercised for the parent's benefit. Section 14(a) of the UTMA, like UGMA section 4(a), empowers the custodian to expend for the minor's benefit so much of the custodial property as the custodian deems advisable for the minor's use and benefit, without regard to any person's obligation to support the minor.²²⁴ Moreover, UTMA section 14(c) expressly provides that such an expenditure is "in addition to, not in substitution for, and does not affect any obligation of a person to

221. UGMA § 3(a). The prefatory note to the 1966 UGMA seems to disagree with including custodial funds in the gross estate under section 2038 and, accordingly, lends support to the view that the parent's primary duty of support would not be discharged by the use of custodial funds. Thus, in critically commenting on Revenue Ruling 57-366, which would include the value of custodial property in the gross estate of the donor because the donor was named custodian, the note states that "the Internal Revenue Service refused to recognize that the clear intent of these statutes was to indefeasibly vest title in the minor." 8A U.L.A. 320 (1983).

222. *Cf. Sutliff v. Sutliff*, 515 Pa. 393, 407, 528 A.2d 1318, 1324-25 (1987). "If a parent did refuse to fulfill his support obligation, a custodian acting in good faith could make interim expenditures for the children's necessary support. Thereafter, he could seek to recover any distributions he made on behalf of the children from the responsible parent . . ." *Id.* *Cf. Erdmann v. Erdmann*, 67 Wis. 2d 116, 226 N.W.2d 439 (1975). Indeed, custodial accounts in states taking the approach discussed in the text should not be subject to I.R.C. § 2036(a)(1) (1986) if the parent creating the account is the custodian. *But see Weisbaum v. Weisbaum*, 2 Conn. App. 270, 273-74, 477 A.2d 690, 693 (Conn. App. Ct. 1984) (stating that purpose of general statute § 45-104(b) [UGMA § 4(b)] is to protect custodian from claims by minor of unauthorized disbursements); *In re Levy*, 97 Misc. 2d 582, 590-91, 412 N.Y.S.2d 285, 291 (Nassau Co. Surr. Ct. 1978) (liability under UGMA could not be based upon good faith mismanagement by mother of custodial accounts).

223. Even assuming that legally the parent as custodian may not benefit from an exercise of this power, as a practical matter, the power will be exercisable for the custodian-parent's benefit because it is unlikely that a child will enforce the parent's primary duty through litigation or otherwise. Perhaps this is sufficient to justify inclusion of the value of the custodial funds in the estate for elective share purposes. Cases arising in the divorce and child support context illustrate, however, that the child's other parent or guardian may seek to enforce the custodian-parent's duties on behalf of the child.

224. UTMA § 14(a) provides, in pertinent part:

A custodian may deliver or pay to the minor or expend for the minor's benefit so much of the custodial property as the custodian considers advisable for the use and benefit of the minor, without court order and without regard to (i) the duty or ability of the custodian personally or of any other person to support the minor, or (ii) any other income or property of the minor which may be applicable or available for that purpose.

8A U.L.A. 197 (Supp. 1988).

support the minor.”²²⁵ On first impression it seems that under the express language of UTMA section 14(c) an enforceable debtor-creditor relationship arises each time a parent as custodian expends custodial funds for the support of the minor if the parent has a legal obligation of support. If the minor has such a claim, then for purposes of an elective share statute, the parent as custodian does not retain any power that is exercisable for the parent’s own benefit.²²⁶

Based on the comment to UTMA section 14(c), however, this approach is subject to question. The drafters apparently included section 14(c) to prevent the attribution of income to the parent for income tax purposes.²²⁷ Although the drafters recognized that this could have been accomplished by expressly providing that the use of custodial income for the minor’s support gave the minor a cause of action “against his parent to the extent that custodial property or income is . . . used” to satisfy the parent’s legal obligation of support, they rejected this approach as “too cumbersome.”²²⁸ Nevertheless, the fact that the drafters did not expressly provide that the minor has a cause of action against the parent as custodian who uses custodial funds, whether income or principal, to support the minor should not be decisive. Regardless of the drafter’s intent, the effect of the express language of section 14(c) seems clear—such use “does not affect any obligation of a person to support the minor.”²²⁹ Under these circumstances, the minor should be entitled to enforce this obligation and be reimbursed for the amount of custodial funds expended, and the parent should not be deemed to

225. *Id.* at 198. The UGMA does not contain a comparable provision.

226. In addition, the value of the fund should not be includible in the gross estate under section 2036(a)(1). *See supra* note 216 (quoting section 2036).

227. UTMA § 14, 8A U.L.A. 198 comment (Supp. 1988). Income from custodial property used for the minor’s support is taxable to any person who is legally obligated to support the minor. Rev. Rul. 59-357, 1959-2 C.B. 212; Rev. Rul. 56-484, 1956-2 C.B. 23; 5 B. BITTKER, *supra* note 62, at 75-50. This is true even if the parent is not the custodian.

The comment’s explanation for the addition of subsection (c) is somewhat confusing. The second paragraph of the comment indicates the Internal Revenue Service’s position that the amount of custodial income used to support a minor is includible in the gross income of the individual legally obligated to support the minor. In the very same paragraph, based on Treasury Regulation § 1.662(a)-4 concerning the term “legal obligation,” the comment explains that a parent is not legally obligated if the child’s own resources are adequate and, if under state law, a parent can use the child’s resources to support the child instead of the parent’s own funds. The first sentence of the next paragraph causes the confusion because it states that “[f]or this reason, new subsection (c) has been added” If the phrase “[f]or this reason” refers to the preceding paragraph, as it appears to do, it would indicate that section 14(c) was added in order to preclude a legal obligation from arising by permitting the parent to use custodial income for the child’s support instead of the parent’s own funds. But neither the remaining language of the first sentence nor the language of section 14(c) bears this out as the reason for adding this section. In fact, it is difficult to discern from the comment the reason why section 14(c) was added.

228. UTMA § 14, 8A U.L.A. 198 comment (Supp. 1988).

229. *Id.*

have retained any power over the account for the parent's own benefit.²³⁰ In this event, the value of the funds would not be included in the parent's estate for elective share purposes under the UPC or the Pennsylvania statute.²³¹

2. *Retained power for minor's benefit*

Let us now examine the consequences of a gift to a minor under New York's elective share statute, where the donor is the custodian.²³² The custodian's power under UGMA section 4(b) (EPTL section 7-4.4(b)) to distribute custodial property to the minor or for the minor's benefit would constitute a power to invade or dispose under EPTL section 5-1.1(b)(1)(E) which does not require that the power be exercisable for the decedent's benefit. Can it be said, however, that the decedent retained such a power by the express terms of the disposing instrument, that is, by the express terms of the gift? The power should be so retained because UGMA section 3(b) provides that the donor "incorporates in his gift all the provisions" of the UGMA and grants the custodian all the powers provided in the UGMA, which include the custodian's power to make distributions.²³³ Thus, a gift to a minor under any state's UGMA falls within the scope of EPTL section 5-1.1(b)(1)(E) if the custodian died before the custodianship terminated.

The only directly pertinent New York decision has held that UGMA custodial accounts under New York's UGMA are not testamentary substitutes under EPTL section 5-1.1(b)(1).²³⁴ The court

230. Based on this position, a custodial account established under the UTMA should not be includible in the gross estate for federal estate tax purposes under section 2036.

