Tax manual of the Federal Revenue Act of 1942 and prior laws illustrating their effect on life insurance, endowments and annuities.

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THE PENN MUTUAL LIFE INSURANCE COMPANY
PHILADELPHIA, PA.

TAX MANUAL

OF

THE FEDERAL REVENUE ACT OF 1942 AND PRIOR LAWS

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TAX MANUAL

of

The Federal Revenue Act of 1942 and Prior Laws

ILLUSTRATING THEIR EFFECT ON LIFE INSURANCE, ENDOWMENTS AND ANNUITIES

(*Second Printing*)

The Penn Mutual
Life Insurance Company
Philadelphia, Pa.

No. 1835 Rev. 11-43

Why is life insurance the most economical and effective method of paying inheritance taxes?

BECAUSE:

1. The contract instantly protects the estate.
2. The contract matures when the lien attaches.
3. The contract is redeemable in cash, the medium by which taxes must be paid.
4. The premium deposits create a sinking fund to pay a preferred claim.
5. The premium deposits are insignificant compared to the guaranteed protection.

Trained Penn Mutual representatives are prepared to advise you in the creation, distribution and preservation of your estate.

THE PENN MUTUAL
LIFE INSURANCE COMPANY

INDEPENDENCE SQUARE
PHILADELPHIA

Printed in the U. S. A.

PREFACE

To the Fifteenth Edition

Next January it will be twenty-five years since the first publication of this Manual. Approximately 125,000 copies have been distributed.

Devised primarily as an instrument of education for Penn Mutual underwriters, the Manual has rendered profitable service to executives, lawyers, accountants, trust officers and policyholders, who have found, in its abbreviated form, ready answers to questions of the moment, with citations to assist more detailed inquiry if desired. No attempt has been made to cite all the cases in support of an answer, but the inquirer will find that most of the cases cited contain lists of prior decisions on points germane to the issue.

The term "annuity," as used in this book, means a contract issued by a life insurance company which immediately or eventually pays an income (annually, semi-annually, quarterly or monthly) to the beneficial holder of the contract. It should be distinguished on the one hand from a testamentary annuity which arises from the bequest of a decedent, and on the other hand from a life insurance policy, the proceeds of which are sometimes paid at death in instalments that have the form of an annuity. All three types of beneficiaries enjoy what is popularly termed an "annuity" and all pay taxes; but they are taxable in three different ways.

The Revenue Act of 1942 has made more changes than any law since the Revenue Act of 1918 which inaugurated the estate tax of life insurance proceeds paid to named beneficiaries. While 1918 levied the tax it allowed $40,000 exemption, and this, 1942 has taken away.

Today there is a $60,000 overall exemption applicable to life insurance and general estate, instead of $40,000 each for life insurance and general estate, or $80,000 in all. This means that so far as Federal Estate Tax is concerned life insurance need not be paid to a named beneficiary—although for State Inheritance Tax and other reasons, that procedure still is desirable. Totally tax exempt life insurance still may be created but no ownership must exist in the insured and the insured must not pay any premiums.

In Gift Tax there likewise has been a reduction of general exemption from $40,000 to $30,000 and in specific annual gifts from $4,000 to $3,000.

In Income Tax there is a complete new section devoted to Employees' Trusts, according rather liberal deductions to employers who contribute to such plans if not discriminatory, and allowing employees the privilege of non-inclusion until they receive something of value—in other words, when the pension begins.

Another concession by Congress is to permit the assigning of business insurance from one firm to another without exposure to Income Tax on the proceeds, provided the transfer of business assets is non-taxable. This has been much needed and will save the surrender of life insurance where there is no necessity or desire to do so.

Interest paid on money borrowed to purchase single premium insurance is no longer deductible. In the past there have been a few transactions of this type. As money can be borrowed for 3% and less if the security is triple A and life insurance cash values increase at appxoximately the same rate, the taxpayer has been increasing his values exempt of tax and deducting interest paid from gross income. This needed correction.

In Higgins vs. Smith, 60 S. Ct. 355, the Supreme Court said, "The Government may look at actualities and upon determination that the form employed for doing business or carrying out the challenged tax event is unreal or a sham, may sustain or disregard the effect of the fiction as best serves the purpose of the statute."

Obviously, the answers in the Manual are not guaranteed. Emphatic as this admonition has been in the past, when the law was comparatively simple in structure and language, it is much more necessary today. The sources of these answers should be consulted by the exacting reader. But it is hoped that this Manual will assist Penn Mutual underwriters to be the best informed in their communities and to convert their training not only into paid production, but into the ultimate of service to policyholders.

We invite you, the reader, to share with us our pride in the institution of life insurance. We have faith in our business. Benjamin Franklin's wise allusion to this uncertain world and the fact that we can be sure of only "death and taxes" has now gained a third guaranty, life insurance protection. In our country's most trying times of financial depression and now in a war of survival, it has written an epic of dependability. When the most solemn obligations failed, life insurance redeemed its promises. If it be true that our most perplexing problem is to provide social security for all, while maintaining a reasonable measure of liberty for the individual, then never before has Government charged with this responsibility received such salutary aid from private enterprise.

Grateful acknowledgment is here made to Warner F. Haldeman, Esq., Associate Counsel, Robert W. Hamilton, Esq., Assistant Counsel and Lawrence M. Bregy, Attorney, for assisting in the completion of this work and contributing valuable suggestions for its improvement.

E. PAUL HUTTINGER,
Second Vice-President

November, 1943

N.B.—Between chapters a jump in question numbers will be observed. This is to enable us to insert new questions in later editions without renumbering the questions and revising the entire index.

ABBREVIATIONS

The following abbreviations are used throughout the Manual to designate source of authority:

A. R. R.—Committee on Appeals and Review.

Art.—Article (of Regulations).

B. T. A.—Decision of Board of Tax Appeal now known as the Tax Court of U. S.

C. B.—Cumulative Bulletin (published by Revenue Bureau).

C. C. A.—U. S. Circuit Court of Appeals.

Fed.—Lower Court Decision. U. S.

Fed. Supp.—U. S. Dis't Ct. and Ct. of Claims.

G. C. M.—General Counsel Memorandum.

I. T.—Decision of Income Tax Unit.

L.—Law (Revenue Acts of 1926, 1932, 1934, 1935, 1936, 1938, First and Second Revenue Acts of 1940, and Revenue Act of 1942.) Reference is to Sections.

Memo B. T. A.—Memorandum of the Board. (now Tax Court of U. S.)

O.—Opinion of Solicitor of Revenue Bureau.

O. D.—Office Decision of Revenue Bureau.

Reg. 80.—Regultaions No. 80, Estate Tax.

Reg. 103—Regulations No. 103, Income Tax.

Reg. 79—Regulations No. 79, Gift Tax.

S. M.—Solicitor's Memorandum.

S. O.—Solicitor's Opinion.

T. B. R.—Advisory Tax Board Recommendation.

T. C.—Tax Court, formerly Board of Tax Appeals.

T. D.—Treasury Decision.

U. S. also S. Ct.—Decision of U. S. Supreme Court.

Letters mentioned were from the Commissioner of Internal Revenue.

CONTENTS

INCOME TAX

GENERAL PROVISIONS

1. Q. *What payments, in general, received from life insurance companies are subject to Income Tax?*

   A. (a) Annuities
   (b) Endowments paid in instalments
   (c) Profits on surrender of life insurance, endowment (surrender and maturity) and annuity contracts
   (d) Interest on proceeds retained by the company
   (e) Interest in instalment payments elected by a beneficiary
   (f) Profits made upon death or surrender of policies bought for valuable consideration.

2. Q. *How are annuities taxed?*

   A. (a) 3% of the consideration paid for the contract should be included in gross taxable income each year. This renders a portion of the annuity income exempt. After the exempt portion of the annuity cumulatively equals the purchase price, then the entire annuity received each year is included in gross income. For instance, taxpayer buys annuity of $2,000 annually for \$25,000. He includes in gross income \$25,000 × .03 = \$750 each year. That leaves \$1,250 exempt. In 20 years all the annuity income will be taxable.

(b) If the annuity was bought in the past and payments were not included in gross income, under the law then in force, such payments will be added to the current exempt income and will hasten the time when the entire annuity must be reported. L. 22 (b) (2); *Reg. 103, Sec. 19.22 (b) (2) (A)*—2.

(c) Where an annuity is bought for \$50,000 paying \$3,912 a year in semi-annual instalments, the first payment is for *only* 2 months, amounting to \$652. The amount included in gross income is \$50,000 × .03 = \$1,500 ÷ 12 = \$125 × 2 = \$250. *I. T. 3221. C. B. 1938-2.*

(d) Where the annuity becomes wholly taxable in the middle of the year, compute as follows: To the total exempt income up to the end of the prior taxable year add income of current year and subtract premium paid. Thus, annuitant paid \$5,000. She got up to December 31, 1939, tax-free income of \$4,808.55. In 1940 she received \$545.40. Add together and the result is \$5,353.95. Subtract \$5,000, and the remainder \$353.95 is taxable as income.

A refund payable under a refund annuity which continues income to the beneficiary after death of the annuitant is subject to Income Tax. The commuted value of the refund at the annuitant's death is divided by the remaining years that income is guaranteed. This gives the principal in each year which is exempt. The beneficiary should subtract this amount from the annual income received for the year, the result being taxable income. *I. T. 3140, XVI–49–9069.*

(e) The annuity income payable to the surviving annuitant under a joint and survivorship annuity is subject to tax in the same manner as other annuity income. That is to say, the survivor must include as income 3% of the consideration paid, until the exempt incomes received by both the original annuitant and the survivor exceed the consideration paid; after which the entire annuity becomes taxable income. *I. T. 3077, XVI–21–8716.*

(f) Where a joint and survivorship annuity is bought by the husband and is payable to him *or* his wife, the income, computed in the manner set forth in 2 (a) above, is taxable to the husband. *I. T. 3092, XVI–27–8794.*

(g) If premiums are paid in advance and discounted, the discounted value should be used in determining the aggregate premiums or consideration paid under *Sec. 22 (B) (2). I. T. 3513.*

(h) This section does not apply to annuities that are bought by husband to satisfy alimony claims of wife. That is to say, he does not report the income. She does. *L. 22 (b) (2), 22k.*

3. Q. *How are instalments payable under a matured endowment affected by Income Tax?*

A. In the same way as an annuity. See Question 2. After an endowment matures the life insurance factor becomes extinct and the contract if payable in instalments partakes of the nature of an annuity although it may still be known as an endowment. The consideration for the annuity is the premiums paid. Instalment settlement must be elected *before* maturity in accordance with the terms of the policy. Helvering, Com'r to Louis E. Whyte, 9/13/43. *L. 22 (b) (2); Reg. 103, Sec. 19.22 (b) (2)–2. I. T.3202–1938.*

4. Q. *How are profits on the surrender of life insurance, endowment (surrender or ma-*

turity) and annuity contracts, for cash affected by Income Tax?

A. When the insured or annuitant surrenders his contract to the company for cash (or matures an endowment), the difference between what he paid and what he receives, including dividends and interest, represents a profit to him. This profit should be included in gross taxable income. *L. 22 (b) (2); Reg. 103, Sec. 19.22 (b) (2)–1.*

5. Q. *How is straight interest on proceeds (Option D) paid by reason of death affected by Income Tax?*

A. Such interest is treated in the same manner as the taxable interest on any other obligation of indebtedness. The beneficiary or taxpayer includes the interest received in gross taxable income. *L. 22 (b) (1); Reg. 103, Sec. 19.22 (b) (1)–1 (a).* It makes no difference whether the interest is paid at the direction of the insured or the beneficiary. *T. D. 5231.*

6. Q. *How is the interest item in an instalment payment affected by Income Tax?*

A. Guaranteed interest in an instalment paid to the beneficiary at the direction of the insured, is exempt. Com'r vs. Buck, *120* Fed. (2) *775*; Allis vs. LaBudde, *128 Fed.* (*2*) *838*; L. E. Kaufman vs. U. S. *131 Fed.* (*2*) *854; C. C. A.* (*4*); *Reg. 103, Sec. 19.22* (*b*) (*1*)—*1* as amended by *T. D. 5231,* which is retroactive and applies to corresponding articles of Regulations 86, 94 and 101.

This exemption also includes extra interest paid over and above the guaranteed rate. *Letter 4/17/'43, T. Mooney to Fidelity Mutual.* It does not include interest in instalments selected by beneficiary owner of policy before insured's death or where contract payable only in instalments. *Letter T. Mooney to Aetna,* 10/8/'43.

To compute the taxable interest where the beneficiary selects the instalment option, according to *Reg. 103, Sec. 19.22* (*b*) (*1*)–*1* (*a*) (*b*) (*c*) (*d*), ascertain the face value of the policy at the death of the insured and divide the face value by the number of years guaranteed or the life expectancy of the beneficiary whichever is greater. This calculation gives you the amount of *principal* in each instalment, which is exempt. The difference between this principal and the sum received by the beneficiary in the taxable year is deemed to be interest and should be included in gross taxable income. *L. 22 (b) (1); Reg. 103, Sec. 19.22 (b) (1)–1 (b), (c)* and *(d). I.T. 3202.* Prior to January 1, 1934, interest in instalment proceeds was not taxed as income, but payments received in prior years enter into the calculation. See (2) Option A, below. See different rule for Option B.

ILLUSTRATIONS SHOWING COMPUTATION OF INTEREST PORTION OF INSTALMENT PAYMENTS

(1) *OPTION A—20 Years Certain. First Payment 1942.*

(Instalments) 20)$10,000.00—proceeds at death

$500.00—average amount of proceeds included in each instalment

$625.80—payment of guaranteed instalment (Present Option)

Less 500.00—tax exempt proceeds included in 1942 payment

$125.80—taxable interest received in 1942

(2) *OPTION A—20 Years Certain. First Payment 1930*

$10,000.00—proceeds at death

*Less 3,108.26—aggregate amount of payments 1930 to 1933, inclusive **

* Rule became effective January 1, 1934.

