COMBINED ANNUITY AND SINGLE PREMIUM LIFE INSURANCE UNDER THE ESTATE TAX: EFFECT OF ASSIGNING THE INSURANCE*

AGE and physical condition often preclude elderly persons from obtaining life insurance.[1] But many insurance companies offer to sell such individuals single premium policies without a medical examination on a condition which distinguishes such policies from orthodox insurance: the insured must relieve the company of the risk of early death by the simultaneous purchase of an annuity.[2] Although the single premium for the insurance part of such a

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* Bohnen v. Harrison, 199 F.2d 492 (7th Cir. 1952), *cert. granted*, 21 U.S.L. WEEK 3233 (U.S. Mar. 9, 1953).

1. All companies have age limits beyond which they will not issue ordinary life insurance despite medical fitness. Prudential Life Insurance Company of America, for example, has an age limit of seventy.

2. The following companies issue combination single premium life insurance and life annuity policies without medical examination:

	Ratio of Total Premium to Insurance Face Value	*Maximum Total Premium*
American National	variable	$ 50,000
Columbian National	110%	10,000
Continental Assurance	110%	110,000
Dominion Life	110%	110,000
Equitable, Iowa	110%	55,000
Great-West	107%	133,750
Life of Virginia	108%	54,000
Manhattan Life	110%	55,000
Manufacturers	108%	200,000
Occidental, California	107%	(a)
Ohio National	110%	27,500
Pan-American	110%	55,000
Prudential	110%	220,000
United States Life	110%	55,000

(a) $25,000 insurance plus the annuity.

From WHO WRITES WHAT (1952), a standard insurance reference.

These combinations have achieved considerable popularity. Prudential, for example, had 1,694 of these contracts in force on September, 1952, providing insurance totaling $31,209,818. Communication to the YALE LAW JOURNAL from James V. Hughes, Manager of the General Actuarial Division, Prudential Life Insurance Company of America, dated December 5, 1952, in Yale Law Library.

Some ordinary life insurance is also written without a medical examination. MACLEAN, LIFE INSURANCE 255-8 (7th ed. 1951).

For discussion of the difference between annuities and life insurance, see Cohen, *Annuities and Transfer Taxes*, 7 KAN. B.A.J. 139 (1938); Note, 26 VA. L. REV. 230 (1939).

In VANCE, INSURANCE §§ 1, 10 (3d ed. 1951) the contract of insurance is defined largely in terms of "risk," which is designated as one of th essential elements of an insurance contract. The insurance-annuity combination involves some risk, but not of an insurance nature; rather it is an investment risk—that incident to the management and investment of the insured's funds.

combination purchase is below the face amount of the policy,[3] the difference is more than made up by the amount paid for the annuity. In fact, total premiums paid for the combination usually equal about one hundred ten percent of the face value of the insurance policy.[4] If the insured dies before the insurance premium plus accrued interest equals the face value, the proceeds of the policy are paid partly from the unused balance of the annuity fund.[5]

Because the insurance-annuity combination thus differs from orthodox insurance, problems have arisen as to whether it should be treated as "insurance" for purposes of the federal estate tax.[6] In 1941, when life insurance proceeds up to $40,000 could be excluded from a decedent's gross estate,[7] the Supreme Court in *Helvering v. Le Gierse*[8] decided that the insurance part of such a combination was *not* "insurance" within the meaning of that statute. Indicating that the policy of the exemption was to promote insurance contracts which protect beneficiaries against the financial risk of the early death of those who support them, the Court found that such an element was absent from the combination. Since the presence of the annuity removed all elements of insurance risk,[9] the Court viewed the combined purchase as a "single investment"[10] and declared the exemption inapplicable.[11]

3. For an explanation of how net single premiums are computed, see MACLEAN, *op. cit. supra* note 2, at 96-101.

4. For list of companies see note 2 *supra.*

5. See discussion in Helvering v. Le Gierse, 312 U.S. 531, 541 (1941).

6. For discussion of some of the tax problems, other than the one considered by this Note, raised by the insurance-annuity combination and by annuities in general, see Meisenholder, *Taxation of Annuity Contracts Under Estate and Inheritance Taxes,* 39 MICH. L. REV. 856 (1941).