231. UPC § 2-202(1)(ii); 20 PA. CONS. STAT. ANN. § 2203(a)(3) (Purdon Supp. 1988).

232. With respect to the Delaware elective share statute, which adopts the federal estate tax approach (*see supra* note 17), and based on the existing federal estate tax cases, the custodial funds would be includible regardless of whether the donor as custodian was also the parent. This is because the courts have held that if a donor retains the power as custodian over UGMA property, the custodial property is includible in the donor's gross estate under section 2038(a)(1). *See Stuit v. Commissioner*, 452 F.2d 190 (7th Cir. 1971). The court held that decedent's gifts to her minor grandchildren, naming herself as custodian under Illinois' UGMA, were includible under section 2038 because her powers as custodian under UGMA § 4(b) to pay over to the minor so much or all of the custodial property as she deemed advisable in her sole discretion constituted a power to terminate. *Id.* *See also Eichstedt v. United States*, 354 F. Supp. 484, 487-88 (N.D. Cal. 1972) (stating transfers to daughters under California UGMA and its predecessor were includible under section 2038); *Estate of Jacoby v. Commissioner*, 29 T.C.M. (CCH) 737, 738-39 (1970) (ruling decedent's gift to grandchild under Missouri UGMA was includible).

233. EPTL § 7-4.3(b) (McKinney Supp. 1988). This section reads, in pertinent part, as follows:

By making a gift in a manner prescribed by this part, the donor incorporates in his gift all the provisions of this part and grants to the custodian . . . the respective powers, rights and immunities provided in this part.

Id.

234. *In re Estate of Zeigher*, 95 Misc. 2d 230, 232, 406 N.Y.S.2d 977, 978 (Nassau Co.

reasoned that because the only gifts included under EPTL section 5-1.1(b)—specifically subdivision 1(A)—are gifts *causa mortis* “it can be inferred that all *inter vivos* gifts are excluded.”²³⁵ In so doing, the court overlooked EPTL section 5-1.1(b)(1)(E) which covers any disposition “in trust or *otherwise*” if the decedent retains a power to invade or dispose. This is precisely what occurs if an *inter vivos* gift is made under the UGMA; there is a disposition by which the donor as custodian retains the equivalent of a power to invade or dispose.²³⁶ It is true, as the court stated, that with an *inter vivos* gift under the UGMA the “full ownership vests in the donee.”²³⁷ However, the key to EPTL section 5-1.1(b)(1)(E), as with estate tax section 2038(a), is neither ownership nor benefit to the decedent, but rather the decedent’s retention of a certain degree of control over the gift which the donor as custodian possesses.²³⁸ Accordingly, if the decedent’s power as custodian is properly regarded as being retained by the express provisions of the disposing instrument, a question discussed above, and if its exercise is not subject to an external standard, a question discussed below, then the custodial property should be includible for elective share purposes under EPTL section 5-1.1(b)(1)(E).

Finally, is the custodian’s power to invade or dispose subject to an external standard? In *Stuit v. Commissioner*,²³⁹ the decedent made a gift of stock to her minor grandchildren, naming herself as custodian under Illinois’ UGMA.²⁴⁰ The Tax Court held that the retained power to distribute the custodial property to the minor was a power

Surr. Ct. 1978). The court also mistakenly relied on *Estate of Schwartz*, 449 Pa. 112, 295 A.2d 600 (1972) (plurality opinion). A plurality of Pennsylvania’s Supreme Court construed section 11 of the Pennsylvania statute as applying only to a transfer with a retained power to consume exercisable in decedent’s favor. See *supra* notes 201-11 and accompanying text (discussing *Schwartz*). EPTL § 5-1.1(b)(1)(E) applies to a retained power to dispose or invade regardless of whether it is exercisable in favor of the decedent or a third person. No authority indicates that it was intended to be limited to powers exercisable only for the decedent’s benefit. For analogous federal tax cases, see *Commissioner v. Estate of Holmes*, 326 U.S. 480, 489 (1946) (stating that “[d]ecedent’s failure to reserve for himself any beneficial interest or power to recapture one is not controlling [under § 811(d), predecessor of § 2038]”); *Estate of Porter v. Commissioner*, 288 U.S. 436, 443 (1933) (holding trust corpus includible in gross estate where decedent retained right to amend or terminate trust for benefit of others but not for himself or his estate); *Florida Nat’l Bank v. United States*, 336 F.2d 598, 601 (3d Cir. 1964) (stating that under section 2038 power need not be exercisable for decedent’s benefit), *cert. denied*, 380 U.S. 911 (1965).

235. *In re Estate of Zeigher*, 95 Misc. 2d 230, 231, 406 N.Y.S.2d 977, 978 (Nassau Co. Surr. Ct. 1978).

236. UGMA § 4(f), 8 A U.L.A. 369-70 (1966).

237. *Zeigher*, 95 Misc. 2d at 231, 406 N.Y.S.2d at 978.

238. *Id.*, 406 N.Y.S.2d at 978.

239. 54 T.C. 580 (1970), *aff’d*, 452 F.2d 190 (7th Cir. 1971).

240. ILL. ANN. STAT. ch. 110 1/2, para. 201-11 (Smith-Hurd 1978) (repealed by L. 1985, P.A. 84-915 and replaced by ILL. ANN. STAT. ch. 110 1/2, para. 251-74 (Illinois’ UTMA, effective July 1, 1986)).

to terminate within the meaning of section 2038(a)(1),²⁴¹ and, accordingly, that the value of the custodial property was includible in the decedent's gross estate.²⁴² In so holding, the Tax Court, therefore, concluded that the word "benefit" does not constitute an external standard as do the words "support, maintenance [and] education."²⁴³ The court reached this result first by comparing UGMA section 4(b) with section 4(c) which empowers the court to direct the custodian to expend funds for "the minor's support, maintenance or education."²⁴⁴ Because the word "benefit" is omitted from section 4(c),²⁴⁵ the Tax Court reasoned that it must have "a meaning separate from the words 'support, maintenance, [and] education.'" ²⁴⁶ The court then stated that, as an independent word, "benefit" is synonymous with "happiness"—a word that has been found "not to create an external standard."²⁴⁷ Although the *Stuit* court's conclusion that the word "happiness" is not an external standard may be questioned,²⁴⁸ and an argument may be made that the word "benefit" is synonymous with "welfare,"²⁴⁹ and thus creates an external standard,²⁵⁰ the likelihood is that the *Stuit* view would prevail.

241. *Stuit v. Commissioner*, 54 T.C. 580, 582 (1970), *aff'd*, 452 F.2d 190 (7th Cir. 1971).

242. *Accord* *Estate of Prudowsky v. Commissioner*, 55 T.C. 890, 892-94 (1971), *aff'd*, 465 F.2d 62 (7th Cir. 1972); *Estate of Jacoby v. Commissioner*, 29 T.C.M. (CCH) 737 (1970). *Cf.* *Lober v. United States*, 346 U.S. 335 (1953). The Supreme Court held that because the decedent irrevocably transferred property to himself as trustee for the benefit of his minor children, reserving to himself a power at any time to turn over any part of the principal to his children, the value of the trust was includible under section 811(d)(2) (predecessor of section 2038) for estate tax purposes. *Id.*

243. *Stuit*, 54 T.C. at 583. *Accord* *Estate of Jacoby*, 29 T.C.M. (CCH) at 738. On the basis of *Stuit*, the court rejected the application of the doctrine of *ejusdem generis* to the words "support, maintenance, education and benefit" under section 404.040 of Missouri UGMA (Mo. ANN. STAT. § 404.040) (Vernon 1978) (repealed in 1985 and replaced by UTMA, Mo. ANN. STAT. § 404.016 (Vernon Supp. 1988)). *Id.* The court concluded that the word "benefit" does not provide "an independent ascertainable standard." *Id.* *Cf.* *Estate of Bell v. Commissioner*, 66 T.C. 729, 736 (1976) (holding that "benefit standing alone does not establish an objective standard" under trust permitting distributions for beneficiary's benefit).