(Remaining instalments) 16) $6,891.74—tax exempt proceeds still to be received

$ 430.73—average amount of proceeds included in 1934 and subsequent instalments

$652.60—amount of guaranteed instalment (Old Option)
Less 430.73—tax exempt proceeds included in 1942 payment

$ 221.87—taxable interest received in 1942

OPTION F (without refund)—FEMALE 64—First Payment 1942

Annual Income—$682.90 (Present Option)

(Life expectancy of beneficiary) 19)$10,000.00—Proceeds at death

$ 526.32—average amount of proceeds included in instalments

$682.90—guaranteed payment
526.32—exempt portion of payment (first 19 years)

$ 156.58—taxable interest included in each payment during 19 year period—thereafter the entire amount of each payment will be subject to Income Tax

OPTION F (without refund)—FEMALE 64 at time proceeds applied. First payment in 1932

Annual Income—$877.50 (Old Option)
$10,000.00—proceeds at death
Less 1,755.00—aggregate amount of payment 1932 and 1933 *

* Rule became effective January 1, 1934.

(Life expectancy of beneficiary) 15) $8,245.00
January 1, 1934

$ 549.67—exempt portion of payment during 15 years from January 1, 1934
$877.50—guaranteed payment

549.67—exempt portion of payment next 15 years

$327.83—taxable interest included in each payment during 15 year period from January 1, 1934

OPTION B—20 Years Certain and Continuous. First payment in 1942

Female Beneficiary Age 50 — Annual Instalment $490.80 (Present Option)

(Life expectancy of beneficiary) 30)$10,000.00—proceeds at death

$ 333.33—average amount of proceeds included in each instalment certain

$490.80—amount of guaranteed instalment

Less 333.33—tax exempt proceeds included in 1942 payment

$ 157.47—taxable interest received in 1942

OPTION B—20Years Certain and Continuous. First payment in 1935

Beneficiary Age 50 — Annual Instalment $565.90 (Old Option)

$10.000.00—proceeds at death

Less 1,212.84—aggregate amount of payments 1935 to 1936, inclusive

(Life expectancy of beneficiary) January 1, 1937 19)$ 8,787.16—tax exempt proceeds still to be received

$ 462.48—exemption allowed for 1938 and subsequent instalments

$565.90—amount of guaranteed instalment

462.48—tax exempt proceeds included in 1942 instalment

$103.42—taxable interest received in 1942

7. Q. *How are profits on policies purchased for a valuable consideration affected by Income Tax?*

A. The profits are taxable. If A should insure his life and sell the policy to B instead of surrendering it to the company, B is liable for Income Tax on the profit which he derived from the transaction either during the life of A or at his death. The profit is determined by subtracting from the amount B receives under the contract, the cost of its purchase plus premiums paid by B. *L. 22* (*b*) (*1*); *Reg. 103, Sec. 19.22* (*b*) (*1*)*–1.* This does not apply to a non-taxable transfer of assets between two business concerns. *L. 22* (*b*) (*2*). See Question 37.

8. Q. *How are dividends affected by Income Tax?*

A. "Amounts received as a return of premiums under life insurance, endowment or annuity contracts, and the so-called 'dividend' of a mutual insurance company which may be credited against the current premium, are not subject to tax. L. 22 (*b*) (*2*); *Reg. 103, Sec. 19.22* (*a*)*–12.*" However, if dividends are accumulated the interest credited each year on such accumulations is taxable income when credited. *Letter, T. Mooney, Deputy Com'r to C. C. H., Dec. 13, 1940.*

9. Q. *Are dividend accumulations on life insurance received by the insured when the policy becomes full-paid taxable as income?*

A. Not unless the sum of the accumulated dividends exceeds the premiums paid. The cash surrender value of the full-paid policy remaining in force does not enter into the computation. *S. M. 5680; C. B. V–1, page 32, L. 22* (*b*) (*2*); *Reg. 103, Sec. 19.22* (*b*) (*2*)*–1.* Until the aggregate amount of the dividends exceeds the aggregate premiums paid, the insured is not required to include in gross income the cash dividend received. After the insured has recovered tax free dividends equal to the aggregate premiums paid, the full amount of dividends received is required to be included in gross income. Dividends applied to purchase paid up additional insurance are not required to be included in gross income for Federal Income Tax purposes, except where such dividends exceed the aggregate premiums paid. *Letter from T. Mooney, Deputy Commissioner dated Dec. 13, 1940.*

10. *Q. Are dividend accumulations subject to Income Tax if drawn down before the policy matures or becomes full paid?*

A. No. However, if the policy is subsequently surrendered or matured in a single sum, the accumulations exclusive of interest credited in prior years should be added to the cash received in order to compute the taxable profit. *O. D. 490. C. B. 2, page 85; L. 22 (b) (2); Reg. 103, Sec. 19.22 (b) (2)–1.*

11. *Q. Is interest on dividends accumulated subject to Income Tax?*

A. Yes, in the year credited, where there is no restriction as to the time of payment; in other words, where the policyholder may withdraw at will, the interest credited is taxable in the year credited. If the policyholder does not have the right to withdraw at will, interest is not taxable. Letter to Home Life, Feb. 16, 1943, by T. Mooney, Deputy Com'r., applied in this case to an annuity and endowment payable in instalments.

12. *Q. Are the proceeds of life insurance paid as the result of the death of the insured subject to Income Tax?*

A. No. However, when paid in instalments (for specified years or for life) the principal thereof is exempt but the interest in each instalment payment is taxable income if elected by the beneficiary as an optional mode of settlement. See Question 6. And if the policy has been purchased for valuable consideration the buyer is subject to Income Tax on the profit derived from the transaction, provided the transfer is not of assets from one business to another in a reorganization that is tax free. See Questions 7, 37 and 39. *L. 22* (*b*) (*1*); *Reg. 103, Sec. 19.22* (*b*) (*1*)–*1*.

13. Q. *Is life insurance paid to the insured's estate subject to Income Tax?*

A. No. *L. 22* (*b*) (*1*); *Reg. 103, Sec. 19.22* (*b*) (*1*)–*1*. See Question 12.

14. Q. *Are corporations subject to Income Tax upon the receipt of the proceeds (principal) of life insurance?*

A. No. *L. 22* (*b*) (*1*); *Reg. 103, Sec. 19.22* (*b*) (*1*)–*1*. See Question 37 concerning policies purchased for a valuable consideration and Question 12 for instalments.

15. Q. *How are the recipients of endowments, annuities and life insurance policies given to them by other persons, affected by Income Tax?*

A. In the same manner as if they had personally paid the premiums. That is to say, if given away before maturity, the difference, if any, between the premium or premiums paid by the giver and the amount realized by the receiver is income to the receiver of the gift policy. The premium paid by the giver is not subject to Income Tax, but if it is large enough it will be subject to Gift Tax. *L. 22 (b) (2); Reg. 103, Sec. 19.22 (2)–1.* For Gift Tax see Question 93. In the case of gift annuities or endowments payable in instalments the receiver should include in income 3% of the premium or premiums paid by the giver. By irrevocably designating a beneficiary of the *endowment* payment *before* maturity the result is as follows:

1. Lump sum payment. The profit, or difference described above, is taxable to the receiver or beneficiary.
2. Proceeds retained at interest for first beneficiary for life or term of years (with no right of withdrawal), then proceeds to second beneficiary. Interest income taxable to first beneficiary. Profits taxable to second beneficiary when received as under 1.
3. Proceeds paid in instalments. This

brings policy under rule affecting endowments payable in instalments. *See Question 3. I. T. 2635 C. B. August, 1932, adapted to the present law. See I. T. 3033, December, 1936.*

16. Q. *Is Gift Tax paid on transfer of a life insurance, endowment or annuity contract deductible from gross income in the same manner as real estate and personal property taxes?*

A. No. *L. Sec. 23 (c)–1.* Moreover, an executor cannot deduct such tax (having been paid by decedent during his lifetime) from the income of decedent's estate. Perry vs. Com'r, *32 B. T. A. 513.*

17. Q. *Are corporate dividends paid out of insurance proceeds collected by the corporation taxable in the same manner as other dividends?*

A. Yes. After the insurance is collected, its identity as insurance is lost. While insurance paid by reason of death is not income to the corporation, if it is paid out afterwards as a dividend to stockholders, it is taxable in their hands like any other dividend. *I. T. 2131, C. B. IV–1, page 50,* Cummings vs. Com'r, *73 Fed.* (*2*) *477*. This is also the case where proceeds are paid to trustee to distribute pro rata to stockholders. Golden vs. Com'r, *113 Fed.* (*2*) *590*. And where a corporation insures employee, turning over proceeds at his death to his widow, deducting payment as business expense, the widow is chargeable with tax on income received. Sutro vs. U. S. *Dist. Ct.* (*Calif.*).

18. Q. *Are partnerships subject to Income Tax and Surtax with respect to life insurance paid to them?*

A. No. *L. 22* (*b*) *1. T. B. R. 22, C. B. 1, page 82.* See Question 37 concerning policies purchased for a valuable consideration.

19. Q. *How are annuity payments affected by the Income Tax during their first year?*

A. Where a monthly, semi-annual or quarterly annuity starts after the beginning of the tax year, say June 30th, the amount reportable for that year is proportionally reduced. "Such portion of each installment shall be included in gross income as is equal to 3% of the aggregate premiums paid * * * divided by the number of instalments so payable." *G. C. M. 14593; XIV–16–7437.*

20. Q. *How is an assigned annuity taxable?*

A. If the owner of an annuity divests himself of all rights in it, the income thereafter is taxable to the assignee on the same basis as it was formerly taxable to the annuitant. Siegel, Executor, *20 B. T. A., 563.* See Questions 2, 15, and 19.

21. Q. *How does the Income Tax affect an annuity combined with life insurance* (*P. L. I.*) *in a single contract?*

A. It is a contract for the payment of the interest or earnings on a certain fund and not life insurance or annuity contracts within the meaning of the Revenue Act. The total annual income is taxable. *G. C. M. 21716.* The former ruling *G. C. M. 6395,* more favorable to the taxpayer, was revoked.

22. Q. *Are disability annuity payments subject to Income Tax?*

A. No. Sums received under total and permanent disability benefits may be considered health insurance and are entirely exempt from Income Tax. *L. 22* (*b*) *5.* Also pensions and annuities for personal injuries or sickness resulting from active service in armed forces of any country. *L. 22* (*b*) *5.*

23. *Q. Is interest from policy proceeds subject to Income Tax?*

A. Yes. *L. 22* (*b*) (*1*)–*1*. Formerly, interest income on proceeds left with the company at the direction of the insured was exempt, but this was amended by the Revenue Act of 1926 and subsequent laws.

MATURED ENDOWMENTS

26. *Q. How are matured endowments payable in one sum affected by the Income Tax?*

A. The profit is taxable. This is the difference between the amount received plus dividends and the total premiums paid. If dividends were used to reduce premiums, count the net premiums paid as the cost. If dividends were accumulated, count the dividend accumulations (exclusive of interest) in the amount received. *Reg. 103, Sec. 19.22* (*b*) (*2*)–*1*. If the result shows no profit nothing is reportable. Losses are not deductible.* There is some ground for the belief that no profit is derived even though installment option is not elected until maturity,

* Policies taken before March 1, 1913, may be computed by a different method excluding all accumulations prior to that date.

but of course, before acceptance of the check. There is no ruling on this point. This is true even though there is an option in the policy to take cash. *G. C. M. 22519–1941.*
The profit at maturity of War Risk Insurance endowment is not taxable as income. *I. T. 3294–1939.* See Question 29 for endowments paid in instalments.

27. Q. *Is a matured endowment policy or the cash surrender of a life insurance, endowment or annuity contract entitled to the benefits of the capital gain or loss provision of the Income Tax law?*

A. No. *I. T. 2661. C. B. Dec. 1932, p. 39,* Hellman vs. Com'r, *33 B. T. A. 901, G. C. M. 18233; XVI–21–8717;* Cobbs vs. vs. Com'r, *111 Fed.* (2) *644;* Avery vs. Com'r, *113 Fed.* (2) *933.*
The answer is also "no" for a combined annuity and life insurance contract because its surrender is not a sale or exchange of a capital asset within the law. Bodine vs. Com'r, *103 Fed.* (2) *982.* This rule does not apply to an employees' trust maturity. *L. 165* (*b*).

28. Q. *If the policyholder elects to leave the proceeds of a maturing endowment with*

company at interest, how is the transaction taxed?

A. The contract has matured and the policyholder is entitled to his money. His profit from the transaction is subject to Income Tax according to the method of calculation described in Question 26. Interest income from the deposit of the proceeds with the company is subject to Income Tax in its entirety if insured has right of withdrawal, whether election is made before or after maturity. *I. T. 2380 C. B. VI.—2, page 32.* See Questions 15 and 29.

29. *Q. If proceeds are payable in instalments how does law apply?*

A. Where endowment calls for payment of proceeds in instalments at maturity, or is put on that basis *before* maturity, the contract is treated as an annuity and the policyholder reports 3% of the aggregate premiums paid as taxable income, the remainder of the instalment being exempt until he has received back what he paid for the contract. *G. C. M. 21666.* Might apply even to elections after maturity but, of course, before deposit of check.

30. *Q. Where matured endowment proceeds are left with the company under interest to*

the insured for life, then to his wife, then to the wife's estate, what tax obligations are incident to the transaction?

