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SUPREME COURT OF THE UNITED STATES

October Term 2010

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COMMISSIONER OF INTERNAL REVENUE

Petitioner

v.

No. 2010-15

Estate of Inka Pleat

Respondent

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On Writ of Certiorari to the Court of Appeals

For the Thirteenth Circuit

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**BRIEF FOR THE RESPONDENT**

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**BRIEF FOR THE RESPONDENT**

## **QUESTION PRESENTED**

1. Whether a member of a distribution committee for a trust possesses a general power of appointment when the power cannot be exercised except with the unanimous agreement of the distribution committee or with the agreement of the grantor of the trust.
2. Whether a grantor creates a general power of appointment when the grantor did not complete the gift of property to the trust because he retained both testamentary control over the property and the power to limit the class of beneficiaries.
3. Whether the Commissioner of the Internal Revenue Service may, after the Service has issued and published private letter rulings stating its position of not finding a general power of appointment for distribution committee trusts, find a general power of appointment and tax the trust property to a member of a distribution committee when the settlor created the trust in reliance upon the private letter rulings' decisions.

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## STATEMENT OF THE CASE

In 2006, Kantcom Pleat (hereafter “the Grantor”) created a trust seemingly modeled after several I.R.S. private letter rulings. (R. at 2, 7). The trust created a three-person distribution committee, one member of which was Inka Pleat, the Grantor’s daughter. The trust provided, in pertinent part, that the trustees hold and manage the trust property; making distributions to a limited class of beneficiaries consisting of the Grantor, the Grantor’s spouse, the Grantor’s siblings, and the Grantor’s descendants. The trust further provided that the trustees could only distribute trust property as directed by the unanimous agreement of all members of the distribution committee, or by the unanimous agreement of the Grantor and one member of the distribution committee. (R. at 2-3). According to the trust the Grantor reserved the power of testamentary appointment and the ability to further limit the class of beneficiaries, but at any time he could release this power. (R. at 3). In the event that such power has not been exercised by the time of the Grantor’s death, the trust principal and income were to be distributed to the Grantor’s descendants per stirpes. (R. at 3). If no descendants were living, the trust property was to go to the descendants of the Grantors parents and to qualified charitable organizations. (R. at 3). The Distribution Committee initially included the Grantor’s sister Dora and the Grantor’s son David, in addition to Ms. Pleat. The trust required that there must be three members of the distribution committee at all times, and if one member should predecease the Grantor, the then-living oldest descendent of the Grantor who is also a beneficiary will become the successive member. (R. at 3).

The private letter rulings, containing essentially the same language as the Grantor’s trust, established that (1) there was no completed gift on the establishment of the trust, (2) the trust was

not a grantor trust for income tax purposes, and (3) members of the distribution committee did not have a general power of appointment. (R. at 7).

Ms. Pleat suddenly died on January 2, 2007, and since the Grantor was still alive, his next eldest son John became the third member of the distribution committee. (R. at 3). It was at this time that the IRS Commissioner, the petitioner, declared a deficiency on Ms. Pleat's estate, the respondent herein, for not including a one-third share of the trust property in the gross estate. (R. at 4).

The executor for Ms. Pleat's estate petitioned the Tax Court for a redetermination of the deficiency. The Tax Court applied I.R.C. §2041(b)(1)(C)(ii) and ruled in favor of Ms. Pleat's estate, deciding that the members of the Distribution Committee had substantially adverse interests and therefore there was no general power of appointment. (R. at 4).

The Commissioner then appealed the Tax Court's decision and the case was heard by the United States Court of Appeals for the Thirteenth Circuit. The Thirteenth Circuit affirmed the Tax Court's decision that there was no general power of appointment, but did so under I.R.C. § 2041(a)(2). The Court's rationale was that the trust property was not required to be included in the gross estate because, at the time of her death, the Grantor had not made a completed gift. (R. at 4-5).

Judge Madden filed a concurring opinion in which he agreed with the majority's determination that the estate should not include the trust property, but did so based upon the principle that the IRS owes a duty of consistency to taxpayers because of the explanation of tax consequences discussed in private letter rulings issued between 2005 and 2007. (R. at 6). The Commissioner then filed for a writ of certiorari with this Court.

### **SUMMARY OF THE ARGUMENT**

The I.R.S. Commissioner improperly assessed an estate tax deficiency against Inka Pleat's estate by including one-third of the value of the trust property after determining that Ms. Pleat held a general power of appointment. The Internal Revenue Code (I.R.C.), regulations to the Code, and I.R.S. publications do not support the finding that a general power of appointment exists for an individual who is a member of a distribution committee when the individual can only act in accordance with the grantor of the trust or with the other members of the distribution committee who have a substantial interest adverse to the interest of the individual. The Code, regulations, and publications also do not support a finding that a general power of appointment exists when there has been no complete gift of power from the grantor. Lastly, the I.R.S. has a duty to act in a way that is consistent to positions taken in its publications when a taxpayer has relied and acted upon such a positions.

Ms. Pleat, as a member of the distribution committee, did not have a general power of appointment because she only had the power to distribute trust income and principal with the agreement of all other members of the distribution committee or with the agreement of the Grantor, all of whom had substantial interests adverse to the interest of Ms. Pleat. A member of the distribution committee, wanting to distribute funds to herself, could do so with the agreement of the other two members and therefore receive a one-third share of the trust property. The same member, however, could distribute funds to herself with the agreement of the Grantor and therefore receive a one-half share of the trust property. Because of this incentive to act in opposition to the Grantor and the other members of the distribution committee, each member of the distribution committee had a substantial interest that was adverse to the interests of not only each other, but also the Grantor. Due to the existence of these adverse interests, there could not have been a general power of appointment under the Internal Revenue Code.