244. *Stuit*, 54 T.C. at 583. UGMA § 4(c) (1966) provides as follows:

The court, on the petition of a parent or guardian of the minor or of the minor, if he has attained the age of fourteen years, may order the custodian to pay over to the minor for expenditure by him or to expend so much of or all the custodial property as is necessary for the minor's support, maintenance or education.

8A U.L.A. 369 (1983).

245. The purpose of section 4(c), according to the Tax Court in *Stuit*, "is to assure the minor a minimum standard of living." *Stuit*, 54 T.C. at 583.

246. *Id.*

247. *Id.* (citations omitted).

248. *See* *United States v. Powell*, 307 F.2d 821, 828 (10th Cir. 1962) (stating that where decedent retained power to invade principal for "maintenance, welfare, comfort or happiness" of beneficiaries, trust corpus not includible in gross estate because "happiness" is "synonymous with 'welfare' and 'comfort,'" which constitute an external standard).

249. RANDOM HOUSE COLLEGE DICTIONARY 1493 (rev. ed. 1982).

250. *See supra* note 248. *Cf.* *Brantingham v. United States*, 631 F.2d 542, 547 (7th Cir. 1980) (holding that power given to wife to invade corpus "as in her judgment is necessary for

In contrast to UGMA sections 4(b) and (c), the UTMA has a single standard governing the power of the custodian and the court over the custodial property.²⁵¹ The change from UGMA sections 4(b) and (c) was, according to the comment, "intended to avoid the implication that the custodial property can be used only for the *required* support of the minor."²⁵² It is improbable, however, that the drafters intended that the words "use and benefit" would have no limitations or restraint. Here too, it seems that the words "for the use and benefit" might be construed to be the equivalent of the words "for the minor's welfare," which some might argue creates an external standard.²⁵³

Of course, each state must interpret its Uniform Act to determine whether the word "benefit" under the UGMA or the words "use and benefit" under the UTMA constitute an objective standard.²⁵⁴ Even if they do, however, because the decedent's exercise of a reserved power may benefit the decedent,²⁵⁵ the fact that it is governed by an external standard should not alone justify excluding the transfer for elective share purposes.²⁵⁶

Regardless of the precise answers to the questions discussed, a legislature should make a policy decision as to whether the value of gifts to minors under the Uniform Acts should be excluded from the net estate for elective share purposes. If a parent donor chooses to retain the power, as custodian, to use the custodial funds to support his child instead of his own funds, then it seems reasonable, on this basis alone, to treat such a transfer the same as a transfer in trust. Including custodial property for elective share purposes to the same extent as a lifetime transfer in trust would not be a harsh result, because the decedent can easily avoid the inclusion of any of the

her maintenance, comfort and happiness" constituted ascertainable standard under I.R.C. § 2041(b)(1)(A)).

251. See *supra* note 224 (quoting UTMA § 14(a)). UTMA § 14(b) provides as follows:

On petition of an interested person or the minor if the minor has attained the age of 14 years, the court may order the custodian to deliver or pay to the minor or expend for the minor's benefit so much of the custodial property as the court considers advisable for the use and benefit of the minor.

8A U.L.A. 197 (Supp. 1988).

252. UTMA § 14, 8A U.L.A. 198 comment (emphasis added).

253. See *supra* notes 248-50 and accompanying text.

254. See *In re Muller*, 38 Misc. 2d 91, 94, 235 N.Y.S.2d 125, 128-29 (N.Y. Sup. Ct. 1962) (construing "benefit" in N.Y. Personal Property Law § 266(2) (predecessor of EPTL § 7-4.4(b) (McKinney Supp. 1988) in a narrow sense), *aff'd*, 18 A.D.2d 1067, 239 N.Y.S.2d 519 (N.Y. App. Div. 1963). Without explanation, the court did not view use of funds for children "for travel expense to Europe and for school purposes" as falling within purview of word "benefit". *Id.*, 235 N.Y.S.2d at 128-29.

255. See *supra* text accompanying note 194.

256. See *infra* notes 273-76 and accompanying text (arguing existence of external standard is immaterial).

custodial funds by naming any trustworthy third person as custodian.²⁵⁷

VII. RECOMMENDATIONS FOR CLOSING LOOPHOLES

To ensure that the surviving spouse will receive the full protection that elective share statutes are designed to provide and to recognize the spouse's contributions to marriage, we recommend that the elective share statutes discussed in this article be amended. More specifically, we suggest that the testamentary substitute provisions be changed in conformance with the following guidelines.

A. *Life Estates*

Currently, EPTL section 5-1.1(b)(1) does not confer a right of election against a transfer in which the decedent has retained only a life estate,²⁵⁸ a significant economic benefit—but no power over the principal. For example, if A transfers \$500,000 in trust to T to pay the income to A for life with remainder to B, the transferred property is not includible in A's net estate under EPTL section 5-1.1(b)(1). In contrast, if A deposits the same \$500,000 in an interest bearing account or invests it and retains ownership until death, it will be includible in A's estate for elective share purposes.

The omission of transfers with a retained life interest can frustrate the purpose of the statute, because by making such transfers a decedent may thereby enjoy significant economic benefits until death and simultaneously prevent the surviving spouse from sharing in any part of the transferred property. In addition to the fact that a retained life interest may give the decedent the same lifetime enjoyment as outright ownership, as the example above illustrates—the decedent has determined (by the quasi-testamentary gift of the remainder) who shall own the property after his death.²⁵⁹ This interest may well be more significant to the decedent than a retained power in conjunction with another or even a retained power to dispose of the principal to third parties.²⁶⁰ Therefore, a transfer with a retained life interest should be treated no differently for elective

257. In this case, however, the surviving spouse may be deemed to possess a general power of appointment for federal estate tax purposes. See I.R.C. § 2041(a)(2) (1986); Treas. Reg. § 20.2041-1(c)(1) (as amended in 1961); Pennell, *Custodians, Incompetents, Trustees and Others: Taxable Powers of Appointment?*, 15 U. MIAMI INST. ON EST. PLAN. ¶¶ 1600, 1602 (1981).

258. EPTL § 5-1.1(b)(1) (McKinney 1981).

259. Cf. 5 B. BITTKER, *supra* note 62, ¶ 126.6 at 126-74 to 126-75 (explaining rationale for I.R.C. § 2036(a)(1) (1986)).

260. A retained power to invade principal for the benefit of third parties is relevant only to the EPTL and not to the UPC or the Pennsylvania statute. See *supra* notes 190-92 and accompanying text.

share purposes from property owned or controlled in certain respects by the decedent at the time of death. Consequently, the New York statute should be amended to include this type of transfer as well as any transfer under which the decedent retains the possession or enjoyment of, or the right to the income from, the property for any period not ascertainable without reference to the decedent's death, or for any period that does not end before his death.²⁶¹

The UPC and the Pennsylvania statute already include dispositions of property in which the decedent "retained at the time of his death the possession or enjoyment of, or right to income from, the property."²⁶² However, such a provision is easily circumvented be-