A. The policyholder should report as income the profit on the endowment at maturity as if the money were received. He is then held to have purchased an annuity with the matured value and should report 3% of the matured value as taxable income. If he should die his wife will report likewise until the total exempt income received by both exceeds the cost of the annuity, at which time the entire annual income is taxable. *I. T. 3033, Dec. 1936.* The rule holds even if there is an option in the policy to take cash. *G. C. M. 22519–1941.*

31. Q. *When an endowment policy is surrendered* BEFORE *maturity and the cash value is accepted in instalments over a period of years, not involving a life beneficiary, is the pay off an annuity?*

A. No. It is a return of capital. The rule that requires 3% of the cost to be included in income is not applicable. There is no tax until the aggregate sum received exceeds the cost of the contract. Thornly vs. Com'r, *2 T. C. 31.*

32. *Q. Is there taxable income when one policy is exchanged for another?*

A. Yes, probably under certain circumstances. If the new policy has a cash surrender value exceeding the net cost of the old one, the result is a taxable profit for the year the exchange takes place. Should the taxpayer receive a cash payment in addition, of course such payment ought to be computed in the profit. If the new policy has *no* cash surrender value and there is no cash payment received, or if the new policy has no cash value and the cash payment is less than the net cost of the old policy, no taxable income results. *S. O. 55, C. B. 3, page 54.*

33. *Q. How are cash surrenders affected by the Income Tax?*

A. The profit is taxable. See Question 71 if an employees' trust. This is the difference between the amount received plus dividends and the total premiums paid. If dividends were used to reduce premiums, count the net premiums paid as the cost. If dividends were accumulated, count the dividend accumulations exclusive of interest credited in prior years in the amount received. *Reg. 103, Sec. 19.22 (b) (2)–1.* If the result shows no profit nothing is reportable. Losses are not deductible.* See Question 4.

34. Q. *Is loss deductible from gross income when insurance policies are surrendered or transferred for less than the premiums paid?*

A. No. A loss was so decided to be deductible as a business expense. Forbes Lithograph Manufacturing Co. vs. White, *42 Fed. (2) 287.* After appeal the case was settled by compromise, taxpayer not contesting Revenue Bureau's denial of deduction and Revenue Bureau yielding on another matter involved. Subsequently, it was decided loss is not deductible and this should be considered the present rule. Century Wood Company vs. Com'r, *69 Fed. (2) 967*; London Shoe Co. vs. Com'r, *80 Fed. (2) 230.*
Neither is loss deductible if insurance company becomes insolvent. Morse vs. Com'r, *37 B. T. A. 399.*

35. Q. *If loss is sustained in the surrender of an annuity is such loss deductible from gross income?*

A. Yes. A contract for an annuity is not a contract for insurance and the price paid

* Policies taken before March 1, 1913, may be computed by a different method excluding all accumulations prior to that date.

for annuities is not a premium paid for an insurance policy. Where the annuitant is convinced that the investment is not a wise one and forfeits not only the amount theretofore paid, but all future rights under the contract, the loss in the year of forfeiture is an allowable deduction. Cohan vs. Com'r, *11 B. T. A. 743*. Where the taxpayer loses money through the ownership of an annuity on the life of another person, such loss is not deductible from gross income. Helvering vs. Louis, *77 Fed. (2) 386*. Also, no deduction is allowed a decedent's estate if he lost money on an annuity which ceased at his death. *I. T. 2915; XIV–34–7661*. Industrial Truts Co. vs. Broderick, *94 Fed. (2) 927*.

TRANSFERS

37. Q. *How are life insurance payments affected by Income Tax if purchased for a valuable consideration?*

A. When life insurance policies are assigned and purchased for a valuable consideration, an amount equal to the purchase price, together with subsequent premiums, if any, paid by the purchaser, is exempt from tax, but any amount over and above this received by the purchaser is taxable income to him. *I. T. 2591 C. B. X.–2, page 123.*

It is possible this rule also would be applied when insurance is assigned to liquidate a debt if the creditor collects a sum greater than the debt, interest due, and premiums, if any, paid by him. Where, however the consideration is greater than the proceeds there is no taxable income. Lambeth vs. Com'r, *38 B. T. A. 351.*

The plain intent of the law is to tax as income profit arising from a life insurance contract which inures to a person other than the insured who has obtained that contract through a commercial sale or transfer thereof. See Questions 38, 39 and 53. *L. 22 (b) (2) (A)–3.*

38. Q. *What is the meaning of the term "valuable consideration?"*

A. The term "valuable consideration" is intended to describe a commercial transaction in which fair value is given and received. There is a difference between "valuable consideration" and "good consideration." A *good* consideration is one that is recognized by the courts as binding. Transfers in consideration of one dollar, or for love and affection are recognized as *good* and sufficient at law, but they are not recognized as *valuable.*

For instance, where the President of a corporation applies for insurance, payable to his estate, and immediately assigns it to the corporation, which pays the first and subsequent premiums, it is not a transfer for a valuable consideration. *Letter to H. R. Limberg from J. C. Wilmer, Deputy Commissioner, dated April 30, 1931.*

39. Q. *Has the tax on a transfer for valuable consideration ever been enforced?*

A. Yes. A and B were partners. A insured B, taking absolute title to the policy. B insured A, doing likewise. B died. B's executors sold the policy on A's life to the firm. The firm continued to pay the premiums. Upon A's death, the firm, as transferee, was entitled to Income Tax exemption of only the actual value of the consideration paid for the policy and the subsequent premiums. The difference between these sums and the amount received was subject to Income Tax. *I. T. 2591 C. B. X–2, page 123.*

But where there is a transfer of assets including life insurance from one business to another in a reorganization that is free of tax, the life insurance will retain the same status it held in the hands of the original holder. If it was exempt it will continue to be exempt even though transferred for consideration. *L.22 (b) (2).* This rule is applicable to any transfer after Dec. 31, 1940. Prior to that time all transfers for a valuable consideration were taxable.

Where corporation acquires policy from predecessor, said predecessor's liability determines transferee's liability. Thus X Co. to Y Co. in a tax free organization, no tax on proceeds. But X Co. to Y Co. for valuable consideration and not in a tax free reorganization then Y Co. to Z Co. in a tax free reorganization, the proceeds are taxable at death for difference between amount received and cost of policy. *T. D. 5271. Amending Section 19.22 (b) (2) (A)–3.*

Insured assigned all right, title and interest in the policy to his wife in consideration of her paying him the cash value. Thereafter the wife paid the premiums. Later she assigned the policy to her daughter for "natural love and affection," reserving the right to revoke. When the insured died it was held that the excess of proceeds received over the amount paid for the policy constitutes taxable income to the daughter. The second transfer for love and affection did not cure the transfer for valuable con-

sideration in the first instance. Hacker vs. Com'r, *36 B. T. A. 659.*
However, where insured purchased from his employer a policy on his (the insured's) life it is not considered to be a transfer for valuable consideration. *I. T. 3212—1938.* This ruling is more arbitrary than logical.

PREMIUM DEDUCTIONS

40. Q. *Are premiums paid on life insurance policies deductible from gross income?*

A. Generally speaking, no. *Reg. 103, Sec. 19.24–1 and 24–3.* (See Question 41 for exceptions to rule.)

41. Q. *What premiums paid for life insurance are deductible from gross income?*

A. In the following cases, premiums may be deducted from gross income under the heading "Business Expense," but proof may be required to sustain the deduction.
1. Premiums paid on group insurance. *Reg. 103, Sec. 19.22 (a)–3.* Also health insurance. Mooney, Deputy Com'r., 8/26/43. But not if employer has any pecuniary interest in the policy. *G. C. M. 7997. C. B. IX–1, p. 210,* Merrimac Hat Corporation, *29 B. T. A. 690.*
2. Premiums paid by employer and taxpayer on individual policies of reasonable

amounts on officers or employees where the taxpayer retains no direct or indirect beneficial interest therein. *Reg. 103, Sec. 19.24–3.* But where employer names itself as beneficiary, even though it agrees to pay proceeds to beneficiary named by employee (if employee continues in service) the premiums are *not* deductible. Omaha Elevator Co., *6 B. T. A. 817.* See Questions 43 and 47.

3. Premiums paid by a corporation upon insurance taken out by the corporation on the life of the guarantor of a debt to the corporation. *O. D. 1109; C. B. 5, page 177.*

4. Premiums paid by an individual of technical ability who is associated in partnership with another person or persons, providing financial support to the business, where the former, in order to secure said support, must insure his life in favor of the latter. This deduction is not available where the proceeds are intended to be used directly or indirectly for the satisfaction of contracts or other pecuniary obligations of the premium payer. *I. T. 1340, C. B., I–1, page 119.*

5. Premiums paid by a creditor where the debt is ascertained to be uncollectible and the cash surrender value is less than the

debt, although the face value may exceed the amount of the debt. Dominion National Bank vs. Com'r, *26 B. T. A. 421; G. C. M. 14375.* See Question 56.

6. Premiums paid by an individual for life insurance to be distributed as a charitable gift, but the policy should be out of insured's control and premium, together with other contributions of similar nature, must not exceed limit prescribed by law. See Question 46.

7. Waiver of premium, disability annuity and double indemnity premiums attached to a life insurance policy are not at present considered deductible as accident and health insurance. *Letter, Norman D. Cann, Acting Com'r, dated Apr. 5, 1943.* There is some confusion on this question and no doubt there will be later rulings.

42. Q. *Are insurance premiums paid in advance deductible?*

A. If deductible at all, only a pro rata deduction for the current year may be taken. *G. C. M. 23587.*

This question has been answered differently in past years. The present rule was first in effect, and then deduction was allowed for total sum paid in the year paid. *G. C. M. 13148,* which is now revoked. However, if total deduction has been taken in past, taxpayer may not deduct again proportions of same premiums. These rulings related to fire insurance. The question is placed here to show possible attitude of Revenue Bureau toward a life insurance premium paid in advance if it falls in class of deductible items.

43. Q. *Suppose a corporation, partnership, or individual engaged in business were to take out an individual policy on the life of an officer or employee, paying the premiums on the policy and retaining no beneficial interest therein, would the premiums be income to the employee?*

A. Yes. That is in the nature of additional compensation. The premiums paid for the employee would be income to the employee. *O. D. 627, C. B. 3, p. 104.* Geo. M. Adams, *18 B. T. A. 381*; N. L. Danforth, *18 B. T. A. 1221; G. C. M. 8432,* C. B. Dec. 1930, *p. 114.* Old Colony Trust Co. vs. Com'r, *279 U. S. 716.* Com'r vs. Bonwit, *87 Fed.* (2) *764.* See Questions 41–(2) and 47.

44. Q. *Are premiums paid by an employer on group insurance for his employees a part of the employee's income for Income Tax purposes?*

A. No. *Reg. 103, Sec. 19.22* (*a*)*–3.* Nor are they wages upon which Social Security Tax is levied. *S. S. T. 273*. Also includes health insurance. Mooney, Deputy Com'r., 8/26/43.

45. *Q. Are contributions made by an employer toward the purchase of retirement annuity contracts for the benefit of his employees used in computing taxable income of the employees?*

A. No. *I. T. 2891 XIV–19–7478*. When the annuity becomes payable to the employee he will report 3% of the amount contributed *by him*. This fulfills the terms of *Section 22 (b) (2)* of the law taxing annuity receipts. But employee should report as taxable income any part of the premium paid by employer which is allocated to life insurance protection for the employee or his beneficiaries. *I. T. 3268. C. B. 1939–1*. See Questions 69 and 70.

46. *Q. Are premiums on insurance for the benefit of religious, charitable, scientific and educational corporations deductible from gross income of an individual?*

A. Yes, provided:

1. The corporations are such as described by the law.
2. The beneficiary cannot be changed at the option of the insured.

3. The premiums, together with other charitable gifts, do not exceed 15% of taxpayer's net income. *O. D. 299, C. B. 1, page 151*; M. C. Adler, *5 B. T. A. 1063*. Hunton vs. Com'r, *1 T. C. 821*. Where, however, policy was assigned to a charity as security for a promissory note payable at death, the premiums were *not* deductible. The reason is evident that insured might take up the note at any time before maturity, after having obtained the benefit of the premium deductions. *I. T. 1453, C. B. I–2, page 144*.

Premiums are also deductible if the policy is irrevocably assigned to a trustee for the benefit of religious, charitable, scientific and educational corporations. E. R. Behrend, *23 B. T. A. 1037*.

47. Q. *If the lives of officers owning the stock of a corporation are insured, and the policies are made payable to their respective wives, the corporation paying the premiums, is this expense an allowable deduction?*

A. Where the ownership of the corporation, the authorization of payment of premiums and the naming of the beneficiaries rest in the same parties, and it does not appear that payment of premiums would increase the efficiency of such officers, they are not deductible as an ordinary and necessary business expense. *I. T. 2279, C. B. V–1, page 67.* Premiums so paid would be a taxable distribution to stockholders if stockholders were beneficiaries in proportion to their holdings. *O. D. 659; 3 C. B. 182.* Where certain corporations of which petitioner owned all the capital stock, paid premiums on insurance in which he was permitted to name his wife and children as beneficiaries, the corporations receiving no benefit from the policies, the petitioner received a benefit from the payments and they were taxable income to him. Yuengling vs. Com'r, *69 Fed.* (2) *971.* Canaday vs. Com'r, *76 Fed.* (2) *303.* See Question 17.

48. Q. *Are premiums on corporation life insurance deductible if stockholders are made beneficiaries thereof?*

A. No. The corporation itself is indirectly a beneficiary under such a policy. Moreover, premiums so paid are a charge against surplus and represent dividends to the stockholders subject to surtax (also normal tax as a result of a change in the law) to the extent that such premiums are paid out of earnings or surplus accumulated since 1913. *O. D. 659; C. B. 3, page 192.*

49. *Q. Are premiums on corporation life insurance deductible by a stockholder as business expense if he paid them out of his own pocket?*

A. No. Cappon vs. Com'r, *28 B. T. A. 357.*

50. *Q. What is the effect on corporation insurance of the Excess Profits Tax in the Revenue Act of 1940?*

A. 1. As premiums on business insurance payable to the business are not deductible as an expense from gross income, *L. Sec. 24 a* (4), it follows that so much of the corporations gross income which is used to pay life insurance premiums would be included in the amount subject to Excess Profits Tax—as well as normal tax.

2. There would be no Excess Profits Tax on the annual increase in cash value, but there would be a Capital Stock Tax payable on the value of the capital stock, in which the cash value life insurance policies would be included.

3. There would be no tax on the proceeds of life insurance collected at death, because such proceeds do not constitute gross income to the corporation, *L. Sec.*

22 b (1). See Question 37 for transfer for value.