7. "The value of the gross estate . . . shall be determined by including the value . . . of all property . . . [t]o the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent of the excess over $40,000 of the amount receivable by all other beneficiaries as insurance under policies taken out by the decedent on his own life." Revenue Act of 1926, § 302(g), 44 STAT. 70 (1926), 26 U.S.C. § 411(g) (1935).

The first of these insurance-annuity combinations before the courts was one unit—a life annuity with a lump sum payable at death. That combination was denied the exemption because the necessary insurance risk was absent and it was considered as an investment with income reserved for life and with a remainder to the beneficiaries. Old Colony Trust Co. v. Commissioner, 102 F.2d 380 (1st Cir. 1939).

8. 312 U.S. 531 (1941). Estate of Keller v. Commissioner, 312 U.S. 543 (1941), and Tyler v. Helvering, 312 U.S. 657 (1941), dealing with the same problem, were decided the same day as *Le Gierse.*

9. See note 2 *supra.*

10. "Investment" is used here in the colloquial sense by which stocks and bonds are termed investments while insurance is not. Functionally, however, life insurance in contrast with indemnity insurance is a form of investment. See VANCE, INSURANCE 32, 65, 101, 105 (3d ed. 1951). Although the terminology may thus be inapt, the distinction is nevertheless a valid one. The exemption (see note 7 *supra*) applied specifically to "insurance"; it seems appropriate to have denied that exemption to other modes of saving "investments" which lacked the essential elements of insurance.

11. "To say they are distinct transactions is to ignore actuality . . . [They] fail to spell out any element of insurance risk." Helvering v. Le Gierse, 312 U.S. 531, 540-1

The exemption for insurance was removed from the estate tax in 1942;[12] hence no estate tax problem is now presented by the insurance-annuity combination so long as the insurance [13] is the property of the insured at death. The full proceeds of the insurance part of the combination will be included in the gross estate of a decedent whether the package be considered insurance or an investment.[14] But when by irrevocable assignment the insurance policy has been separated from the annuity,[15] the *Le Gierse* holding that the combination is not insurance troubles courts forced to decide whether to include the proceeds of the insurance in the gross estate of the insured. Taking the position that they cannot apply established criteria for handling orthodox insurance,[16] the courts undertake an analysis of the policy as an "investment."

In 1946 the Second Circuit in *Burr v. Commissioner* [17] included the insurance proceeds in the decedent's estate although the policies had previously been irrevocably assigned to certain beneficiaries.[18] The decedent purchased the

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(1941). Insurance contemplates shifting the economic risk of death to the insurer. When a combination policy is purchased, the insured himself covers that risk by buying the annuity.

12. The provision exempting the first $40,000 was omitted from the Revenue Act of 1942.

13. For the sake of convenience, this Note will continue to call the insurance part of the combination "life insurance," even though it may not technically qualify as "insurance" under the *Le Gierse* ruling.

14. The proceeds would be includible as property owned by the decedent at death under INT. REV. CODE § 811(a).

15. Under an irrevocable assignment all the legal incidents of ownership may be transferred. These include: the right to the economic benefits of the policy; the power to change the beneficiary; to surrender, cancel or assign the policy; to revoke an assignment; to pledge the policy for a loan, or to obtain a loan against the cash surrender value of the policy. See U.S. Treas. Reg. 80, art. 25 (1934).

16. From 1919 to 1942 INT. REV. CODE § 811(g) included in the estate the face value of policies "taken out by the decedent upon his own life." The Treasury Department, in part to appease the courts, inconsistently utilized two tests in determining whether a decedent had "taken out" a policy within the statutory meaning. One test measured includibility by whether the decedent paid the premiums; the other tests, by whether the decedent held "incidents of ownership" after the policy was transferred. For detailed descriptions of the antics of the Treasury in this connection, see Eisenstein, *Estate Taxes and the Higher Learning of the Supreme Court,* 3 TAX L. REV. 395, 514-21 (1948); Schlesinger, *Taxes and Insurance: A Suggested Solution to the Uncertain Cost of Dying,* 55 HARV. L. REV. 226, 230 (1941). The last Treasury Decision before the 1942 amendment removed the "taken out by the decedent" language, abandoned the incidents of ownership test. Insurance henceforth was to be includible if the decedent paid the premiums. T.D. 5032, 1941-1 CUM. BULL. 427.