261. This provision would be similar to I.R.C. § 2036(a)(1) (1986) which includes transfers with a retained life estate in the federal gross estate. See *supra* note 216. Assuming that the statute applies to transfers pursuant to a contract, the proposed amendment should cover a shareholders agreement with a buy-sell provision, because the decedent-stockholder would have retained a life interest in the transferred stock. If the buy-sell provision requires payment of the purchase price fixed in the shareholders agreement to the decedent's estate, this proposal would benefit the surviving spouse only to the extent this provision requires inclusion in the estate of the amount by which the actual value of the stock exceeds the agreed upon purchase price. Under current law the purchase price itself would be includible in the net estate as a probate asset under EPTL § 5-1.1(c)(1) just as it would be includible in the gross estate for federal estate tax purposes as property owned by the decedent at death under I.R.C. § 2033 (1986). However, in many cases the purchase price is only a fraction of the stock's true value. See *In re Estate of Brown*, 446 Pa. 401, 403, 406, 289 A.2d 77, 78-79 (1972) (stating that surviving shareholder had option to purchase stock at \$1 per share whereas lowest fair market value figure submitted at trial was \$76 per share). To make the proposed provision reasonably meaningful, the stock should be valued using the federal estate tax approach as a model. See I.R.C. § 2036(c) (1986); Treas. Reg. § 20.2031-2(f) (1976); Rev. Rul. 59-60, 1959-1 C.B. 237, § 4.01. Cf. *Amodio v. Amodio*, 70 N.Y.2d 5, 509 N.E.2d 936, 516 N.Y.S.2d 923 (1987) (holding value of stock under shareholders agreement which met requirements of estate tax regulations was binding for purposes of equitable distribution). This valuation principle is particularly important because in many cases the stock may constitute the bulk of the decedent's assets. Parenthetically, New York does not now permit a challenge to "the adequacy of consideration under . . . a buy-sell provision when said consideration passes through the estate." *Isaacson v. Beau Label Corp.*, 93 A.D.2d 880, 880, 461 N.Y.S.2d 420, 421 (N.Y. App. Div. 1983). To the extent that there are monetary proceeds available from the sale of the shares, we do not recommend that the surviving spouse realize an elective share from any part of the stock of the company, as was suggested in *In re Burk*, 37 Pa. D. & C.2d 528, 532 (1965) (holding surviving spouse receive elective share of stock) and *In re Estate of Brown*, 446 Pa. 401, 407, 289 A.2d 77, 80 (1972) (discussing Orphans court opinion). To do so, would frustrate important purposes of a shareholders agreement, such as to ensure continuous management of and exclude outsiders from the company. See *supra* notes 30 and 37 (discussing *In re Estate of Brown* and purposes of shareholders agreements). To the fullest extent possible, the elective share should be satisfied using proceeds from the sale of the stock.

262. UPC § 2-202(l)(i)(1983); 20 PA. STAT. ANN. § 2203(a)(2) (Purdon Supp. 1988). The Pennsylvania statute gives the surviving spouse a life estate in one-third of any property in which the decedent "had the use of the property or an interest in or power to withdraw the income thereof."

Pennsylvania's section 11 did not cover a reservation of income for life. See *supra* note 37. The probable explanation for this omission, according to Bregy, is that "the spouse's rights arise only on the donor's death," and accordingly, "the disposition of income before that time is a matter of no concern." P. BREGY, *supra* note 143, at 5862. "This concept," he explained, "was favored over the philosophy that the spouse is entitled to a share of the property actually being enjoyed by the decedent during his life." *Id.*

cause it does not include a transfer that reserves the right to receive income until, for example, one month prior to the decedent's death. To close this loophole, these statutes should be amended to include the language proposed above.²⁶³

B. Contracts

The elective share statutes also should be explicitly clarified to include transfers, dispositions, or conveyances pursuant to contractual transactions such as the sale of shares under a buy-sell provision in a shareholders agreement.²⁶⁴ If a contract governs the transmission of any of a decedent's assets, even if the contract does not technically constitute a transfer, disposition or conveyance, the surviving spouse should be able to reach these assets under an elective share statute to the same extent as any lifetime transfer, disposition or conveyance of a decedent's property.²⁶⁵

C. Transfers for Value

Elective share statutes should exempt transfers with retained interests made for "full and adequate consideration in money or money's worth." Thus, to the extent that the decedent has not received full value for the property transferred pursuant to a contract or by conveyance, the value of the property transferred should be included in the net estate for elective share purposes, to the extent that such value exceeds the value of the consideration received. This approach would prevent disinheritance of the surviving spouse even if the transfer was part of a business transaction but full value was not received.²⁶⁶

263. This language is used in I.R.C. § 2036(a)(1) (1986). See *supra* note 216. Alternatively, if "time of death" is retained in the statute, the provision stating that a transfer subject to a retained power, the exercise of which is contingent on notice, should be subject to the surviving spouse's right of election. Such a notice provision would render the transfer includible in the federal gross estate by virtue of I.R.C. § 2038(b) (1986).

264. Inasmuch as *Riefberg* considered contracts to be subject to EPTL § 5-1.1(b)(1)(E), it may be unnecessary to amend that statute. See *supra* notes 37-42 and accompanying text (discussing *Riefberg* and EPTL).

265. Thus, contractual transactions should be subject to the elective share to the extent that they are not made for full consideration in money or money's worth. See *infra* note 266 and accompanying text.

266. See *supra* notes 177-78 and accompanying text (stating contract should be deemed for full and adequate consideration under elective share statutes only if full value is received for the underlying property transferred).

*D. Retained Powers**1. Operation of law*

As previously discussed,²⁶⁷ no reason exists to differentiate between a power to revoke or terminate reserved by the terms of the disposing instrument and such a power arising by operation of law, and elective share statutes should be amended to rectify this discrepancy. However, in view of the fact that parties to a contract cannot make the contract irrevocable, such amendments should exclude contracts made in the ordinary course of business, to the extent they are made for an adequate and full consideration in money or money's worth.²⁶⁸

2. For benefit of decedent or a third party

Property transfers as to which the decedent has retained a power to invade, consume, or dispose should be includible in the net estate regardless of whether the decedent is a beneficiary of the power. This proposal departs from the UPC and the Pennsylvania statute²⁶⁹ which reach only those transfers as to which the decedent retained a power to invade for his own benefit.²⁷⁰ Their approach is too restrictive, because it allows a decedent to retain significant economic control over the disposition of the property transferred during his lifetime and yet disinherit his spouse.²⁷¹ The consequence of decedent's retention of substantial economic control over the transferred property should be to treat the property for elective share purposes as if it had not been transferred.²⁷² Otherwise, a decedent who wants to disinherit his spouse without relinquishing substantial economic control would have a relatively easy and effective avenue, significantly reducing the protection that these statutes are designed to afford the surviving spouse.

*3. Subject to external standard**a. Retained powers exercisable for decedent's benefit*

Transfers as to which the decedent retains a power to invade for

267. See *supra* notes 93-108 and accompanying text.

268. See *supra* notes 176-78 and accompanying text.

269. See *supra* notes 190-92 and accompanying text (discussing Pennsylvania's elective share statute and UPC).

270. EPTL § 5-1.1(b)(1)(E) does not contain the words "for his own benefit." As pointed out previously, a settlor-trustee may not exercise a discretionary power for his own benefit. See *supra* note 185.

271. For example, the decedent can create an irrevocable trust and retain a power to invade or dispose in favor of anyone other than himself, and such a trust would not be includible under the UPC or Pennsylvania statutes.