DEBTOR—CREDITOR

53. Q. *Are creditors subject to Income Tax on the proceeds of insurance on the life of the debtor?*

A. Not if there is a loss. Yes, if there is a profit and the policy is assigned or transferred. Such a transaction is for a valuable consideration. See Question 37. But where creditor, which in this case happened to be the employer, was named as beneficiary and there was no transfer of policy, the proceeds paid at death were exempt even though employer had charged off the debt as a bad debt. Durr Drug Co. vs. U. S., *99 Fed. (2) 757.*

54. Q. *If there is a loan against debtor-creditor insurance and the creditor pays interest, is it deductible?*

A. Yes. The creditor may deduct interest. *A. R. R. 7895, C. B. III–2, page 114. L. 23 (b)*. See Question 59. For deductions of premiums paid, see Question 56.

55. Q. *Are premiums paid by the insured debtor on policies in favor of his creditor deductible from taxable income?*

A. No. Since death will pay off the obligation for which the insured's estate is liable, the insured is indirectly a beneficiary under the policy. For that reason premiums paid are not deductible. *L. 24* (*a*) (*4*); Rieck vs. Heiner, *25 Fed.* (*2*) *453*. Decision the same even though right to change beneficiary not reserved. Klein vs. Com'r, *84 Fed.* (*2*) *310*.

56. Q. *Are premiums paid by the creditor on a life insurance policy assigned to him by the debtor, deductible as business expense?*

A. Whether a creditor to whom a debtor has assigned an insurance policy as security for a debt is entitled to deduct in the year of payment amounts paid by the creditor as current premiums on the policy, depends upon two factors (1) whether the creditor has a right of reimbursement therefor, and (2) if so, whether such right is worthless.

Such right may rest upon the express contract of the assignor-debtor or it may arise by implication. The express contract may be an agreement to reimburse the creditor at all events regardless of the amount collected from the policy, or it may be merely an express agreement that the

assignee may reimburse himself out of the proceeds of the policy. *G. C. M. 14375.*
Cadwalader's Executors, *15 B. T. A. 1.* But interest paid on a policy loan may be deducted. See Questions 41–5 and 54.

57. Q. *Are premiums paid by the creditor's estate chargeable as income to the creditor's legatee?*

A. No. Where premiums on debtor-creditor insurance are continued by the creditor's estate, said premiums may be deducted from the income of the legatee of the estate and said legatee cannot be charged with the premiums paid as if they were his share of the income from the estate Cadwalader vs. Com'r, *27 B. T. A. 1078.*

58. Q. *Are bad debts deductible when protected by life insurance assigned by the debtor as collateral?*

A. Yes. Where policies of life insurance assigned by a debtor to his creditor have a greater face value, but a lower cash surrender value than the amount of the debt, and the debt has been ascertained to be uncollectible, the creditor may charge off the difference between the amount of the debt and the cash surrender value of the policies, even though he continues to hold the policies. Dominion National Bank vs. Com'r, *26 B. T. A. 421.* If the life insurance is on the term plan and has no cash surrender value, the entire debt may be deducted. Northern National Bank, *16 B. T. A. 608.*

59. Q. *Is interest paid to a life insurance company on loans upon a policy deductible from gross income?*

A. Yes. *L. 23* (*b*). *Reg. 103, Sec. 19.23* (*b*)*–1.* But not if charged against policy reserve and taxpayer reports on cash basis, because this is held to be an accrual. Alsberg vs. Com'r, *42 B. T. A. 61;* Prime vs. Com'r, *39 B. T. A. 487*; Mass. Mutual vs. U. S., *288 U. S. 269.*

Also interest is not deductible if paid or accrued on indebtedness created to buy single premium life or endowment contracts. Any contract calling for premiums of four years or less is deemed to be single premium. *L. 24* (*a*) (*6*).

But where policy converted from ordinary life to 15 payment life and 6% interest charged on difference in premiums, said interest is not deductible, the transaction not having the elements of a debt. Fleisher vs. Com'r, *Memo T. C. April 26, 1943.*

60. *Q. Can the United States subject policy values to a claim for tax due by insured?*

A. No, not in a direct suit against the insurance company to compel it to turn over cash value, even though the insured has the right to change the beneficiary. U. S. vs. Mass. Mutual, *127 Fed.* (*2*) *880*; U. S. vs. Penn Mutual, *130 Fed.* (*2*) *495*. But there is a possibility the Government might be successful in a suit in equity joining the insured, company and beneficiary.

61. *Q. Are annuity contract values subject to distraint by the United States for taxes due by the annuitant?*

A. Yes. Cannon vs. Nicholas, *80 Fed.* (*2*) *934*. See Question 60 regarding life insurance. Decisions there quoted may affect answer here given in future.

LIFE INSURANCE TRUSTS

62. *Q. How is the income from a funded life insurance trust taxable?*

A. Where any part of such a trust is or may be applied to the payment of premiums upon policies of insurance upon the life of the *grantor* (the original owner of the trust property) such premiums shall be included in computing the net income of the grantor. *L. 167* (*a*) (*3*). *Reg. 103,* *Sec. 167–1;* Burnet vs. Wells, *289 U. S. 670; 53 S. Ct. 761.* This holds, even though the trust is irrevocable. duPont vs. Com'r, *289 U. S. 685*; also if the policy is an endowment, Heffelfinger vs. Com'r, *87 Fed* (2) *991.* The only exception is in the case of a trust created for a charitable purpose.

If evidence indicates that establishing trust, transfer of policies and payment thereafter of premiums by wife at suggestion of husband are part of same transaction, income is taxable to husband even though there is no obligation on wife or trustee to pay premiums. *G. C. M. 20070; 1938.*

And where the wife transfers corporate shares irrevocably to a trust of which she is one of the beneficiaries, directing the payment of premiums on *her husband's* life insurance also held by the trust the income might be taxable to her. Helvering vs. Blumenthal, *56 S. Ct.; 305, 296 U. S. 552;* Com'r vs. Morton, *108 Fed.* (2) *1005,* both reversing lower court decisions. In the Morton case the court said, "Nor are the provisions of the statutes defining instances in which the grantor remains taxable, as in the case of certain reservations for his benefit or provisions for the payment of premiums upon

policies of insurance on his life, to be regarded as excluding instances not specified, where in contemplation of law the income remains in substance that of grantor. No such exclusion is expressed and we see no ground for implying it."
Likewise, trust income is taxable to wife where she creates it to pay premiums upon insurance taken out by her on his life to pay her share of estate taxes on his estate with any residue reverting to her. Phipps vs. Helvering, *124 Fed. (2) 288;* Grantor not taxable where beneficiary of trust voluntarily pays premiums. Memo T. C. Lewis Barker.
And where the insurance trust is created by the wife for her husband and their children and in default of these to a charity foundation, there being no possibility of reversion to the wife, she is not taxable for the trust income. Com'r vs. Jergens, *127 Fed. (2) 973.*
And even though wife created trust for paying premiums on husband's life, the proceeds at death being payable to another trust, income of which is payable to wife, it was ruled wife is not taxable on income. Com'r vs. Willson, *44 B. T. A. 583.* Morton, Phipps and Higgins cases distinguished.
See footnote to Question 91.

63. Q. *Is there any preference in taxation between the interest income from life insurance proceeds left with life insurance companies and life insurance trusts administered by trust companies?*

A. No. See Question 6 for interest in installments.

EMPLOYEES' TRUSTS *

65. Q. *What is an employees' trust?*

A. In general, the type of trust described as exempt under *Section 165.* It may be a stock bonus, pension or profit-sharing plan but it should be for the exclusive benefit of employees or their beneficiaries. It should be permanent rather than temporary, non-discriminatory and not a device for distributing profits to shareholders nor a fund that could be diverted by the employer to other purposes. *Reg. 103, Sec. 19.165 (a) (1)—1. T. D. 5278.*

66. Q. *May annuities, life insurance or a combination of both be the media of an employees' trust?*

A. Yes, employees' trusts can depend on contracts of life insurance companies because they are actuarily sound. These may be

* This section devoted to Employees' Trusts does not cover the subject in detail.

group or individual policies—annuities, life insurance or a combination of both.

67. Q. *Are contributions made by the employer deductible as business expense?*

A. Yes, if the plan or plans (there may be more than one) qualify for tax exemption by meeting the following requirements:

1. Employer's contribution cannot be diverted to purposes other than for employees and their beneficiaries, prior to satisfaction of all liabilities to them. *Reg. 103, Sec. 19.165* (*a*) (*2*). *T. D. 5278.*
2. 70% of the employees must be eligible to participate and 80% (presumably in the case of contributory plans) of such employees must participate. Employees up to and including five years' service and part-timers (less than 20 hours a week and five months a year) need not be counted. *L. 165* (*a*), *Reg. 103, Sec. 19.165* (*a*) (*3*). *T. D. 5278.*

But if the plan does not meet these requirements it may be tax exempt if it does not discriminate in favor of officers, stockholders, highly paid employees or those with supervisory duties. It is not discrimination if every employee in the plan gets a uniform percentage of his average annual salary in certain years; or if the plan applies only to salaried or clerical employees or those earning over $3,000, the Federal Social Security salary limit, or for the sum their salaries exceed $3,000. *L. 165 (a) (5), Reg. 103, Sec. 19.165 (a) (3). T. D. 5278.*

68. Q. *Are premiums deducted by the employer to be included in employee's income?*

A. Not if he gets nothing of readily realizable value in the pension or annuity. The purpose of the trust is to place the policies in the hands of a trustee (or custodian) with instructions of what to do when the employee dies, leaves or completes his term of service.h If the plan qualifies the employee need report no income until he receives the pension. *Reg. 103, Sec. 19.22 (b) (2) (B)–1.*

Any sum paid for life insurance by employer is includible in employee's income. In a policy consisting of both life insurance and annuity the cost of the insurance is the one year term premium. If the company does not issue such a policy then it may be computed using the same mortality table, interest and loading. *Sec. 19.165 (b) 19.23 (p) (1) (A)–1. T. D. 5278.*

69. Q. *How is employee taxed when he receives his annuity pension?*

A. As if he had bought an annuity. The employee's contribution will be considered as his payment for the pension. He will include 3% of his total payments in his gross income until the total exempt income received by him equals his total contributions, and from then on report all pension received in gross income. *L. 22 (b) (2), L. 165 (b). Reg. 103, Sec. 19.165 (b). T. D. 5278.* If employee contributes nothing he includes *all* his pension from beginning.

70. Q. *If the annuity does not qualify under employees' trust, how is it taxable?*

A. The employer's contribution is deductible if it can be justified as a legitimate business expense, but it is taxed in the employee's income in the year the contribution is made. *L. 165 (c); Reg. 103, Sec. 19.165 (c); 19.22 (b) (2) (B)–1, 19.23 (p) (1)–1. T. D. 5278.*
But care should be exercised that it does not violate the Salary-Wage Freeze Regulations.

71. Q. *If the employee leaves service before maturity of the pension plan, what happens?*

A. If contributions are made available to the employee within year of leaving service, the amount he receives in excess of his own contribution shall be considered a gain from sale or exchange of a capital asset held more than six months. *L. 105 (b)*.

72. Q. *Suppose employee dies and beneficiary receives death benefit, what is result?*

A. If a lump sum, it is taxable as income to the extent it exceeded employee's contributions. If paid as an annuity, it is taxable as an annuity as it would have been taxable in hands of employee if he had lived; viz., 3% of employee's contributions includible as income until exempt income equals contributions, thereafter all annuity is taxable. *Reg. 103, Sec. 19.22 (b) (2) (B)–1. T. D. 5278.* See Question 111 for Estate Tax.

73. Q. *Is an employee's trust, such as described, taxable on its income?*

A. No. *L. 165 (a)*.

74. Q. *Need the employer create a trust to get deductions of contributions?*

A. No. Any annuity plan which meets the requirements of an employee's trust is entitled to tax deductions. *L. 23 (p) (1)*.

Also applies to stock bonus and profit-sharing plans. *Reg. 103, Sec. 19.23 (p) (1)–1.*

75. Q. *What is the limitation on contributions to pension trusts and pension plans which may be deducted by employer?*

A. 5% of pay of employees in plan, subject to review by Commissioner at five year intervals. May be reduced if found to be more than necessary to provide reasonable retirement income based on past and current service. *L. 23 (p) (A) (i); Reg. 103, Sec. 19.23 (p) (1) (A)–2.*

If 5% is not enough to cover both past and current service pension credits, the employer may, with Commissioner's consent contribute and deduct in excess of 5% on a level contribution or percentage of pay plan over future years if actuarially sound; but not if more than 50% of extra contribution applies to any three employees. As to them, contributions must be spread over at least five years. *L. 23 (p) (ii); Reg. 103, Sec. 19.25 (p) (1) (A)–3.*

If employer wishes to cover separately past service pension credits he may contribute and deduct for them, but not at the rate of over 10% of the cost per year until all past service has been covered. In the meantime he may contribute and deduct the normal cost of present service. This also requires the Commissioner's approval. *L. 23 (p) (iii)*; *Reg. 103, Sec. 19.23 (p) (1) (A)–4.*

If employer pays in more than he is allowed to deduct in any year, the amount disallowed may be credited as a contribution in succeeding years. *L. 23 (p) (iv)*; *Reg. 103, 19.23 (p) (1) (A)–5.*

Note: However, total deductions in succeeding years may not exceed limitations of the preceding paragraphs.

76. Q. *Is a deferred annuity without cash value, purchased by an employer for an employee, subject to Income Tax?*

A. No income is realized by the employee upon delivery of the contract to him, for he gets nothing but a promise to pay. The annuity income is taxable when he gets it. It is the receipt of something of readily realizable value which creates tax liability. *I. T. 1810; C. B. II–2, page 70.*

However, where annuity is bought by employer at employee's suggestion, purchase

N.B.—While these rulings are prior to the present law they are deemed important to show the theory upon which the law is based.

price of contract is taxable as compensation to employee. Deupree vs. Com'r, *1 T. C. 113.* This follows even though the employee has no option but to accept the annuity contract. Brodie vs. Com'r, *1 T. C. 275.*

77. Q. *Are annuity premiums paid by an employer on behalf of an employee taxable income to the employee?*

A. Not if the plan qualifies as a pension trust under Revenue Act of 1942. If it does not so qualify the employee is taxable on premiums paid on his behalf as if he had received additional wages. *L. 165* (*c*).