INT. REV. CODE § 811(g)(2) specifies the criteria to be used today. See notes 27, 28 *infra*.

17. 156 F.2d 871 (2d Cir. 1946), *cert. denied*, 329 U.S. 785 (1946).

18. Estate of Cora C. Reynolds v. Commissioner, 45 B.T.A. 44 (1941), was the first case dealing with the general problem. The transferred policy was included in the decedent's estate as a transfer designed to take effect at death and in which the decedent had reserved a life income. In that case the policy was transferred to trustees.

combination when he was seventy-five. Shortly after the purchase, he made the transfer and paid a gift tax.[19] But the court considered the combination indivisible for estate tax purposes. Basing its decision on the *Le Gierse* rationale that this was a single investment, it found that the annuity payments constituted income from the entire investment package. Since the court felt that the decedent had reserved that income to himself for life, the arrangement was likened to an annuity with a life estate retained and with a remainder to be transferred at death. Thus it was held includible under Internal Revenue Code Section 811(c)(1)(B), which taxes as part of the estate transfers of property the income from which is reserved to the grantor for life.[20] In February, 1952, the Sixth Circuit in *Conway v. Glenn*[21] followed *Burr* in an indistinguishable fact situation.

On the other hand, the Seventh Circuit in *Bohnen v. Harrison*[22] recently held on facts almost identical to *Burr* that such irrevocably assigned insurance was *not* includible in the insured's estate. Mrs. Bohnen purchased the combination when she was sixty-two years old. Immediately after the purchase she assigned all her rights in the insurance policy to certain beneficiaries and paid a gift tax on the transfer.[23] The Seventh Circuit, affirming the district court's judgment for the taxpayer,[24] held that the insurance was separable from the annuity and that the assignment took the policy proceeds out of the decedent's estate. The court also ruled that the income reserved by retention of the annuity was traceable to the annuity only and not to the whole investment. The *Bohnen* court, therefore, squarely rejected *Burr*'s

19. The valuation of a one-premium life insurance policy for the gift tax is the cost at the time of the gift of acquiring a similar policy. U.S. Treas. Reg. 108, § 86.19(i) (1943). This is so even though the cash surrender value is smaller. Guggenheim v. Rasquin, 312 U.S. 254 (1941). The same basis for valuation is applied to a gift of the insurance part of an insurance-annuity combination, despite the fact that there is no ordinary insurance risk and the purchase of the annuity was required for purchase of the insurance. Letter of Deputy Commissioner D. S. Bliss, March 27, 1941, CCH Fed. Est. & Gift Tax Rep. ¶ 5478.55 (1946). The annuity purchase was merely a condition precedent to the purchase of the insurance, and not part of the consideration for the insurance.

The gift tax paid on a transfer which is later included in the estate may be credited against the estate tax. Int. Rev. Code § 813(a).

20. Burr v. Commissioner, 156 F.2d 871, 872 n.1 (2d Cir. 1946). Int. Rev. Code § 811(c)(1)(B) includes in the estate transfers "under which [the decedent] has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death . . . the possession or enjoyment of, or the right to the income from, the property. . . ."

21. 193 F.2d 965 (6th Cir. 1952).

22. 199 F.2d 492 (7th Cir. 1952), *cert. granted*, 21 U.S.L. Week 3233 (U.S. Mar. 9, 1953).

23. See note 19 *supra* for discussion of valuation of the transferred insurance for the gift tax.

24. Bohnen v. Harrison, 100 F. Supp. 118 (N.D. Ill. 1951). The district court based its decision on the fact that there had been no retained reversionary interest as there had been in Goldstone v. United States, 325 U.S. 687 (1945).

rationale and its extension of the *Le Gierse* doctrine; but the court accepted the conclusion that the insurance-annuity transaction constituted an "investment" rather than insurance. On March 9, 1953, the Supreme Court granted certiorari.