272. This approach accords with the federal estate tax scheme.

his own benefit should be subject to the elective share statute regardless of the existence of an external standard or a mandatory power.²⁷³ Otherwise, the decedent through such transfers can retain virtually the same economic benefits as a reserved life estate while defeating the surviving spouse's elective share rights.²⁷⁴ Such transfers should be includible in the net estate for the same reasons that justify the inclusion of transfers with retained life interests.²⁷⁵ This should also apply when the decedent is the beneficiary but not the trustee and the trustee's power is mandatory or its exercise is subject to an external standard. In such cases, the decedent, in effect, has retained some form of a life interest because the trustee is under a duty to exercise the power, and the decedent has the right to enforce that duty and enjoy the transferred property.²⁷⁶

b. Retained powers exercisable for benefit of a third party

Transferred property subject to a retained power exercisable in favor of a third-party in the discretion of the decedent also should be includible in the net estate to the extent of the retained power, regardless of whether the decedent's discretion is unlimited or is subject to an external standard.²⁷⁷ Even if there is an external standard, the decedent enjoys a degree of control over the disposition of the property, notwithstanding imposition of specified parameters. Although in a limited number of cases the transfer may be appropriately excluded through application of the external standard doctrine (such as invasion to meet the costs of a medical emergency), in many circumstances external standards provide an inappropriate degree of discretion in which to operate (such as invasion for support and maintenance). The federal estate tax external standard approach should be inapplicable here²⁷⁸ because it does not promote the pur-

273. See *supra* notes 180-87 and accompanying text (discussing *Twersky*).

274. See UPC § 2-202 comment (1983) (discussing purpose of augmenting probate estate in computing elective share).

275. See *supra* notes 259-63 and accompanying text (discussing transfers with retained life interests).

276. See *supra* note 194 and accompanying text. The property should be includible only to the extent the power is exercisable.

277. Interestingly, Pennsylvania's current statute is narrower in this respect than its predecessor, section 11. See Estate Act of 1947, Pub. L. No. 100, § 11, 20 PA. CONS. STAT. ANN. § 301.11 (Purdon 1988) (repealed 1952) (quoted *supra* note 37). The current section only applies to powers exercisable for the decedent's personal benefit, whereas section 11 covered testamentary powers of appointment exercisable in favor of third parties. See *In re Estate of Behan*, 399 Pa. 314, 317-21, 160 A.2d 209, 213-15 (1960) (comparing current statute with section 11 of Estates Act of 1947).

278. Commentators have also criticized the external standard doctrine for these reasons in the estate tax area. See Pedrick, *Grantor Powers and Estate Taxation: The Ties That Bind*, 54 NW. U.L. REV. 527, 539-45 (1959) (noting limitations on decedent's power to exercise control).

poses of an elective share statute.²⁷⁹

Only if the decedent has made a transfer for the benefit of a third person and retained, as trustee, no more than a mandatory power, as evidenced in *Twersky*,²⁸⁰ should the transferred property be excluded from the net estate. In this instance, the decedent has only ministerial duties and has retained neither a benefit nor any meaningful opportunity to exercise discretion or judgment.²⁸¹ Because precisely the same distributions of trust corpus would be made whether or not the decedent were trustee, such transfers should not be subject to the surviving spouse's right of election.

4. *Time of exercise*

For the same basic reasons applicable to retained income interests,²⁸² property transferred subject to retained powers should be included in the net estate, even if exercise of a power is subject, at decedent's death, to a notice provision or contingency relating to the decedent's death.²⁸³

E. *Gifts to Minors*

No legitimate reason exists to differentiate under EPTL section 5-1.1(b)(1)(E) between a transfer in trust for the support of a minor child and the establishment of a custodial account for a minor child if the decedent's retained powers are the same. A donor who wishes to exclude such an account from the net estate for elective share purposes should simply not serve as custodian.²⁸⁴

A custodial account established by a parent should also be subject to the right of election under the UPC and the Pennsylvania statute.

279. Currently, because of the unified rate structure for estate and gift taxes, the external standard doctrine does not substantially affect the amount of revenue collected. A transfer with a retained power subject to an external standard would escape the estate tax but be treated as a completed transfer for gift tax purposes. This is not the case under an elective share statute because the surviving spouse is not able to elect against the decedent's "completed transfers," except to the extent that they were made in contemplation of death in Pennsylvania or in a UPC jurisdiction. See *supra* note 6.

280. See *supra* notes 180-84 and accompanying text.

281. See *supra* notes 185-86 and accompanying text (discussing decedent's maintenance of control over property).

282. See *supra* notes 261-63 and accompanying text.

283. For an example of a recent case in which decedent did not retain a power at the date of death, see *In re Kohut*, 133 A.D.2d 687, 687, 519 N.Y.S.2d 858, 859 (N.Y. App. Div. 1987). The court held that where the decedent's retained power to invade any contribution to the principal of the trust lapsed thirty days after receipt of notice from the trustee of such contribution, decedent, who died more than thirty days after her contribution, did not retain a "power to invade the trust at the date of her death" and the trust was not a testamentary substitute. *Id.*

284. See *supra* note 257 and accompanying text (discussing decedent's ability to use custodial funds rather than his own to support a minor child).

This should apply whenever the parent as custodian has the legal right under state law to use custodial funds to discharge the parent's legal obligation of support. But regardless of whether a parent-donor has the legal right, as custodian, to use custodial property for the minor's support, as a practical matter, it is likely that the custodian-parent will do so with impunity. Accordingly, a donor-parent's retained powers over a custodial account should be deemed to be for the decedent-parent's benefit and the custodial account should be includible in the net estate for elective share purposes.²⁸⁵

F. Life Insurance and Retirement Benefits

Contrary to the position taken by the UPC,²⁸⁶ the EPTL,²⁸⁷ and the Pennsylvania statute,²⁸⁸ we would include insurance proceeds and retirement benefits in the augmented or net estate²⁸⁹ to the same extent as any other transfer with reserved rights or interests.²⁹⁰ Currently, these payments are excluded from the net estate

285. If the minor child successfully asserts a claim against his parent's estate for improper use of custodial assets for the child's support, inclusion of the custodial funds would not increase the value of the estate for elective share purposes.

286. UPC § 2-202(1), 8 U.L.A. 77 comment (1983). The purpose of this section was to include those "kinds of transfers readily usable to defeat an elective share." *Id.* Accordingly, life insurance was excluded "because it is not ordinarily purchased as a way of depleting the probate estate and avoiding the elective share of the spouse" *Id.*

287. EPTL § 5-1.1(b)(2) (McKinney 1981). Estate of Hildebrand, N.Y.L.J., May 6, 1983, at 18, col. 1 (Westchester Co. Surr. Ct.) (holding death benefits are excluded from net estate).

288. 20 PA. CONS. STAT. ANN. § 2203(b) (Purdon Supp. 1988).

289. Also included in this category would be deferred compensation plans that have been held to be covered under the New York statute. See *In re Estate of Devita*, 132 Misc. 2d 185, 187-88, 503 N.Y.S.2d 267, 269 (Nassau Co. Surr. Ct. 1986), *aff'd*, 532 N.Y.S.2d 796 (N.Y. App. Div. 1988) (discussing implications of failure to exclude deferred compensation plans from EPTL § 5-1.1(b)(1)). Interestingly, in the Fourth Report, the Bennett Commission recommended that EPTL § 5-1.1(b)(1)(E) be amended "to exclude contributory pensions, profit-sharing plans, stock options, stock bonus and deferred compensation plans, as well as insurance proceeds." FOURTH REPORT, *supra* note 42, at 148. This report expressly commented "that none of these transactions were intended to be included [in subdivision E]." *Id.* The legislature enacted EPTL § 5-1.1(b)(2) which excludes insurance proceeds and pension and profit-sharing plans from subdivision (b)(1)(E) but does not mention deferred compensation plans.