78. Q. *How are pension annuities purchased from a life insurance company taxed as income to the annuitant?*

A. Where the employee has contributed a portion of the premiums paid, he should report as gross income 3% of the consideration paid by him, the employee, until his total tax exempt income equals his total contribution, after which time all the pension annuity is taxable. *L. 22* (*b*) (*2*) *165* (*b*).

(Straight pensions granted without consideration moving to grantor other than past services, are not regarded as annuities. Such pensions are treated as compensation for past services and the entire amount should be included in gross income. *G. C. M. 14593; C. B. 1935.*)

VICTORY TAX

80. Q. *What is the Victory Tax?*

A. An extra levy of 5% on Victory Tax gross income. The deductions except for business expense, are much more restricted than under regular Income Tax. A specific exemption of $624 is permitted to each individual. In the case of husband and wife, they each get $624 exemption only if both have incomes in excess of that amount and they each file separate Income Tax returns. The husband cannot take part of his wife's unused exemption to increase his own. *L. 450, 451.*

81. Q. *How does Victory Tax affect life insurance?*

A. There is a credit deductible from the tax for premiums on life insurance in force September 1, 1942, on the life of the taxpayer, his spouse or any dependent. *L. 453 (a) (1).* The amount of *all* credits (there are others beside life insurance premiums) must not exceed the amount of post war credit or refund. *L. 453 (b).*

82. *Q. Can you get credit for renewals or conversions?*

A. Yes, but *only* for the amount of the premium on September 1. It's the premium on that date that counts.

83. *Q. Can you date back a conversion prior to September 1 and get credit for the increased premium?*

A. We doubt it.

84. *Q. Are annuity premiums also allowed credit?*

A. No. The law names only life insurance premiums. *L. 453* (*a*) (*1*).

85. *Q. Are endowment premiums allowed credit?*

A. We believe so, if the policy provides for enough premium payments to make it life insurance protection.

GIFT TAX *

90. *Q. Are gift endowments, annuities, and life insurance policies subject to Gift Tax?*

A. Yes, if the value of the gift exceeds the exemption in the law. *Reg. 79, Art. 2.*

* The following states now have gift taxes: California, Colorado, Louisiana, Minnesota, North Carolina, Oregon, Tennessee, Virginia and Wisconsin.

91. Q. *What are the exemptions under the Gift Tax law?*

A. There are two exemptions. The first is a specific exclusion of $3,000 per year per person in the case of present interests as distinguished from gifts of future interest. A future interest is one that is limited to commence in use and enjoyment at some future date.

The $3,000 exclusions (denied by the Revenue Act of 1939 for gifts in trust) are again permitted by the Revenue Act of 1942 for gifts in trust† provided they are present gifts and not gifts of a future interest, i.e., provided the trust beneficiaries enter into immediate enjoyment of the trust benefits.

Where a gift of a present interest is made in trust, the $3,000 exclusions are now permitted for each beneficiary. Com'r vs. Hutchings, *312 U. S. 393.*

The second exemption is a general exemption of $30,000 which may be consumed by one gift or by a number of gifts made either contemporaneously or over

† Taxpayer who created an irrevocable life insurance trust is not chargeable with Gift Tax on the premiums, on the theory he has in effect reserved in himself a life estate in the income to pay the premiums. Beck vs. Com'r, *43 B.T.A. 147.*

But allowance of specific exclusion was denied where payment of premiums on life insurance held in trust created suspicion of a future interest. Com'r vs. Boeing, *123 Fed. (2) 86.*

a period of years. This is not an annual exemption. Once the $30,000 general exemption is consumed it cannot be used again during the lifetime of the donor and as long as the Gift Tax is in force. See Question 92 for gifts in trust.

92. Q. *Is the gift of a life insurance premium denied $3,000 exclusion as constituting a gift of a future interest?*

A. No, provided the premium is paid on a policy owned outright by donee.

However, a premium paid under a policy held in trust is a gift of a future interest if the trustee must await maturity before making distribution under the policy to the beneficiaries as the interest of the beneficiaries constitutes a future interest. Ryerson vs. United States, *312 U. S. 405*. Also in case of annuity where policy contains restrictions. Roberts vs. Com'r. *2 T. C.* —.

93. Q. *Is the naming of a beneficiary in a life insurance contract or its assignment a gift?*

A. Yes, if the contract is irrevocably assigned, or a beneficiary is named without retaining any of the legal incidents of ownership. *Reg. 79, Art. 2.* It is also indicated by *Reg. 79, Art. 19,* that gifts of annuities and endowments are affected in the same manner.

If the policy contains a reversion to the insured should the beneficiary die first there is no gift. McLean vs. Com'r, *41 B. T. A. 565.*

94. Q. *Are premiums paid by the giver on gift policies taxable?*

A. Yes, if the premium exceeds the exemption. Where premiums are paid by a person who has transferred the legal incidents of ownership, each payment is a gift. See Question 92. *Reg. 79, Art. 2.*

95. Q. *How is the value of a gift of an insurance policy determined?*

A. Lower court cases, all of which involved single premium policies, hold that it is the net cash value or present worth adjusted to the date of the gift. Helvering vs. Cronin, *106 Fed. (2) 907;* Haines vs. Com'r, *104 Fed. (2) 854.* Also other memo. B. T. A. opinions. This cannot be reconciled with *Reg. 79, Art. 19 (9)* which indicates the value of the gift is the single premium that would be charged by the company. *G. C. M. 13147.* The regulations were upheld in Ryerson vs. U. S. *312 U. S. 405.*

The Regulations indicate that the value of an annual premium policy is the reserve adjusted to the date of the gift plus the cost of the insurance protection from that date to the next premium due date. If a *single* premium policy is bought and shortly thereafter transferred as a gift, the value of the gift is the premium paid, not the cash surrender value. Powers vs. Com'r. *312 U. S. 259.*

Where two annual premiums have been paid on an ordinary life policy, hence no cash value, the value is the cost of duplicating the policies. Phipps vs. Com'r, *43 B. T. A. 790.*

If the gift is made some time after the date of the contract and no comparable policies are obtainable at the time the gift is made, the interpolated terminal reserve may be used as a measure of the gift. *Reg. 79, Art. 19 (9).*

Community Property: Under Texas decisions payment of premium out of community property gives wife no vested interest in policy. Hence, full transfer of policy to her is taxable gift for entire cash value. Blaffer vs. Com'r, *103 Fed. (2) 498;* Farish vs. Com'r, *103 Fed. (2) 1007.*

96. Q. *Is there a Gift Tax due when A pays for a joint and survivorship annuity for himself and after his death to B?*

A. There is probably a gift of a future interest. But see Question 124, which treats B's share as an estate of inheritance after A's death. If subsequent decisions confirm this view, there should be credit given for Gift Tax paid.

97. *Q. How is the gift of an annuity determined?*

A. Where the giver purchases it unconditionally for another person the value of the gift is the *cost* to the giver. Where, however, the giver reserves the right to revoke the gift only such annuity payments as are made prior to revocation are taxable gifts. *Reg. 79, Art. 19.*

98. *Q. How are annuities valued for Gift Tax?*

A. Value of annuity issued by company or comparable contract.

99. *Q. How are endowments payable in instalments valued for Gift Tax?*

A. By Tables A and B. See pages 102 to 106.

100. *Q. When were the present Gift Tax rates effective?*

A. Jan. 1, 1936. *1935 L. 301* (*c*); the Second Revenue Act of 1940 increased the tax on all gifts made between June 25, 1940 and December 31, 1945, by 10% in order to raise funds to help defray the cost of defense expenditures.

101. *Q. When is the Gift Tax due?*

A. It is to be paid by the giver on or before March 15th following the close of the calendar year in which the gift is made. *1932 L. 509 (a).*

102. *Q. How is the Gift Tax computed?*

A. 1. Ascertain amount of net gifts in calendar year.
2. The net gifts for preceding calendar years after June 6, 1932, deducting exemptions claimed.
3. Add to gifts of calendar year, net gifts of preceding years.
4. Compute tax on total.
5. Compute tax on same rate schedule for each of the preceding years only.
6. Subtract amount found in Step 4 from amount in Step 5.

If no gifts have been made in the past, this answer is much simplified. Today the first $3,000 * of gift to each donee is not counted and there is an overall exemption of $30,000.† *Reg. 79, Art. 5. T. D. 5241.*

ILLUSTRATION—GIFT TAX COMPUTATION

A person makes three gifts (none of them in trust and none of future interests): one of $2,000, one of $10,000 and one of

* Formerly $5,000 and $4,000.
† Formerly $50,000 and $40,000.

$55,000. The gift tax is computed as follows (assuming no prior gifts):

Total gifts to three persons	$67,000
Deduct exclusions	8,000
Balance, before specific exemption	59,000
Deduct specific exemption	30,000
Balance, subject to tax rates (in table)	$29,000
Tax on first $20,000, from table	$ 1,200
Tax on next $9,000, from table (10½%)	945
Total gift tax	$ 2,145

ESTATE TAX

GENERAL PROVISIONS

107. Q. *Is life insurance subject to Federal Estate Tax?*

A. Yes, life insurance of every description if the insured paid the premiums during his lifetime and the net general estate together with the taxable life insurance principal exceeds $60,000.* This holds true whether the insurance is paid to the estate or to a named beneficiary. *L. 404 (a). Reg. 105, Sec. 81.25, 81.28.*

One factor which determines the taxation or exemption of life insurance proceeds is the source of the premiums. If

* Formerly, there was $40,000 general estate exemption plus $40,000 life insurance exemption if paid to named beneficiary or beneficiaries.

the insured pays directly or indirectly (gives it to beneficiary, who pays) the proceeds are taxable; if the beneficiary pays they are exempt. If one pays part and the other pays part, the proceeds become taxable and exempt in proportion as the premiums of each bear to total premiums paid.

The second factor is the party who possesses the incidents of ownership—the right to surrender, borrow, change the beneficiary, etc. To the extent the insured has retained this at his death, either alone or in conjunction with another person, the proceeds become taxable even if somebody else paid the premiums. A reversionary interest in the insured's estate is not an incident of ownership, except where beneficiary was named prior to Jan. 10, 1941. *L. 404 (g). Reg. 105; Sec. 81.27.*

108. *Q. Does this rule vary in Community Property states?*

A. Formerly it did, but no longer. The law now reads premiums paid by the insured out of community property are considered to be paid by the insured unless the survivor can show the premiums or part of them were for personal services actually performed, or derived originally from such compensation or from separate property of surviving spouse. *L. 404 (g) (4). Reg. 105; Sec. 81.24. T. D. 5239.*

109. Q. *What is included in the term "insurance"?*

A. All insurance of every description paid because of death, including accident insurance and death benefits paid by fraternal beneficial societies, operating under the lodge system. *Reg. 105; Sec. 81.25.*

110. Q. *Are double indemnity benefits taxable?*

A. Yes. Amounts received on account of accidental death under accident policies or under the double indemnity provisions of life insurance policies are amounts received "under policies taken out by the decedent upon his own life." Hence, such amounts should be included in the gross estate of the decedent. *L. 404 (g) (2).* Ackerman vs. Commissioner, *15 B. T. A. 635. Reg. 105, Sec. 81.25.*

111. Q. *Are employees' trust proceeds of life insurance taxable?*

A. It has been ruled that Estate Tax would not be imposed on proceeds bought by employer, where employee's only right was to designate beneficiary. Dimock vs. Corwin, *19 Fed. Supp. 56.* By inference we would suppose that the portion paid for by the employee is subject to Estate Tax if estate exceeds $60,000. If the amount payable to the beneficiary is in the nature of a refund annuity, then the present value may be calculated and taxable portion ascertained. This is an opinion.

112. *Q. Does beneficiary's right to withdraw principal make such principal subject to Estate Tax in beneficiary's estate?*

A. Yes, the right to withdraw principal is considered the power to consume or appoint one's self the beneficiary and we believe that would be included in the taxable power of appointment under the law. *Reg. 105, Sec. 81.24. T. D. 5239.*

113. *Q. How is a Continuous Monthly Income policy valued?*

A. At the principal amount plus the annuity. The Continuous Monthly Income is a contract written to pay an income for life, but at least for a minimum number of years whether the beneficiary lives or dies. Consequently if the beneficiary is living at the death of the insured, such person has more than the face value of the policy. She has in addition a guarantee of an income after she has consumed all the principal in the contract. International Trust Company vs. U. S., *Dist. Ct.* (*Colorado*). *May 20, 1943.*

114. Q. *If proceeds of a matured endowment are left with the company at interest, are proceeds taxable as part of insured's estate?*

A. Yes, even though beneficiary clause provides that the widow of the insured shall continue to receive interest and then daughter get instalments. The provision by which the insured receives interest on the proceeds after maturity and then distributes to his wife and daughter after his death is a transfer intended to take effect in possession and enjoyment after death and is taxable. Schultz vs. U. S. *Dist. Ct.* (*Mo.*) *E. D. 1878, June 22, 1943.*

115. Q. *Are corporations subject to Estate Tax on proceeds of corporation life insurance?*

A. No. The Estate Tax affects only insurance "purchased with premiums paid directly or indirectly by the decedent," meaning insurance which the policyholder controls. See Question 120.