The *Bohnen* opinion appears justified in rejecting *Burr*'s application of *Le Gierse*. *Le Gierse* dealt only with the question of whether the insurance part of the combination was insurance within the purview of the estate tax exemption. No assignment had been made, and it was conceded that the whole package was includible unless exempt as insurance.[25] The *Le Gierse* holding that the combination was a single investment *when purchased* does not preclude a later splitting of that investment by assignment of the life insurance.[26]

The *Le Gierse* ruling could be restricted further and held wholly inapplicable to the type of question presented in the *Burr*, *Conway*, and *Bohnen* cases. In *Le Gierse* the Supreme Court pointed out that the exemption under consideration was designed to protect insurance contracts, which—by distributing losses—guard individuals against the risk of the premature death of those upon whom they depend for support. The policy behind *Le Gierse*, therefore, seems to be a recognition that protection of such persons is not furthered by the insurance-annuity combination, which in fact involves no distribution of individual losses. But such social policy provides no basis for distinguishing the *assigned* insurance portion of a combination from assigned orthodox insurance in order to include it within the gross estate under Section 811(c).[27] In the hands of assignees, both policies would be precisely the same. And identical treatment for the policies in no sense would permit taxpayers to defeat any legislative policy geared to the special "insurance risk" nature of the transaction. Present legislative policy is designed to include almost all insurance in the gross estate. But *assigned* insurance is included in the gross estate only if the decedent had "incidents of ownership" in the policy either at death or after January 10, 1941, whichever was earlier, or if he originally took out the policy on his own life after that date.[28] In

25. Helvering v. LeGierse, 312 U.S. 531, 537-8 (1941).

26. The annuitant's rights are also assignable in the absence of a condition to the contrary in the annuity contract. RESTATEMENT, CONTRACTS §§ 151, 155 (1932). In the *Burr* case, for example, the annuity was assignable. Transcript of Record, p. 28, Burr v. Commissioner, 156 F.2d 871 (2d Cir. 1946).

27. According to INT. REV. CODE § 811(g)(2) the value of the gross estate is determined by including proceeds of life insurance "receivable by . . . other beneficiaries ... [and] purchased with premiums ... paid ... by the decedent, in proportion that the amount so paid by the decedent bears to the total premiums paid for the insurance . . . or with respect to which the decedent possessed at his death any of the incidents of ownership, exercisable either alone or in conjunction with any other person."

28. Section 811(g) of the Code is to be applied as provided by § 404(c) of the Revenue Act of 1942:

"The amendments . . . shall be applicable only to estates of decedents dying after the date of the enactment of this Act [October 21, 1942]; but in determining the proporthose limited situations where insurance is still excluded from the gross estate, therefore, the exclusion is based entirely on the fact of assignment. By surrender of the "incidents of ownership" of the policy, the decedent is considered to have made a present gift of the policy, with no economic interest passing at his death.[29] Thus in *Bohnen* the Supreme Court could, without logical inconsistency, distinguish *Le Gierse*: it could continue to treat the insurance-annuity combination as failing to contain those elements of "insurance risk" needed to qualify for the pre-1942 insurance exemption; at the same time, it could handle the assigned insurance portion of the combination in the same manner as orthodox insurance for the purpose of determining whether it should be included in the gross estate under Section 811(g)(2)(A). Under the facts of the *Bohnen* case, such treatment as true insurance would probably lead to exclusion of the proceeds from the gross estate. But it would provide a far more realistic and workable solution to the tax problem raised by the combination than present tortuous attempts to fit the transaction into an "investment" category.

The *Burr* rationale that the annuity payments represent income from the total investment appears highly unrealistic. The annuity could have been purchased alone—even though the insurance could not have been purchased without the annuity—and the income therefrom would have been the same.[30] And if the insurance policy had been cashed in by the beneficiaries, no change would have resulted in the annuity payments.[31] In viewing the existence of the power to cash in the policies as immaterial because unexercised, *Burr* failed to consider the significance of the immutability of the annuity payments as evidence of their source.[32] Further evidence of the independence of the

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tion of premiums paid . . . by the decedent . . . the amount so paid . . . on or before January 10, 1941 [the effective date of T.D. 5032, 1941-1 CUM. BULL. 427], shall be excluded if at no time after such date the decedent possessed an incident of ownership in the policy."