In *In re Devita*, the Surrogate's Court said that "[t]he failure to exclude deferred compensation plans [from the coverage of EPTL section 5-1.1(b)(1)(E)] must be deemed" deliberate because of "[i]ts inclusion in an early version of the proposed statute [EPTL section 5-1.1(b)(2)] and its later omission in the legislation that was enacted into law" *In re Devita*, 132 Misc. 2d at 187-88, 503 N.Y.S.2d at 269. The court's reference to "an early version of the proposed statute" is apparently a reference to the FOURTH REPORT, because there appears to be no proposed statute that mentioned deferred compensation. *Id.* The Appellate Division, finding that the insurance spreadout plan at issue was different from a deferred compensation plan, agreed with the Surrogate that "omission of deferred compensation plans from EPTL § 5-1.1(b)(2) was not an oversight." 532 N.Y.S.2d at 799.

290. Macdonald contended that "the surviving spouse should have a stronger claim against the husband's life insurance than she would under the present estate tax provisions." MACDONALD, *supra* note 1, at 278. This position would subject property over which the decedent relinquished control to the right of election, which would unreasonably restrict the decedent's right to dispose of his property in situations in which he does not retain any control.

by EPTL section 5-1.1(b)(2) regardless of the beneficiary, while the UPC includes these payments in the augmented estate only if the surviving spouse is the beneficiary.²⁹¹ Insurance and retirement funds are major assets in many decedents' estates. To deprive the spouse of a share in such property could, in many cases, work a significant disinheritance.²⁹² Furthermore, insurance and retirement plans commonly constitute an important element of a savings plan. For example, a person frequently will give up present income in order to invest in a retirement plan or use income to purchase insurance. These substituted savings should be subject to the right of election if the decedent retained a beneficial interest or a prohibited power.²⁹³ There is no reason to treat insurance proceeds and retirement benefits any differently from other types of will substitutes. Indeed, the justification for excluding insurance proceeds from the elective share has been largely historical and is untenable today, given the fact that for many people, insurance constitutes the bulk of a decedent's estate, as well as a valuable lifetime asset.²⁹⁴

The central role insurance policies and retirement plans play in estate planning should also result in their includability in the net estate if the surviving spouse is the beneficiary. We thus endorse the position of the UPC,²⁹⁵ which we believe would prevent the sur-

To the extent that the decedent has retained any incidents of ownership with respect to an insurance policy, however, sufficient to trigger I.R.C. § 2042(2) (1986), the insurance proceeds should be includible in the net estate for elective share purposes.

291. UPC § 2-202(2), 8 U.L.A. 76-77 (1983).

292. There is also the danger that a decedent may use significant wealth to purchase insurance policies. Although this possibility was recognized by the drafters of the UPC, they did not view it as a major problem because insurance "is not ordinarily purchased as a way of depleting the probate estate." Thus, the drafters decided against including insurance proceeds payable to persons other than a spouse in the augmented estate. UPC § 2-202(1), 8 U.L.A. 77 comment (1983). See *supra* note 286 (discussing purchase of life insurance to deplete probate estate).

293. For example, retention of a power to revoke, consume, invade or dispose.

294. New York, Pennsylvania and the UPC all appear to have excluded insurance proceeds (the UPC excluding them only when payable to a third party) from the net or augmented estate out of deference to tradition. Although the Report noted that life insurance is "a potential weapon of evasion," it observed that "[o]n the whole the courts appear to assume that life insurance is immune to the widow's attack." REPORT, *supra* note 5, at 128. In its conclusion, the Report summarily states that "[t]he surviving spouse will not be permitted to attack insurance policies or annuities." *Id.* at 139. See *supra* note 292 (discussing implications of purchase of insurance policies). In Pennsylvania, the Supreme Court allowed a widow to elect against the proceeds of an insurance trust under section 11. *In re Estate of Brown*, 384 Pa. 99, 119 A.2d 513 (1956). However, the statute was amended in 1956, in response to this decision, specifically to exclude insurance policies from the right of election. 20 PA. STAT. ANN. tit. 20, 301.11(a) (amended by 20 PA. CONS. STAT. ANN. § 2203(a) (Purdon Supp. 1988)).

295. The Comments to UPC § 2-202 advocate inclusion of insurance proceeds payable to the surviving spouse "because it seems unfair to allow a surviving spouse to disturb the decedent's estate plan if the spouse has received ample provision from life insurance." 8 U.L.A. 78 (1983).

living spouse from receiving a windfall²⁹⁶ and still promote a decedent's legitimate estate plan. The possibility of a windfall is particularly evident with respect to retirement benefits governed by the Retirement Equity Act of 1984.²⁹⁷ Therefore, elective share statutes should take into account retirement benefits paid to the surviving spouse in determining whether the spouse is entitled to any additional property from the decedent's estate.

G. Gifts in Contemplation of Death

Neither the New York statute nor the UPC approach to gifts in contemplation of death is effective. EPTL section 5-1.1(b)(1)(A) includes gifts *causa mortis*²⁹⁸ in the net estate, most likely on the theory that such gifts are revocable up to the time of death and, therefore, subject to the decedent's control during life.²⁹⁹ From a theoretical viewpoint such transfers should be includible in the net estate for elective share purposes, but the evidentiary problems associated with proving whether a gift has, in fact, been made *causa mortis* make this approach undesirable.

The UPC approach, which avoids these difficulties by including all substantial gifts made by the decedent within two years of death,³⁰⁰ extends too far. Because subjecting such transfers to the right of election may interfere with legitimate tax planning, impose re-

296. This possibility exists in New York where a spouse could receive, for example, one million dollars of insurance and still elect against a will which gives the balance of the decedent's probate estate to others. The danger of a windfall is particularly great with respect to benefits governed by the Retirement Equity Act of 1984 (REA), Pub. L. No. 98-357, 98 Stat. 397 (1984), which essentially requires that the surviving spouse be entitled to receive at least one-half of the decedent's account balance if the spouses were married for at least one year prior to the annuity starting date or the decedent's death. I.R.C. §§ 401(a)(11), (13) and 417(d) (1986). REA may preempt any state law that would include qualified retirement benefits in the surviving spouse's elective share. See S. REP. NO. 575, 98th Cong., 2d Sess. 16-17, reprinted in 1984 U.S. CODE CONG. & ADMIN. NEWS 2547, 2562-63. Consequently, in some cases, the surviving spouse may receive too great a share of the decedent's estate, and REA should be amended to guarantee the surviving spouse only a fractional share in the decedent's retirement benefits that is properly integrated with state law.

297. *Id.*

298. EPTL § 5-1.1(b)(1)(A) (McKinney 1981).

299. The Report gives virtually no explanation of why such gifts should be included in the net estate, but merely states that "[c]ertainly the gift *causa mortis*, of all transfers, should not be immune to the widow's claim." REPORT, *supra* note 5, at 126 (quoting from W. MACDONALD, *supra* note 1, at 197).