Corporation insurance is not usually in this class. *1926 L. 404 (g); Reg. 105; Sec. 81.28.*

116. *Q. Is corporation insurance subject to Estate Tax in the insured's estate when it is payable to a trustee for purpose of purchasing insured's stock?*

A. No. Proceeds payable under an insurance trust agreement to take over decedent's business interest, premiums previously having been paid by corporation, are not part of decedent's gross estate for tax purposes. The fact that decedent owned stock in the corporation did not make him indirect payer of premiums. Wilson vs. Crooks, *52 Fed. (2) 692.*

117. *Q. How are common-law partnerships affected by the Estate Tax?*

A. The individual partners are subject to the Estate Tax for a proportionate share thereof, provided the estate is large enough to be subject to tax and the total insurance on the life of the decedent together with his taxable general estate exceeds $60,000, because each partner pays a proportionate share of the premium on his own insurance. See

Question 118. Sampson Ex'r vs. U. S. *1 Fed. Supp. 95.*

118. *Q. If partners individually own policies on the lives of each other would there be any Estate Tax upon the proceeds?*

A. No. The Estate Tax has reference only to insurance taken out by a decedent upon his own life. This does not include insurance owned and paid for by parties other than the insured; for instance, the beneficiary. *Reg. 105, Sec. 81.25.*

119. *Q. Does the fact that the insured signs the application make any difference?*

A. No. *Reg. 105, Sec. 81.25.*

120. *Q. How may the proceeds of life insurance policies be made totally exempt from Federal Estate Tax?*

A. By applying for insurance on the life of another person where a valid insurable interest exists and paying all the premiums due upon the policy until it matures. For instance, a wife buys a policy on her husband's life, a creditor upon the life of his debtor, a corporation on the life of its president or other officer. Of course the payment of premiums must be out of funds belonging to the beneficiary and not transferred by the insured for that purpose. *L. 404 (g) (1) (2).*

If the insurance was taken out before Jan. 10, 1941, and there was a complete transfer of incidents of ownership to beneficiary or assignee prior to that date, the payment of premiums by the insured prior to that date will not destroy the exemption, but any premium paid by the insured after Jan. 10, 1941, will make the proceeds proportionally taxable. *T. D. 5032.* The main incidents of ownership are the right of insured or his estate to economic benefits, to change the beneficiary, surrender the policy for cash, to assign, revoke assignment, or make loans upon it. This means a complete and irrevocable transfer of the policy. *I. T. 2553; C. B. IX–2, p. 101. Reg. 105, Sec. 81.27.* Where incidents of ownership are transferred in contemplation of death the proceeds are taxable even though insured paid no premiums. *Reg. 105, Sec. 81.25.* This section also indicates that a gratuitous transfer reserving to the insured's estate the proceeds if beneficiary does not survive, is taxable under *L. 811 (c)* as a transfer to take effect in possession or enjoyment at death. *Reg. 105, Sec. 81.25.*

Whether the "proceeds" of exempt insurance include dividends accumulated, depends on what the policy says. It has been held they are taxable if subject to insured's control at time of death. Helvering vs. Parker, *84 Fed. (2) 838.*

121. Q. *If a wife takes out insurance on the life of her husband, paying the premiums thereon, would the proceeds be subject to taxation?*

A. No. A wife may insure her husband's life for any amount, and, provided she receives notices, pays premiums out of her separate estate, and holds the policy, the proceeds when received would not be subject to either the Estate Tax or the Income Tax. *Letter to Prentice-Hall, September 15, 1922.*

122. Q. *Are life insurance proceeds irrevocably payable to religious, charitable, scientific and educational corporations subject to Estate Tax in any amount?*

A. No. *L. 812 (d).* John McKelvy Estate vs. Com'r, *82 Fed. (2) 395. Reg. 105, Sec. 81.44. T. D. 5239.*

123. Q. *Is the refund of a Cash Refund Annuity subject to Estate Tax?*

A. Yes. The present worth or commuted

value at the date of the decedent's death of the Cash Refund Annuity contract where he had right to change beneficiary, is held to constitute a part of the gross estate, subject to estate tax. This contract is not insurance, hence not entitled as such to exemption. Guaranty Trust Company, Exc'r., vs. Commissioner, *16 B. T. A. 314.* Reversed but not appealed. The Attorney General of Iowa has ruled in an opinion dated Aug. 5, 1936, that the refund is taxable as a transfer effective at or after death.

124. *Q. Is a joint and survivorship annuity subject to Estate Tax after the death of the first annuitant?*

A. Yes. Haskell vs. Com'r, *Memo opinion, June 12, 1933*, on ground it is a transfer to become effective in possession and enjoyment at or after death. Similar decisions, Com'r vs. Wilder's Est., *118 Fed. (2) 28;* Mearkle vs. Com'r, *129 Fed. (2) 386.* The value of survivor's interest is the premium it would cost to buy the survivor an annuity of the amount received at the date of death, assuming the purchaser of the annuity is the party who dies.

But exemption was allowed in a case involving New York Estate Tax. "The right of survivor under a joint and survivorship annuity policy cannot be considered a taxable interest or transfer taking effect in possession or enjoyment at death." Re Wilson's Estate, *257 N. Y. Supp. 230.*

Annuity held not taxable where beneficiary irrevocable and policy taken out before Mar. 3, 1931, because in nature of irrevocable trust. At that time such trusts were exempt from Estate Tax, even though creator reserved life income to himself. Chemical Bank & Saxe vs. Com'r, *37 B. T. A. 535.* Guarantee Tr. vs. Com'r, *16 B. T. A. 314,* distinguished.

125. Q. *Are the proceeds paid at death of a combined annuity and life insurance contract entitled to exemption as life insurance?*

A. No, even though paid to named beneficiaries. The court said, "We think this is purely an investment risk relating only to management in investing the fund. There is no evidence the company assumed any of the risks of life insurance." Old Colony Trust & Morss vs. Com'r, *37 B. T. A. 435.* Valequette vs. Com'r, Dist. Ct. (Ohio) S. D. Civil Action 142, Feb. 6, 1943.

Where two separate contracts are issued

at the same time, one an annuity and the other an insurance policy, there has been a conflict of decisions. Policy proceeds were not insurance in Estate of Anna H. Clise, *122 Fed.* (2) *998*. Held not to be insurance in Helvering vs. Tyler, *312 U. S. 5;* Com'r vs. Keller, *312 U. S. 543*. The Supreme Court has fixed the law for the present by holding that the two policies must be considered together and that the transaction is a transfer to take effect in possession and enjoyment at death. C. C. A. reversed. Helvering vs. Le Gierse, *312 U. S. 531*.

It is to be noted that all of the above decisions involve situations in which the policyholder was too old to buy a life insurance policy without an annuity and no medical examination was required.

No case appears to have been decided where a physical examination has taken place or where the two policies were issued at different times.

126. Q. *How is the present Estate Tax computed?*

A. Neither the 1941 nor 1942 Revenue Act changed Estate Tax rates. Changes were made in description of property subject to tax and administrative provisions.

The 1926 Estate Tax has been retained, with a credit up to eighty per cent for state inheritance taxes paid. The exemption is $100,000. An additional Estate Tax has been superimposed by the 1935 Act, which merely amended the rates of the 1934 Act. The 1942 law now in force allows $60,000 exemption and no credit for state inheritance taxes paid. The additional Estate Tax is the *difference* between the tax imposed by the 1926 law and the tax as provided in the schedule of the 1935 law.

The estates of all persons dying after 11:45 a. m. on June 25, 1940, must pay an additional tax of 10%. *Sec. 951, L. 1940.*

ILLUSTRATION—ESTATE TAX COMPUTATION

*(Applicable to estates of decedents dying after October 21, 1942)**

Basic tax computation:

Gross amount of estate	$235,000
Deduct:	
Specific exemption (basic)	100,000
Funeral and administrative expenses, claims, commissions, etc.	30,000
Charitable bequests	10,000
Total deductions and exemption	140,000
Net amount of estate, for basic tax	$ 95,000

Applying basic tax rates from table:

Tax on $50,000	$ 500
Tax on $45,000 (in 2% bracket)	900
Gross basic estate tax	1,400
Credits:	
State inheritance taxes (80% maximum)	1,120
Net basic estate tax	$ 280
Additional tax computation:	
Gross amount of estate (from above)	$235,000
Deduct:	
Specific exemption	60,000
Basic tax deductions, exclusive of basic tax exemption	40,000
Total deductions and exemption	100,000
Net amount of estate, for additional tax	$135,000
Applying aggregate tax rates, from table:	
Tax on $100,000	$ 20,700
Tax on $35,000 (in 30% bracket)	10,500
Total tentative tax	$ 31,200
Less gross basic estate tax (from above)	1,400
Additional estate tax	$ 29,800
Add net basic estate tax (from above)	280
Total estate tax	$ 30,080

127. Q. *What are the statutory exemptions?*

A. There is a general estate exemption in the basic Estate Tax (*L. 1926*) of all legal debts, including administration expenses and $100,000 for residents or

* The method of computing the tax on estates of decedents dying on or before October 21, 1942, is substantially the same, varying only by virtue of differences in rates and exemptions applicable at the time of death.

citizens of the United States. For purpose of additional Estate Tax an exemption of $60,000 if decedent died after Oct. 21, 1942. *L. 1942; 414; Reg.105, Sec. 81.2, T. D. 5239.* There is no special exemption of life insurance paid to a named beneficiary as in prior laws.

128. Q. *Where there is more than $60,000 taxable general estate and insurance and several beneficiaries, how is the exemption applied?*

A. Proportionally. For instance, suppose there is no general estate to speak of and a life insurance total of $75,000, $60,000 of which is payable to one beneficiary and $15,000 to another. There is only one $60,000 exemption and this must be divided proportionally. Thus, the first beneficiary will get four-fifths of the exemption, or $48,000, and the second beneficiary one-fifth of the exemption, or $12,000. Estate of Adelaide E. White, *22 B. T. A. 1076.*

129. Q. *Is a policy absolutely assigned "for value received" subject to Estate Tax?*

A. No. Where the decedent makes an absolute and unconditional assignment of a policy of insurance on his own life, no part of the proceeds received by the assignee need be included in determining the value of the gross estate. Guettel et al vs. U. S. (1929) *67 Ct. Claims (U. S.) 613.*

But the receiver might be subject to Income Tax on the profit if a valuable consideration passed between the parties. See Question 37. Assignments are often described as "for value received" when in point of fact nothing valuable passes between the parties. In such case it is better to describe that no value has been received, that the transfer is a gift, etc.

If, however, the estate receives some benefit from the assignment such as paying off a debt of the insured, then the insurance even though assigned, is included in the estate. Mason vs. Com'r, *43 B. T. A. 813;* Hofferbert vs. Com'r, *46 B. T. A. 110.*

130. *Q. If a wife takes out insurance on the life of her husband and pays the premiums thereon, is the policy a part of her estate should she predecease her husband?*

A. Yes, if the policy is her absolute property, the inventory of her estate should show the cash value of the policy at her death.

131. *Q. If a policyholder reserving incidents of ownership or paying premiums (See Question 120) already has life insurance, and a general estate exceeding $60,000 should additional insurance be made payable to his estate?*

A. Considering only the Federal Estate Tax, it makes no difference how policies are payable after the $60,000 exemption is exceeded. However, there is a difference when state inheritance taxes are considered. Most State Inheritance Tax laws exempt life insurance proceeds paid to beneficiaries other than executors or administrators in official capacity as such.* For this reason and saving

* Exceptions

Alabama—Taxes transfers occurring by the vesting in a beneficiary of the proceeds of life insurance in excess of $40,000. H. B. 324, L. 1935.

Arizona—Taxes life insurance proceeds to the extent of the excess over $40,000 of the amount receivable by all other beneficiaries than the insured on insurance taken out by the decedent upon his own life. L. 1937, Chapter 27, Sec. 5 (6), as amended by Chapter 10, L. 1939.

Arkansas—Taxes life insurance proceeds paid to beneficiaries not wife, direct descendants or ascendants of insured, where paid as a gift or devise not based on valuable consideration. Act 438, L. 1923; Act 106, L. 1929.

California—Taxes life insurance proceeds paid to named beneficiaries in excess of $50,000. L. 1935, Chapter 358.

Colorado—Taxes life insurance proceeds in excess of $75,000 payable to named or described beneficiaries. The exemption is pro rated among the beneficiaries. Chapter 85, L. 1935, as amended by Chapter 176, L. 1937 and Chapter 111, L. 1939.

Florida—Taxes life insurance in excess of $40,000 payable to named beneficiaries other than the executor or the estate where the gross estate exceeds $100,000. Chapter 16015, L. 1933.

Georgia—Taxes transfers occurring by the vesting in a beneficiary of the proceeds of life insurance in excess of $40,000. Act No. 451, L. 1925, as amended by Act No. 334, L. 1927.

Kentucky—Taxes life insurance proceeds in excess of $10,000 payable to individual beneficiaries. If there is more than one beneficiary the exemption is apportioned. Chapter 8, L. 1936. Does not include corporations. De Leuil vs. Dept. of Revenue, Jan. 27, 1938. Jefferson C. C.

Minnesota—Taxes life insurance proceeds in excess of $32,500 payable to named beneficiaries. Chapter 338, L. 1939.

Mississippi—Taxes life insurance proceeds in excess of $20,000 payable to individual beneficiaries. Chapter 125, L. 1930. Otherwise, where beneficiary has a vested right in the policy. Tax Commission Ruling.

Montana—Taxes all life insurance proceeds over $50,000. Chapter 65, L. 1923. Annuity proceeds considered life insurance. State Bd. of Equalization vs. Fligman, —, p. (2) —.

New York—Taxes life insurance payable to named beneficiaries in excess of $100,000 less personal exemption allowed under N. Y. Estate Tax law to beneficiary. Chapter 710, L. 1930.

North Carolina—Taxes proceeds of life insurance policies in excess of $20,000 payable to lineal issue, lineal ancestors, husband, wife, or adopted child, and all proceeds payable otherwise. H. B. 13, L. 1939.

North Dakota—Taxes all life insurance proceeds in excess of $20,000. Chapter 251, L. 1933.

Ohio—Does not tax insurance payable to individuals except where more than $40,000 of insurance is taxed by the Federal Government and Ohio levies an additional Estate Tax to absorb the balance of the 80% credit allowed under the Federal Estate Tax. Ohio Code, Ann. (Baldwin 1934), Sec. 5332.