According to U.S. Treas. Reg. 105, § 81.27 (1943) if the decdent died on or before October 21, 1942 the excess of such insurance over $40,000 is included: "To the extent to which such insurance was taken out by the decedent upon his own life after January 10, 1941, and . . . [t]o the extent to which such insurance was taken out by the decedent upon his own life on or before January 10, 1941, and with respect to which the decedent possessed any of the incidents of ownership . . . after such date, or, in the case of a decedent dying on or before such date, at the time of his death."

29. Ballard v. Helburn, 9 F. Supp. 812, 814, 815 (W.D. Ky. 1933), *aff'd*, 85 F.2d 613 (6th Cir. 1936). See also Flick's Estate v. Commissioner, 166 F.2d 733 (5th Cir. 1948).

30. The annuity and the life insurance are treated as independent contracts by the insurer. The premiums are the same as if the policies were purchased separately. The reserves are calculated separately. Each is a single independent contract on its face. See Meisenholder, *Taxation of Annuity Contracts under Estate and Inheritance Taxes*, 39 MICH. L. REV. 856, 883 (1941). See also Conway v. Glenn, 97 F. Supp. 331, 332 (W.D. Ky. 1951).

31. Meisenholder, *supra* note 30, at 883.

32. *Burr* declared the combination to be "analogous to a simple annuity with principal payable at death," citing Commissioner v. Clise, 122 F.2d 998 (9th Cir. 1941), *cert.*

annuity payments from the insurance is the fact that the dividends from the insurance policies themselves were paid directly to the beneficiaries as holders of the policies without regard to the ownership of the annuity.[33] Moreover, when this question was raised in an income tax context the payments were held to derive only from the annuity and not from the whole investment.[34]

Closeted in the conclusion that income was retained from the whole "investment," *Burr* did not find significant the fact that a gift of real value was

denied, 315 U.S. 821 (1942), and Commissioner v. Wilder's Estate, 118 F.2d 281 (5th Cir.), *cert. denied,* 314 U.S. 634 (1941), as support for the taxability of such annuities to the estate. Burr v. Commissioner, 156 F.2d 871, 872 (2d Cir. 1946). The *Clise* case, however, concerned "joint and survivor non-participating annuity contracts" and not an annuity with principal payable at death. *Wilder* also concerned survivorship annuities.

The annuity with principal payable at death is the kind considered in Old Colony v. Commissioner, 102 F.2d 380 (1st Cir. 1939). See Note 7 *supra.* Such an annuity is not divisible for surrender purposes because the contract is one unit. See Meisenholder, *supra* note 30, at 884. By contrast, the insurance-annuity combination may be divided and the insurance surrendered. See note 30 *supra.*

There are also refund and cash refund annuities. Under the refund annuity, the insurer continues payments on the annuity after the annuitant's death until the total payments equal the original purchase price. The cash refund type of annuity contract provides that at death the excess of original premium paid over total annuity payments will be paid immediately in cash. Such annuities give a lower yield than the straight life annuities where there is no refund and payments terminate at death. MACLEAN, *op. cit. supra* note 2, at 51-2.

33. In fact such payments are not "dividends" in the same sense as dividends paid on corporate stocks. They are merely an adjustment of the premium cost. Weeks v. Commissioner, 16 T.C. 248, 255 (1951); MACLEAN, *op. cit. supra* note 2, at 158-87.

34. In one case the Commissioner tried to tax as income the amount annually received from the investment. The Tax Court held that under § 22(b)(2)(A) only the amount calculable as interest on the purchase price of the annuity was taxable as income—the rest being recognized as a return of capital—and that the component parts of the investment should be regarded separately in determining the receipts attributable to each. Koehrer v. Commissioner, 4 T.C.M. 219 (1945). *Cf.* Helvering v. Meredith, 140 F.2d 973 (8th Cir. 1944) (annuity payments taxed as annuities under § 22(b)(2)(A) and life insurance dividends not taxed until they exceed aggregate premiums paid).