300. UPC § 2-202(1)(iv), 8 U.L.A. 76 (1983). See *supra* note 6. This section is "designed to prevent a person from depleting his estate in contemplation of death." See *id.*, 8 U.L.A. 77 comment. It appears to have been influenced by I.R.C. § 2035 (1954), which included in the federal gross estate all gifts made by the decedent within three years of death. The Economic Recovery Tax Act of 1981, however, substantially cut back this section, and it now applies only (for purposes of this article) to the relinquishment within three years of death of powers retained pursuant to I.R.C. §§ 2036, 2037, 2038, and transfers of life insurance during that three-year period. I.R.C. § 2035 (1986). See also 20 PA. CONS. STAT. ANN. § 2203(a)(6) (Purdon Supp. 1988) (one year provision).

straints on alienation, and generate difficult tracing problems,³⁰¹ an elective share statute should choose a shorter time period (such as one year) within which to capture gifts made in contemplation of death. This length of time should suffice to capture most gifts made by a seriously ill individual who desires to disinherit a surviving spouse while allowing flexibility in estate tax planning by individuals seeking to minimize their taxable estates.³⁰²

A related UPC provision includes in the augmented estate all transfers from the decedent to the surviving spouse, regardless of when made, to the extent the property is owned by the surviving spouse at the decedent's death or was given by the spouse to third persons if such property would have been included in the spouse's augmented estate.³⁰³ This provision is objectionable because it presumes that all such outright transfers to the spouse should, in effect, be viewed as advancements and credited against the surviving spouse's inheritance. This property should only be includible in the augmented estate if the transfer was substantial (such as in excess of \$10,000 in any year) or accompanied by a contemporaneous writing signed by the decedent expressing an advancement intent.³⁰⁴

H. Joinder of Surviving Spouse in Lifetime Transfers

The UPC approach that excludes from the augmented estate "[a]ny transfer . . . if made with the written consent or joinder of the surviving spouse" should be incorporated into any revised elective share statute.³⁰⁵ Consent of the surviving spouse permits estate planning with greater certainty. If the surviving spouse's consent has been freely given, it should preclude an election against the transferred property after the decedent's death.

301. For example, consider an individual who is otherwise healthy and wishes to minimize estate taxes by utilizing the gift tax annual exclusion of section 2503(b) by giving \$10,000 to each of three children. Although not taxable as gifts or includible in the individual's gross estate if death occurs within two years, these transfers will be includible in the augmented estate under the UPC to the extent they exceed \$3,000 per donee and would thereby inhibit legitimate estate tax planning.

302. It would be highly unlikely for a decedent to transfer irrevocably significant portions of his estate prior to death even if death is certain. See, e.g., *In re Estate of Riefberg*, 58 N.Y.2d 134, 446 N.E.2d 424, 459 N.Y.S.2d 739 (1983) (finding amendment to shareholders agreement entered into one day prior to death); *Newman v. Dore*, 275 N.Y. 371, 9 N.E.2d 966 (finding revocable trust consisted of all of decedent's real and personal property created three days prior to death).

303. UPC § 2-202(2), 8 U.L.A. 76 (1983). This section includes such property "to the extent [it] . . . is derived from the decedent by any means other than testate or intestate succession without a full consideration in money or money's worth." *Id.*

304. Cf. EPTL § 2-1.5 (McKinney 1981) (advancements); UPC § 2-110, 8 U.L.A. 69 (1983) (same).

305. UPC § 2-202(1), 8 U.L.A. 76 (1983). Accord EPTL § 5-1.1(f) (McKinney 1981).

CONCLUSION

The proposed guidelines, if adopted, would significantly clarify the elective share statutes that we have discussed while ensuring that surviving spouses are afforded the protection these statutes are designed to provide. In addition, they should facilitate estate planning for individuals who want to give their spouses no more than the statutory elective share, substantially reduce the amount of litigation in this area by better delineating precisely which types of dispositions are includible in the net estate, and prevent surviving spouses from receiving unjustified economic windfalls.

APPENDIX

20 Pa. Stat. Ann. 2203 (*Purdon Supp. 1988*)

§ 2203. Right of election; resident decedent

(a) Property subject to election.—When a married person domiciled in this Commonwealth dies, his surviving spouse has a right to an elective share of one-third of the following property:

- (1) Property passing from the decedent by will or intestacy.
- (2) Income or use for the remaining life of the spouse of property conveyed by the decedent during the marriage to the extent that the decedent at the time of his death had the use of the property or an interest in or power to withdraw the income thereof.
- (3) Property conveyed by the decedent during his lifetime to the extent that the decedent at the time of his death had a power to revoke the conveyance or to consume, invade or dispose of the principal for his own benefit.
- (4) Property conveyed by the decedent during the marriage to himself and another or others with right of survivorship to the extent of any interest in the property that the decedent had the power at the time of his death unilaterally to convey absolutely or in fee.
- (5) Survivorship rights conveyed to a beneficiary of an annuity contract to the extent it was purchased by the decedent during the marriage and the decedent was receiving annuity payments therefrom at the time of his death.
- (6) Property conveyed by the decedent during the marriage and within one year of his death to the extent that the aggregate amount so conveyed to each donee exceeds \$3,000, valued at the time of conveyance.

In construing this subsection, a power in the decedent to withdraw income or principal, or a power in any person whose interest is not adverse to the decedent to distribute to or use for the benefit of the

decedent any income or principal, shall be deemed to be a power in the decedent to withdraw so much of the income or principal as is subject to such power, even though such income or principal may be distributed only for support or other particular purpose or only in limited periodic amounts.

(b) Property not subject to election.—The provisions of subsection (a) shall not be construed to include any of the following except to the extent that they pass as part of the decedent's estate to his personal representative, heirs, legatees or devisees:

- (1) Any conveyance made with the express consent or joinder of the surviving spouse.
- (2) The proceeds of insurance, including accidental death benefits, on the life of the decedent.
- (3) Interests under any broad-based nondiscriminatory pension, profit-sharing, stock bonus, deferred compensation, disability, death benefit or other such plan established by an employer for the benefit of its employees and their beneficiaries.
- (4) Property passing by the decedent's exercise or nonexercise of any power of appointment given by someone other than the decedent.

N.Y. Est. Powers & Trusts Law 5-1.1 (McKinney 1981) (selected portions)

...

(b) Inter vivos dispositions treated as testamentary substitutes for the purpose of election by surviving spouse.

(1) Where a person dies after August thirty-first, nineteen hundred sixty-six and is survived by a spouse who exercises a right of election under paragraph (c), the following transactions effected by such decedent at any time after the date of the marriage and after August thirty-first, nineteen hundred sixty-six, whether benefiting the surviving spouse or any other person, shall be treated as testamentary substitutes and the capital value thereof, as of the decedent's death, included in the net estate subject to the surviving spouse's elective right:

(A) Gifts causa mortis.

(B) Money deposited, after August thirty-first, nineteen hundred sixty-six, together with all dividends credited thereon, in a savings account in the name of the decedent in trust for another person, with a banking organization, savings and loan association, foreign banking corporation or organization or bank or savings and loan association organized under the laws of the United States, and remaining on deposit at the date of the decedent's death.

(C) Money deposited, after August thirty-first, nineteen hundred

sixty-six, together with all dividends credited thereon, in the name of the decedent and another person and payable on death, pursuant to the terms of the deposit or by operation of law, to the survivor, with a banking organization, savings and loan association, foreign banking corporation or organization or bank or savings and loan association organized under the laws of the United States, and remaining on deposit at the date of the decedent's death.

(D) Any disposition of property made by the decedent after August thirty-first, nineteen hundred sixty-six whereby property is held, at the date of his death, by the decedent and another person as joint tenants with a right of survivorship or as tenants by the entirety.

(E) Any disposition of property made by the decedent after August thirty-first, nineteen hundred sixty-six, in trust or otherwise, to the extent that the decedent at the date of his death retained, either alone or in conjunction with another person, by the express provisions of the disposing instrument, a power to revoke such disposition or a power to consume, invade or dispose of the principal thereof. The provisions of this paragraph shall not affect the right of any income beneficiary to the income undistributed or accrued at the date of death.

(2) Nothing in this paragraph shall affect, impair or defeat the right of any person entitled to receive (A) payment in money, securities or other property under a thrift, savings, pension, retirement, death benefit, stock bonus or profit-sharing plan, system or trust, (B) money payable by an insurance company or a savings bank authorized to conduct the business of life insurance under an annuity or pure endowment contract, a policy of life, group life, industrial life or accident and health insurance or a contract by such insurer relating to the payment of proceeds or avails thereof or (C) payment of any United States savings bond payable to a designated person, and such transactions are not testamentary substitutes within the meaning of this paragraph.