Oklahoma—Taxes life insurance proceeds in excess of $20,000 receivable by all named beneficiaries from policies under which decedent, at the time of his death, had the right to change the beneficiary. Chapter 6, Art. 9, L. 1939.

Tennessee—Taxes all life insurance proceeds other than amounts up to $40,000 payable to husband, wife, son, daughter, lineal ancestor or lineal descendant, legally adopted child and lineal descendant of such adopted child. Tenn. Code 1932, Secs. 1259-1295, as amended by Chapter 79, L. 1933, Chapter 41, L. 1935, Chapter 129, L. 1937 and Chapter 101, L. 1939.

Texas—Life insurance proceeds payable to individual beneficiaries are taxable to the extent of the excess over $40,000 of the amount receivable by all beneficiaries. Chapter 5, Rev. Civ. Stats. 1925, as amended and supplemented.

Washington—Taxes insurance proceeds in excess of $40,000 payable to named beneficiaries. Chapter 180, L. 1935.

Wisconsin—Taxes insurance payable to named beneficiaries other than the estate of the insured but allows a $10,000 exemption which is apportioned among the beneficiaries. Chapter 405, L. 1939.

administration costs there is an advantage in having as much insurance as possible paid to named beneficiaries whether individual or corporate.

132. Q. *Is there any deduction of Federal Estate Tax for State Inheritance and succession taxes paid?*

A. Yes. *1926 L. 301 (b), Reg. 105, Sec. 81.2, Art. 9 (b).* The deduction is limited to 80% of the 1926 Federal Estate Tax. Many states have levied an additional tax to absorb this saving or a portion thereof; hence, the liability of the estate to combined State and Federal governments is not always reduced.

133. Q. *If a decedent leaves debts greater than his legal estate, will the fact that his life insurance is protected from the debts reduce the estate's deductions?*

A. Yes. Deductions for debts of decedent cannot exceed property attachable for those debts. Thus, if insured had $100,000 legal estate and $100,000 life insurance payable to his wife and left $120,000 in debts, the net estate will be $100,000—not $80,000, since the life insurance was exempt from his debts. *L. 405 (a), Reg. 105, Sec. 81.29.*

134. Q. *Are assignments or changes of beneficiary made in contemplation of death subject to Estate Tax?*

A. Yes. L. 404 (a). Reg. 105, Sec. 81.25. T. D. 5239.

This question has not been uniformly decided in the past. Gaither vs. Miles, *268 Fed. 692 (1920)* said "No." *G. C. M. 1164, C. B. VI–1, page 315,* ruled likewise, even though the insurance was in excess of $40,000 exemption existent at that time. But *G. C. M. 16932, XV–38–8307*, restricted the rule to insurance within the said $40,000 exemption then in force.

The latest decision holds that policies assigned in contemplation of death are includable in the gross estate. (The amount of the insurance does not appear.) Billings vs. Com'r, *35 B. T. A. 1147.*

It would seem that a modification, even in contemplation of death, is exempt if the change did not increase the amount payable to named beneficiaries beyond the $60,000 exemption for insurance and the general estate. But where decedent took out a two-year endowment for $100,000 paying a single premium of $97,225 at age 75, it was held that the cash surrender at death was subject to tax, because the estate did not prove the gift was not in contemplation of death. Igleheart vs. Com'r, *77 Fed. (2) 704.*

A Lower Court decision on Pennsylvania Inheritance Tax holds that beneficiary named in contemplation of death *does not* give right to assess Inheritance Tax. Fickers Est. *24 D & C 501.*

135. Q. *What is "contemplation of death"?*

A. Not a general expectation of death such as all persons entertain, nor is it limited to an expectation of immediate death. It is that state of mind influenced by bodily or mental conditions as prompts persons to dispose of their property to those whom they deem proper objects of their bounty. *Reg. 105, Sec. 81.16.* See U. S. vs. Wells, *283 U. S. 102* for complete interpretation.

136. Q. *How is life insurance payable in instalments valued for purposes of the Estate Tax?*

A. It should be listed as the face value of the policy under the option which could have been exercised either by the insured or by the beneficiary, or if no option is granted the net present value used by the insurance company to determine the amount of the instalments. *Reg. 105, Sec. 81.28.*

137. Q. *Under old law, where insurance is payable to a named beneficiary over a period of years, but unpaid instalments revert to the insured's estate if the beneficiary does not live to receive all the payments, is the tax value of the insurance increased?*

A. Yes. The possibility that some of the payments may be received eventually by the insured's estate is a reversionary interest which is taxable as part of the estate. *Reg. 105, Sec. 81.27, T. D. 5239.*

138. Q. *Who must pay the tax on insurance proceeds?*

A. The executor or administrator. Or, the commissioner may proceed against the beneficiary. *Reg. 105, Sec. 81.99. T. D. 5239.* Tax may be collected from beneficiary even though will states that taxes on property shall be paid out of residuary estate.

If the executor pays tax he may proceed against beneficiary. According to a New York State decision he may even recover out of proceeds held under income settlement option. Re Estate F. L. Scott, *249 N. Y. 542;* Cert. denied.

139. Q. *Is there any deduction for premiums paid in ascertaining the net taxable amount of insurance under the Estate Tax?*

A. No. *O. D. 48, C. B. 1, page 160.*

140. Q. *If a resident decedent leaves practically no estate except life insurance, what would be the total amount of his estate exempt under the Estate Tax?*

A. There would be exempt the sum of $60,000, the total exemption allowed for both life insurance and the general estate of decedent. See Question 131.

141. Q. *Is all life insurance payable to the estate subject to the Estate Tax?*

A. Yes. *L. 404, Reg. 105, Sec. 81.25. T. D. 5239.*

142. Q. *Is life insurance taken out to pay the Estate Tax subject itself to the Estate*

Tax along with the other estate of the decedent?

A. Yes, if there is an obligation to so use the fund. *Reg. 105, Sec. 81.26.* The tax will *not* be avoided by making the policy payable to the U. S. Treasury. Two amendments have been offered to exempt such insurance, but both were deleted before final passage of the bills to which they were attached.

But if insurance taken for this purpose is made payable to a named individual beneficiary, and the insured does not reserve the incidents of ownership and has not paid the premiums, it will not be taxed provided there is no binding collateral agreement requiring the beneficiary to use the proceeds to pay taxes.

143. Q. *Would any agreement to the above effect between insured and beneficiary be binding at law?*

A. Probably but it would be at variance with the written contract of insurance, which would make no mention of trusteeship. Moreover, if the trusteeship were proved for the benefit of the estate, the exemption no longer would be available. *Reg. 105, Sec. 81.26.*

144. *Q. If the beneficiary takes the commuted value named in the policy, what sum is to be reported under the Estate Tax?*

A. The commuted value, not the face amount of the policies. Chisholm vs. Com'r, *37 B. T. A. 167. Reg. 105, Sec. 81.28.*

145. *Q. How is insurance left with the company at interest reportable under the Estate Tax?*

A. At the face value. *Reg. 105, Sec. 81.28.*

146. *Q. Suppose the insurance is reduced by a loan, what amount is taxable?*

A. The sum actually received. *Reg. 105, Sec. 81.28.* See Question 156.

147. *Q. May death of important officer of close corporation diminish value of stock?*

A. Yes. "While not challenging the propriety of including proceeds of insurance made payable to the Company as an asset of the corporation * * * the Board (B.T.A.) should have deducted from this sum a substantial part thereof because of the death of Ingalls and the loss to the company that resulted therefrom." Newell vs. Com'r, *66 Fed. (2) 102.*

148. *Q. Where a corporation insured the life of an officer-stockholder, agreeing to purchase his stock after death, are the proceeds collected by the corporation after death included in the estate valuation of the stock?*

A. Yes. The proceeds are considered part of corporate assets unless collected as trustee. The Bureau will value the stock without regard to the contract price between the insured and the corporation. See, however, Question 149 for affect of binding agreement on stock valuation. *Letter to E. P. Huttinger, July 31, 1925.* Confirmed *4 B. T. A. 959. Estate W. A. Blair.* This opinion has also been followed by the Court of Appeals of New York, in a case which involved New York Inheritance Tax. It was held that the proceeds of the policies were in no sense an increment of the corporate assets *after* the decedent's death. "They were the fruit of the policies and an element of the value of the corporate stock which should be included in the value of the decedent's estate. There is no distinction between this case, and where a decedent leaves a policy of life insurance payable to himself or his estate. There the proceeds received are taxable. Here the policies were the property of the corporation, their value became fixed at death and the proceeds became corporate assets, by which the value of stock held by the decedent was to be appraised." *Re Reed, 243 N. Y. 199; 153 N. E. 47.* See Question 147.

149. Q. *Are binding agreements on executors to sell stock to business associates valid for establishing estate tax value?*

A. Yes, even though market value is greater. "The tax is not on the interest to which some person succeeds on a death, but the interest which ceased by reason of death." Lomb vs. Sugden, *82 Fed. (2) 166;* Wilson vs. Bowers, *57 Fed. (2) 682;* Bensel vs. Com'r, *36 B. T. A. 246.*
And where life insurance is used to buy the stock of a deceased associate the Government cannot tax both the life insurance and the value of the stock. If the insurance is taxable the value of the stock is to be reduced by the proceeds thereof. Est. John T. H. Mitchell, *37 B. T. A. 1.*

150. Q. *Is War Risk insurance taxable?*

A. War Risk insurance is treated like any other insurance under Federal law, but in certain jurisdictions it is exempt from State Inheritance Tax whether payable to the estate or to named beneficiaries.*

* The following laws and decisions have appeared with respect to State Inheritance Taxes:

Ala.	Taxable. U. S. Trust Co. of N. Y., Exr. (u/w George H. Bunker) vs. Helvering, 307 U. S. 57, 83 L. ed. 1104 (1939).
Ariz.	Taxable when paid to the estate. Letter from Hon. Evan Stallcup, Inheritance Tax Collector, to Prentice-Hall, Inc., April 27, 1933.
Calif.	Exempt. Chapter 358, L. 1935.
Conn.	Exempt. Chapter 219, L. 1933.
Fla.	Taxable. U. S. Trust Co. of N. Y., Exr. (u/w George H. Bunker) vs. Helvering, 307 U. S. 57, 83 L. ed. 1104 (1939).
Ga.	Taxes transfers occurring by the vesting in a beneficiary of the proceeds of life insurance in excess of $40,000. Act No. 451, L. 1925, as amended by Act No. 334, L. 1927.
Ill.	Taxable. Opinion Atty. Gen., Nov. 21, 1934.
Iowa	Exempt. Estate of Taffl, Dist. Ct., Sept. 22, 1928.
Kan.	Exempt. (Official letter.)
Ky.	Exempt. Opinion Atty. Gen. 1929, p. 728.
La.	Exempt. Re Geier, 99 So. 26; 155 La. 167.
Md.	War Risk Insurance proceeds are not by their nature exempt from Inheritance Tax. Opinion Atty Gen., Jan. 4, 1935. But, where proceeds of a War Risk Insurance policy were payable to a named beneficiary, they were not taxable even though the beneficiary predeceased the insured. Opinion Atty. Gen., Mar. 18, 1932.
Minn.	Exempt. In re Harris Estate, 229 N. W. 781 (1930). The commuted value of War Risk Insurance is subject to Inheritance Tax upon the death of the beneficiaries named in the policy. Opinion Atty. Gen. in letter dated Aug. 1, 1938.
Mo.	The proceeds of War Risk Insurance are not taxable. Ruling by Attorney General.
N. J.	Exempt. Law 1935 Chapter 90.
N. M.	Exempt. (Official letter.) Opinions of Atty. Gen. 1931-1932, p. 117.

N. Y.	Taxable. U. S. Trust Co. of N. Y., Exr. (u/w George H. Bunker) vs. Helvering, 307 U. S. 57, 83 L. ed. 1104 (1939).
N. C.	Exempt. H. B. 13, L. 1939, Sec. 2 (d).
N. D.	Exempt. (Official Letter.)
Ohio	Exempt. Tax Commission vs. Rife, 119 O. S. 83, 162 N. E. 390 (1928).
Okla.	Exempt. L. 1939, Chapter 6, Art. 9, Sec. 6(A)(6).
Ore.	Exempt except when payable to the estate of the insured. Opinions Atty. Gen., Feb. 9, 1926, June 20, 1931.
Pa.	Exempt. Wanzel's Estate, 295 Pa. 419, 145 Atl. 512 (1929).
S. C.	Exempt. Letter from Tax Commission to Prentice-Hall, 3/12/29.
S. D.	Exempt. (Official letter.)
Tenn.	Exempt. Tenn. Code 1932, Secs. 1259-1295, as amended by Chapter 79, L. 1933, Chapter 41, L. 1935, Chapter 129, L. 1937 and Chapter 101, L. 1939.
Wash.	Exempt. L. 1929, Chapter 135, as amended.
W. Va.	Exempt. Watkins vs. Hall, 147 S. E. 876.
Wis.	Taxable. Tax Commission Ruling July 11, 1939. Ruling cites as authority U. S. Trust Co. of N. Y., Exr. (u/w George H. Bunker) vs. Helvering, 307 U. S. 57, 83 L. ed. 1104 (1939).

See Question 26.

Letter to Prentice-Hall dated July 7, 1925.

DEBTOR-CREDITOR

152. Q. *Are the proceeds of life insurance taken out for the protection of creditors subject to the Estate Tax?*

A. Yes, where such transactions contemplate payment of premiums directly or indirectly by the debtor insured. *Reg.*

105, Sec. 81.26. See Question 155.

153. *Q. Suppose the debtor insured does not own the policy and does not pay the premiums, would the proceeds be subject to the Estate Tax?*

A. No. Where there is no element of donative intent and the decedent debtor has retained no interest in the policy and pays no premiums thereon the insurance is not considered as part of the decedent's estate. *Reg. 105, Sec. 81.27. T. D. 5239.* See Question 154.