INT. REV. CODE § 22(b)(2)(A) provides: "Amounts received as an annuity . . . shall be included in gross income; except that there shall be excluded . . . the excess of the amount received in the taxable year over an amount equal to 3 per centum of the . . . premiums . . . until the aggregate amount excluded . . . equals the . . . premiums. . . ." The same section also excludes amounts received as dividends from an insurance policy until such payments exceed the premiums paid.

This section recognizes the fact that annuity payments represent a return of principal with interest. The 3% figure is used because it is assumed that at least that much of the return represents interest and therefore should be taxable income. U.S. Treas. Reg. 111, § 29.22(b)(2)-2 (1943). The tax in effect seems to be a 6% tax because figured each year on the basis of the *original premium,* part of which is consumed each year. See Comment, 11 TEMP. L.Q. 567, 568 (1937).

Under U. S. Treas. Reg. 105, § 81.18 (1942), when a transferor retains the income from a part only of transferred property only "a corresponding portion of the value of the property should be included." It would seem, therefore, that under this regulation the insurance proceeds are not includible.

completely transferred before the death of the insured. The insured received no income from the transferred insurance policies, since the only distributed income was represented by the insurance dividends, which the beneficiaries received. Nor did he retain any reversionary interest.[35] And no additional powers over the original gift passed to the beneficiaries by reason of the transferor's death.[36] The inclusion of the transferred portion of the "investment" under Section 811(c)(1)(B)[37] therefore seems unwarranted. The transfer was merely one way of making a gift that could have been in cash. If this had been done no estate tax issue would have arisen and the gift would have been subject only to the lower gift tax even under the *Burr* reasoning.[38] A similar amount might also have been transferred by giving property outright of the same value. Moreover, if the transferees had exercised their power to cash in the life insurance policies they would have been in the same position as if they had initially received cash. So long as the insurance proceeds are viewed as part of an "investment," there seems to be no valid reason for penalizing those transferees who do not elect immediately to realize the present cash value of the investment transferred to them.

Although the *Burr* "investment" analysis therefore appears erroneous in view of the factual nature of the transaction involved, *Bohnen*'s holding that *all* the proceeds of the insurance policy paid at death are completely exempt is also open to objection. The *Bohnen* court looked exclusively at the techniques of the transaction. Noting that the insurance and the annuity

35. In Goldstone v. United States, 325 U.S. 687 (1945), the transferor reserved the right to the return of the policies if he survived the beneficiaries. Pointing out that this was not insurance under the *Le Gierse* ruling, the Court held it includible in the gross estate as a transfer "intended to take effect in possession and enjoyment at . . . death." The Court decided the question merely on the basis of the decedent's possession of the reversionary interest; it found it unnecessary to reach the question of whether or not there was retained income—the problem which the courts discussed almost exclusively in the *Burr*, *Conway*, and *Bohnen* cases.

36. The gift had a value when transferred, and the transferor's death in no way affected that value. The fact that death resulted in an addition to the original gift did not change the beneficiaries' power over the original gift.

Even after the policy matures at death, it may be left intact with the company which will pay interest thereon. MACLEAN, *op. cit. supra* note 2, at 583-7. In that case, the policy must still be "cashed in" in order for the beneficiaries to realize its value—just as the policy could have been cashed in prior to death to realize the value of the original gift.

37. For text of section, see note 20 *supra*.

38. The federal gift tax rate is only about three quarters of the estate tax rate. Although the difference was originally explained on the basis of the fact that the taxes were enacted at different times, many subsequent reasons have been given. The present rate was first enacted in 1932. Some thought the lower rate would encourage the transfer of personal wealth during life. See Representative Crisp's remarks of March 10, 1932, in 75 CONG. REC. 5691 (1932); Harriss, *Legislative History of Federal Gift Taxation*, 18 TAXES 531, 536 (1940); Magill, *The Federal Gift Tax*, 40 COL. L. REV. 773, 776, 791 (1940).

were independently handled, it excluded all proceeds from the estate. But such treatment does not take account of the fact that the donees at the insured's death received a second gift—measured by the difference between the value of the policy just prior to death and the face value.