(3) Transactions described in subparagraphs (C) or (D) shall be treated as testamentary substitutes in the proportion that the funds on deposit were the property of the decedent immediately before the deposit or the consideration for the property held as joint tenants or as tenants by the entirety was furnished by the decedent. The surviving spouse shall have the burden of establishing the proportion of the decedent's contribution. Where the other party to a transaction described in subparagraphs (C) or (D) is a surviving spouse, such spouse shall have the burden of establishing the pro-

portion of his contribution, if any. For the purpose of this subparagraph, the surrogate's court may accept such evidence as is relevant and competent, whether or not the person offering such evidence would otherwise be competent to testify.

(4) The provisions of this paragraph shall not prevent a corporation or other person from paying or transferring any funds or property to a person otherwise entitled thereto, unless there has been served personally upon such corporation or other person a certified copy of an order enjoining such payment or transfer made by the surrogate's court having jurisdiction of the decedent's estate or by another court of competent jurisdiction. Such order may be made, on notice to such persons and in such manner as the court may direct, upon application of the surviving spouse or any other interested party and on proof that the surviving spouse has exercised his right of election under paragraph (c). Service of a certified copy of such order on the corporation or other person holding such fund or property shall be a defense to it, during the effective period of the order, in any action or proceeding brought against it which involves such fund or property.

(5) This paragraph shall not impair or defeat the rights of creditors of the decedent with respect to any matter as to which any such creditor has rights.

(6) In case of a conflict between this paragraph and any other provision of law affecting the transactions described in subparagraph (1), this paragraph controls.

(c) Election by surviving spouse against wills executed and testamentary provisions made after August thirty-first, nineteen hundred sixty-six; election where decedent dies intestate as to all or any part of his estate.

(l) Where, after August thirty-first, nineteen hundred sixty-six, a testator executes a will disposing of his entire estate, and is survived by a spouse, a personal right of election is given to the surviving spouse to take a share of the decedent's estate, subject to the following:

(A) For the purposes of this paragraph, the decedent's estate includes the capital value, as of the decedent's death, of any property described in subparagraph (b)(1).

(B) The elective share, as used in this paragraph, is one-third of the net estate if the decedent is survived by one or more issue and, in all other cases, one-half of such net estate. In computing the net estate, debts, administration and reasonable funeral expenses shall be deducted but all estate taxes shall be disregarded, except that nothing contained herein relieves the surviving spouse from con-

tributing to all such taxes the amounts apportioned against him under 2-1.8.

(C) The term 'testamentary provision,' as used in this paragraph, includes, in addition to dispositions made by the decedent's will, any transaction described as a testamentary substitute in subparagraph (b)(1).

...

(2) Where, after August thirty-first, nineteen hundred sixty-six, a person dies intestate as to all or any part of his estate, and, in the case of part intestacy, executes a will after such date, and is survived by a spouse, a personal right of election is given to the surviving spouse to take a share of the testamentary provisions made by the decedent, as such provisions are defined in subparagraph (1)(C), subject to the following:

(A) The share of the testamentary provisions to which the surviving spouse is entitled hereunder is his elective share, as defined in subparagraphs (1)(A) and (B), reduced by the capital value of all property passing to such spouse (i) in intestacy under 4-1.1, (ii) by testamentary substitute as described in subparagraph (b)(1) and (iii) by disposition under the decedent's last will.

(B) The satisfaction of such elective share shall not reduce the intestate share of any other distributee of the decedent.

(C) Whenever a testamentary provision for the surviving spouse takes the form of income payable for his life:

(i) The surviving spouse has the limited right to elect to take, absolutely, the sum of ten thousand dollars or the share to which he is entitled hereunder, whichever is less. Such sum, however, is inclusive of any absolute testamentary provision, as described in subparagraph (1)(C), and any amount to which the surviving spouse is entitled in intestacy under 4-1.1, and is payable from the principal of any trust, legal life estate or annuity created by such testamentary provision, the terms of which remain otherwise effective.

...

UPC Section 2-202 [Augmented Estate]

The augmented estate means the estate reduced by funeral and administration expenses, homestead allowance, family allowances and exemptions, and enforceable claims, to which is added the sum of the following amounts:

(1) The value of property transferred to anyone other than a bona fide purchaser by the decedent at any time during marriage, to or for the benefit of any person other than the surviving spouse, to the extent that the decedent did not receive adequate and full con-

sideration in money or money's worth for the transfer, if the transfer is of any of the following types:

- (i) Any transfer under which the decedent retained at the time of his death the possession or enjoyment of, or right to income from, the property;
- (ii) Any transfer to the extent that the decedent retained at the time of his death a power, either alone or in conjunction with any other person, to revoke or to consume, invade or dispose of the principal for his own benefit;
- (iii) Any transfer whereby property is held at the time of decedent's death by decedent and another with right of survivorship;
- (iv) Any transfer made to a donee within two years of death of the decedent to the extent that the aggregate transfers to any one donee in either of the years exceed \$3,000.

Any transfer is excluded if made with the written consent or joinder of the surviving spouse. Property is valued as of the decedent's death except that property given irrevocably to a donee during lifetime of the decedent is valued as of the date the donee came into possession or enjoyment if that occurs first. Nothing herein shall cause to be included in the augmented estate any life insurance, accident insurance, joint annuity, or pension payable to a person other than the surviving spouse.

(2) The value of property owned by the surviving spouse at the decedent's death, plus the value of property transferred by the spouse at any time during marriage to any person other than the decedent which would have been includible in the spouse's augmented estate if the surviving spouse had predeceased the decedent, to the extent the owned or transferred property is derived from the decedent by any means other than testate or intestate succession without a full consideration in money or money's worth. For purposes of this Paragraph:

- (i) Property derived from the decedent includes, but is not limited to, any beneficial interest of the surviving spouse in a trust created by the decedent during his lifetime, any property appointed to the spouse by the decedent's exercise of a general or special power of appointment also exercisable in favor of others than the spouse, any proceeds of insurance (including accidental death benefits) on the life of the decedent attributable to premiums paid by him, any lump sum immediately payable and the commuted value of the proceeds of annuity contracts under which the decedent was the primary annuitant attributable to premiums paid by him, the commuted value of amounts payable after the decedent's death under any public or private pension, disabil-

ity compensation, death benefit or retirement plan, exclusive of the Federal Social Security system, by reason of service performed or disabilities incurred by the decedent, any property held at the time of decedent's death by decedent and the surviving spouse with right of survivorship, any property held by decedent and transferred by contract to the surviving spouse by reason of the decedent's death and the value of the share of the surviving spouse resulting from rights in community property in this or any other state formerly owned with the decedent. Premiums paid by the decedent's employer, his partner, a partnership of which he was a member, or his creditors, are deemed to have been paid by the decedent.

(ii) Property owned by the spouse at the decedent's death is valued as of the date of death. Property transferred by the spouse is valued at the time the transfer became irrevocable, or at the decedent's death, whichever occurred first. Income earned by included property prior to the decedent's death is not treated as property derived from the decedent.

(iii) Property owned by the surviving spouse as of the decedent's death, or previously transferred by the surviving spouse, is presumed to have been derived from the decedent except to the extent that the surviving spouse establishes that it was derived from another source.

(3) For purposes of this section a bona fide purchaser is a purchaser for value in good faith and without notice of any adverse claim. Any recorded instrument on which a state documentary fee is noted pursuant to [insert appropriate reference] is prima facie evidence that the transfer described therein was made to a bona fide purchaser.