154. *Q. Suppose the debtor and creditor each pay some of the premiums?*

A. If the decedent either directly or indirectly paid the premiums thereon, the insurance is considered receivable for the benefit of the estate. *Reg. 105, Sec. 81.26.*

155. *Q. When the debtor dies is the full amount of insurance subject to tax as part of his estate?*

A. No. The face value of the policy should be reported in the gross estate, but the loan with accrued interest will be deductible as a debt. *Reg. 105, Sec. 81.26.* See Question 37, relative to Income Tax on profit to creditor.

156. Q. *Is indebtedness existing against a policy deductible from the gross estate in ascertaining the tax due?*

A. No. Loans on life insurance policies which were deducted from the face of the policies in making settlement, do not constitute claims against the estate. *Appeal of Kennedy, Exec'r, 4 B. T. A. 330.*

Neither is interest on the loan and added thereto deductible. Prime vs. Com'r, *39 B. T. A. 487.*

TRUSTS

158. Q. *If life insurance is made payable to a trust company as trustee for the purpose of paying the estate taxes, would the insurance proceeds be taxed as part of the estate?*

A. Yes. The insurance being for the benefit of the estate, it would be considered a part thereof. *Reg. 105, Sec. 81.26.*

159. Q. *How are life insurance trusts administered by trust companies taxed?*

A. Proceeds are subject to Estate Tax subject to $60,000 exemption for total estate, if the insurance and income from the investment of said proceeds is subject to Income Tax. Morton, Admr., *23 B. T. A. 236*. The amount of insurance will be reduced by trustee's commission if chargeable on insurance proceeds. Memo. T. C. Banker's Trust Co., Executor of Estate of Alan M. Lincoln, 12-24-42.

160. Q. *If life insurance is payable to a trust company or bank as beneficiary or assignee, in trust for individual beneficiaries, is such insurance entitled to exemption?*

A. Yes, if the total estate does not exceed $60,000. See Question 107.

161. Q. *What laws have been passed since insurance has become an object of taxation?*

A. Revenue Act of 1918, signed Feb. 24, 1919.

Revenue Act of 1921, signed Nov. 23, 1921.

Revenue Act of 1924, signed June 2, 1924.

Revenue Act of 1926, signed Feb. 26, 1926.

Revenue Act of 1928, signed May 27, 1928.

Revenue Act of 1932, signed June 6, 1932.

Revenue Act of 1934, signed May 10, 1934.

Revenue Act of 1935, signed Aug. 30, 1935.

Revenue Act of 1936, signed June 22, 1936.

Revenue Act of 1937, signed August 26, 1937.

Revenue Act of 1938 became law at midnight, May 27, 1938, without the President's signature.

Revenue Act of 1939, June 29, 1939.

Revenue Act of 1940, June 25, 1940.

Second Revenue Act of 1940, October 8, 1940.

Revenue Act of 1941, September 20, 1941.

Revenue Act of 1942, October 21, 1942.

This page originally was set aside for tax schedule authorized by the Revenue Act of 1942. But as a new law is promised by January 1, 1944, which will increase taxes on 1943 income we have left this page blank for later insertion.

Net Gifts [1]		Bracket	Percentage Rate of Tax	Tax on Total Net Gift
Over	Not Over			
....	$5,000	$5,000	2¼	$112.50
$5,000	10,000	5,000	5¼	375
10,000	20,000	10,000	8¼	1,200
20,000	30,000	10,000	10½	2,250
30,000	40,000	10,000	13½	3,600
40,000	50,000	10,000	16½	5,250
50,000	60,000	10,000	18¾	7,125
60,000	100,000	40,000	21	15,525
100,000	250,000	150,000	22½	49,275
250,000	500,000	250,000	24	109,275
500,000	750,000	250,000	26¼	174,900
750,000	1,000,000	250,000	27¾	244,275
1,000,000	1,250,000	250,000	29¼	317,400
1,250,000	1,500,000	250,000	31½	396,150
1,500,000	2,000,000	500,000	33¾	564,900
2,000,000	2,500,000	500,000	36¾	748,650
2,500,000	3,000,000	500,000	39¾	947,400
3,000,000	3,500,000	500,000	42	1,157,400
3,500,000	4,000,000	500,000	44¼	1,378,650
4,000,000	5,000,000	1,000,000	47¼	1,851,150
5,000,000	6,000,000	1,000,000	50¼	2,353,650
6,000,000	7,000,000	1,000,000	52½	2,878,650
7,000,000	8,000,000	1,000,000	54¾	3,426,150
8,000,000	10,000,000	2,000,000	57	4,566,150
10,000,000	....	....	57¾	....

[1] After deducting exemption of $40,000 in computing 1942 gift taxes, or $30,000 thereafter, and after taking annual exclusions for individual donees ($5,000 through 1938; $4,000 after 1938 and through 1942; and $3,000 after 1942). The annual exclusions do not apply to gifts of future interests nor to gifts in trust after 1938 but before 1943.

ESTATE TAXES

BASIC ESTATE TAX RATES [1]

Net Estate After Deducting the $100,000 Exemption			Rate of Tax	Amount of Tax	
Over	Not Over	Block		On Block	On Total Estate
....	$50,000	$50,000	1%	$500	$500
$50,000	100,000	50,000	2%	1,000	1,500
100,000	200,000	100,000	3%	3,000	4,500
200,000	400,000	200,000	4%	8,000	12,500
400,000	600,000	200,000	5%	10,000	22,500
600,000	800,000	200,000	6%	12,000	34,500
800,000	1,000,000	200,000	7%	14,000	48,500
1,000,000	1,500,000	500,000	8%	40,000	88,500
1,500,000	2,000,000	500,000	9%	45,000	133,500
2,000,000	2,500,000	500,000	10%	50,000	183,500
2,500,000	3,000,000	500,000	11%	55,000	238,500
3,000,000	3,500,000	500,000	12%	60,000	298,500
3,500,000	4,000,000	500,000	13%	65,000	363,500
4,000,000	5,000,000	1,000,000	14%	140,000	503,500
5,000,000	6,000,000	1,000,000	15%	150,000	653,500
6,000,000	7,000,000	1,000,000	16%	160,000	813,500
7,000,000	8,000,000	1,000,000	17%	170,000	983,500
8,000,000	9,000,000	1,000,000	18%	180,000	1,163,500
9,000,000	10,000,000	1,000,000	19%	190,000	1,353,500
10,000,000	....	Remainder	20%	....	....

[1] These rates are the same as provided in Sec. 810 of the Internal Revenue Code (Sec. 301 (a), 1926 Act).

ESTATE TAXES

AGGREGATE ESTATE TAX RATES UNDER CODE SEC. 935 [1]

Net Estate After Deducting the Allowable Exemption [2]			Rate of Tax	Amount of Tax	
Over	Not Over	Block		On Block	On Total Estate
....	$5,000	$5,000	3%	$150	$150
$5,000	10,000	$5,000	7%	350	500
10,000	20,000	10,000	11%	1,100	1,600
20,000	30,000	10,000	14%	1,400	3,000
30,000	40,000	10,000	18%	1,800	4,800
40,000	50,000	10,000	22%	2,200	7,000
50,000	60,000	10,000	25%	2,500	9,500
60,000	100,000	40,000	28%	11,200	20,700
100,000	250,000	150,000	30%	45,000	65,700
250,000	500,000	250,000	32%	80,000	145,700
500,000	750,000	250,000	35%	87,500	233,200
750,000	1,000,000	250,000	37%	92,500	325,700
1,000,000	1,250,000	250,000	39%	97,500	423,200
1,250,000	1,500,000	250,000	42%	105,000	528,200
1,500,000	2,000,000	500,000	45%	225,000	753,200
2,000,000	2,500,000	500,000	49%	245,000	998,200
2,500,000	3,000,000	500,000	53%	265,000	1,263,200
3,000,000	3,500,000	500,000	56%	280,000	1,543,200
3,500,000	4,000,000	500,000	59%	295,000	1,838,200
4,000,000	5,000,000	1,000,000	63%	630,000	2,468,200
5,000,000	6,000,000	1,000,000	67%	670,000	3,138,200
6,000,000	7,000,000	1,000,000	70%	700,000	3,838,200
7,000,000	8,000,000	1,000,000	73%	730,000	4,568,200
8,000,000	10,000,000	2,000,000	76%	1,520,000	6,088,200
10,000,000	....	....	77%	....	....

[1] These rates are as prescribed by Sec. 935 of the Internal Revenue Code as amended by Sec. 401, 1941 Act. Prior to amendment, Code Sec. 935 corresponded with Sec. 401(b), 1932 Act, as amended.

[2] The exemption as to estates of decedents dying before October 22, 1942, is $40,000. In the case of decedents dying on or after that date, the exemption, by virtue of changes made by the 1942 Revenue Act, is $60,000.

TABLE "A"

Table, single life, 4 per cent, showing the present worth of an annuity, or life interest, and of a reversionary interest.

1 Age	2 Annuity, or present value of $1.00 due at the end of each year during the life of a person of specified age	3 Reversion, or present value of $1.00 due at the end of the year of death of a person of specified age
	Annuity	*Reversion*
0	$14.72829	$0.39507
1	17.30771	.29586
2	18.69578	.24247
3	19.15901	.22465
4	19.41226	.21491
5	19.55301	.20950
6	19.61731	.20703
7	19.62502	.20673
8	19.61097	.20727
9	19.53413	.21022
10	19.45359	.21332
11	19.36943	.21656
12	19.28184	.21993
13	19.19065	.22344
14	19.09590	.22708
15	18.99764	.23086
16	18.89569	.23478
17	18.79010	.23884
18	18.68070	.24305
19	18.56751	.24740
20	18.45038	.25191
21	18.32932	.25656
22	18.20416	.26138
23	18.07471	.26636
24	17.94097	.27150
25	17.80274	.27682
26	17.65984	.28231
27	17.51224	.28799
28	17.35968	.29386

For monthly payments multiply by 1.01820; for quarterly payments multiply by 1.01488; for semi-annual payments multiply by 1.00990

TABLE "A"
(Continued)

1 Age	2 Annuity, or present value of $1.00 due at the end of each year during the life of a person of specified age	3 Reversion, or present value of $1.00 due at the end of the year of death of a person of specified age
	Annuity	*Reversion*
29	$17.20225	$0.29991
30	17.03961	.30617
31	16.87176	.31262
32	16.69846	.31929
33	16.51964	.32617
34	16.33503	.33327
35	16.14437	.34060
36	15.94755	.34817
37	15.74427	.35599
38	15.53421	.36407
39	15.31722	.37241
40	15.09295	.38104
41	14.86102	.38996
42	14.62122	.39918
43	14.37356	.40871
44	14.11860	.41852
45	13.85713	.42857
46	13.58958	.43886
47	13.31698	.44935
48	13.03942	.46002
49	12.75716	.47088
50	12.47032	.48191
51	12.17919	.49311
52	11.88408	.50446
53	11.58531	.51595
54	11.28325	.52757
55	10.97789	.53931
56	10.60982	.55116
57	10.35931	.56310
58	10.04630	.57514
59	9.73131	.58726

For monthly payments multiply by 1.01820; for quarterly payments multiply by 1.01488; for semi-annual payments multiply by 1.00990.

TABLE "A"

(*Continued*)

1	2	3
Age	Annuity, or present value of $1.00 due at the end of each year during the life of a person of specified age	Reversion, or present value of $1.00 due at the end of the year of death of a person of specified age
	Annuity	*Reversion*
60	$9.41474	$0.59943
61	9.09765	.61163
62	8.78052	.62382
63	8.46412	.63600
64	8.14888	.64812
65	7.83552	.66017
66	7.52476	.67212
67	7.21699	.68397
68	6.91298	.69565
69	6.61301	.70719
70	6.31716	.71857
71	6.02612	.72976
72	5.74003	.74077
73	5.45928	.75157
74	5.18402	.76215
75	4.91463	.77251
76	4.65125	.78264
77	4.39383	.79254
78	4.14286	.80220
79	3.89858	.81159
80	3.66071	.82074
81	3.42900	.82965
82	3.20258	.83836
83	2.98024	.84691
84	2.76106	.85534
85	2.54366	.86371
86	2.32795	.87200
87	2.11384	.88024
88	1.90115	.88842
89	1.69107	.89650
90	1.48540	.90441

For monthly payments multiply by 1.01820; for quarterly payments multiply by 1.01488; for semi-annual payments multiply by 1.00990.

TABLE "A"

(*Continued*)

1 Age	2 Annuity, or present value of $1.00 due at the end of each year during the life of a person of specified age	3 Reversion, or present value of $1.00 due at the end of the year of death of a person of specified age
	Annuity	*Reversion*
91	$1.28432	$0.91214
92	1.09024	.91961
93	.90647	.92667
94	.73687	.93320
95	.58435	.93906
96	.46182	.94378
97	.36698	.94742
98	.24038	.95229
99	.00000	.96154

For monthly payments multiply by 1.01820; for quarterly payments multiply by 1.01488; for semi-annual payments multiply by 1.00990.

TABLE "B"

1 Number of years	2 Present worth of an annuity of $1.00 payable at the end of each year, for a certain number of years	3 Present worth of $1.00 Payable at the end of a certain number of years
	Annuity	*Reversion*
1	$0.96154	$0.961538
2	1.88609	.924556
3	2.77509	.888996
4	3.62989	.854804
5	4.45182	.821927
6	5.24214	.790314
7	6.00205	.759918
8	6.73274	.730690
9	7.43533	.702587
10	8.11089	.675564
11	8.76047	.649581
12	9.38507	.624597
13	9.98565	.600574
14	10.56312	.577475
15	11.11839	.555265
16	11.65229	.533908
17	12.16567	.513373
18	12.65929	.493628
19	13.13394	.474642
20	13.59032	.456387
21	14.02916	.438834
22	14.45111	.421955
23	14.85684	.405726
24	15.24696	.390121
25	15.62208	.375117
26	15.98277	.360689
27	16.32958	.346816
28	16.66306	.333477
29	16.98371	.320651
30	17.29203	.308319

For monthly payments multiply by 1.01820; for quarterly payments multiply by 1.01488; for semi-annual payments multiply by 1.00990.

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(Reference is to question numbers)