Within the framework of the present policy of refusing to treat the insurance part of a combination purchase as "insurance," a better approach than either *Burr* or *Bohnen* would include in the decedent's estate that part of the insurance proceeds which the beneficiaries actually receive as a result of death. Such an amount could be included under Section 811(c)(1)(C) of the Code, which taxes as part of the estate transfers "intended to take effect . . . at . . . death." Neither *Burr* nor *Bohnen*, which rested on an interpretation of Section 811(c)(1)(B),[39] considered that provision. Yet a reasonable view of the transaction seems to place it within the scope of that section. As the annuity payments are made, decreasing the annuity principal, the lump sum insurance premium held by the insurance company increases in value through investment earnings. The increase in the cash surrender value of the policy reflects this rise in value.[40] At death the annuity payments cease and the face amount of the insurance policy is paid to the beneficiaries. The difference between the value of the original insurance premium plus accrued interest just before death and the face value of the policy is covered by the remaining annuity principal.[41] The initial gift of the policy could be viewed as the transfer of a liquid security which might be converted into cash at any time before death. And the annuity could be considered as a trust from which the settlor reserves yearly payments for life, with the remaining corpus to be used to pay the face value of the insurance policy if the policy is not converted before the settlor's death. Thus regarded, the original gift would not be included in the estate because it is complete before death and enjoyment can be realized at any time by surrender of the policy; the trust—measured by the difference between the cash surrender value of the policy just before death and its face value[42]

39. For text of section, see note 20 *supra*.

40. For some time after an insurance policy is first written the cash surrender value is lower than the original lump sum premium because of the "loading factor"—the amount added to the net premium to cover the cost of administration, and to give a surplus for unanticipated losses. VANCE, INSURANCE 67 (3d ed. 1951); see also KNIGHT, ADVANCED LIFE INSURANCE, 127-46 (1926). For an example of how the cash surrender value rises yearly see Transcript of Record, p. 23, Burr v. Commissioner, 156 F.2d 871 (2d Cir. 1946).

41. This is true at least in the situation where the decedent does not outlive his life expectancy. If he lives "too long," of course, no annuity principal will remain—since it will have been consumed by the annual payments. The essential point, however, for the *Le Gierse* decision is that the initial risk of the insured dying soon was eliminated by the purchase of the annuity. After many years, when the annuity principal is gone, the investment earnings of the insurance policy will have made up the difference between the insurance premium and its face value.

42. The cash surrender value should be the value used for the tax purpose here because that is the only value actually realizable to the assignees. Unfortunately this

—would be included, however, for that is the economic interest which shifts to the beneficiaries as a result of death and so falls within the terms of Section 811(c)(1)(C).

Should the Supreme Court in deciding *Bohnen* accept the view that *Le Gierse* precludes it from treating the assigned policy as insurance, the Court would face at least three alternatives in handling the transaction under Section 811(c): it could affirm the Seventh Circuit's holding that none of the proceeds are includible in the gross estate; it could reverse the Seventh Circuit and adopt *in toto* the rationale of the *Burr* opinion; or it could attempt to split the proceeds so as to include within the estate only that real economic interest which actually passes at death to the beneficiaries. Within an investment rationale, the last approach appears most closely in harmony with the factual realities of the case. But all involve a difference in tax treatment between assigned orthodox insurance and assigned portion of an insurance-annuity combination that is, perhaps, unwarranted.

The Court also has the alternative of distinguishing *Le Gierse* and handling the combination in *Bohnen* as true insurance under Section 811(g). The sole reason for presently denying such treatment appears to be *Le Gierse*'s previous determination that the combination in the hands of the purchaser at death should be denied special tax advantages then given by Congress for the purpose of stimulating the purchase of orthodox insurance. Since that public policy justification is applicable only to the special pre-1942 insurance exemption and is absent where the question merely involves proper treatment of the *assigned* insurance portion of a combination, this 811(g) solution appears most equitable.

might involve a double tax on the difference between the cash surrender value at death and the value upon which the gift tax was paid since the cash surrender value at death might still be lower than the gift tax basis. For explanation of gift tax evaluation see note 19 *supra*; for full explanation of cash surrender value basis, see VANCE, INSURANCE 73-4 (3d ed. 1951). Some credit, however, may be allowed for the gift tax paid. INT. REV. CODE § 813(a).