Ms. Pleat also could not have had a general power of appointment because there was not a completed gift from the grantor. The I.R.C. does not require that gifted property be taxed to the donee's estate if the donor did not complete the gift of the property. When a donor retains control of the property, there is not a completed gift. Equitable considerations require that the same piece of property cannot be taxed to more than one individual at the same time. Mr. Pleat retained the power to control the distribution of the trust property through testamentary appointment and the ability to limit the class of beneficiaries. Because of this there was no complete gift of the trust property, and therefore, Ms. Pleat did not have a general power of appointment at the time of her death.

The construction of Mr. Pleat's trust is very similar to that of the trusts laid out in IRS private letter rulings. These rulings state that members of the distribution committee do not have a general power of appointment due to the adverse interests, and that there was no completed gift on the establishment of the trust. Since Mr. Pleat's trust was set up in reliance on the IRS published rulings, it would not be fair for the Service to reverse its position and conclude that a general power of appointment and a completed gift be found in such circumstances. The findings of the Tax Court and the Thirteenth Circuit Court of Appeals should be affirmed and the deficiency against Ms. Pleat's estate should be set aside.

### **ARGUMENT**

**I. DECEDENT DOES NOT HAVE A GENERAL POWER OF APPOINTMENT, AS THE POWER OF APPOINTMENT IS EXERCISABLE ONLY IN CONJUNCTION WITH A PERSON HAVING A SUBSTANTIAL INTEREST WHICH IS ADVERSE TO THE POWER OF THE DECEDENT.**

Section 2041(a)(1) states that "any property with respect to which the decedent has at the time of death a general power of appointment . . . would be includible in the decedent's gross

estate.” I.R.C. § 2041(a)(1). The code then goes on to define the term “general power of appointment” as “a power which is exercisable in favor of the decedent, his estate, his creditors, or the creditors of his estate.” *Id.* at §2041(b)(1). It at first may appear that the decedent would have a general power of appointment in this case, but section 2041(b)(1)(C) provides two exceptions. The first exception is that there is no power of appointment if the power is exercisable by the decedent only with the consent of the creator of the power. The second exception states that if the power of appointment is only exercisable “in conjunction with a person having a substantial interest in the property, subject to the power, which is adverse to exercise of the power in favor of the decedent – such power shall not be deemed a general power of appointment.” *Id.* at §2041(b)(1)(C)(ii).

Ms. Pleat did not have a general power of appointment in the instant case, as both of the exceptions previously mentioned are met. The decedent could exercise her power with the two other members of the distribution committee, or alternatively with the Grantor of the trust. According to the letter sent by the ABA in response to IR 2007-127, the first exception mentioned above “forecloses treating either member of the distribution committee as holding a general power of appointment with respect to the ability of a distribution committee member to exercise the power of appointment together with the grantor of the trust creating the power.” ABA Comments: *Incomplete Gift Response*, 2007 TNT 195-41 (Sept. 26, 2007). The more difficult issue is determining whether the other committee members’ interests are adverse to those of the decedent under the second exception. While the Revenue Rulings discussed in the record conclude that there is a general power of appointment, the private letter rulings interpret trusts almost identical to that of the Grantor in the present case as having no general power of appointment. As the language of Mr. Pleat’s trust matches the language in the PLRs and the

rulings of the PLRs can be distinguished from the Revenue Rulings, there is no general power of appointment and decedent's estate should not include her proportion of the trust property.

In each of the PLRs listed in the record, a trust was established in which a distribution committee could make decisions by acting unanimously or if one distribution committee member acted together with the grantor. If one of the members of the distribution committee were to die before the grantor, a successor (typically the oldest living descendent), would serve as a replacement member of the committee. In determining whether there was a general power of appointment, the Service recognized that the members of the committee had the power to distribute trust income and corpus, but that they could not act on their own. *E.g.*, I.R.S. P.L.R. 200502014 (Jan. 14, 2005), I.R.S. P.L.R. 200612002 (March 24, 2006), I.R.S. P.L.R. 200637025 (Sept. 15, 2006), I.R.S. P.L.R. 200647001 (Nov. 24, 2006), I.R.S. P.L.R. 200715005 (April 13, 2007), I.R.S. P.L.R. 200729025 (July 20, 2007), I.R.S. P.L.R. 200731019 (Aug. 3, 2007). In an example where B, C, and D are members of a distribution committee and A is the grantor of the trust, B's power can only be exercised with the consent of C or D, or with the consent of A. Likewise, C's power can only be exercised with the consent of B or D, or with A. The same can be said for D. On the death of B, C, or D, the deceased's power "will devolve to the surviving committee members and A jointly (and a new committee member will be appointed)." I.R.S. P.L.R. 200729025. The ruling goes on to state that B, C, and D do not have a general power of appointment "by reason of the joint distribution power." *Id.*

The Revenue Rulings, Ruling 76-503 in particular, focuses on the fact that since a distribution committee member is replaced upon death, the interests of the other members do not change. The Service relies primarily on the example provided in Regulation 20.2041-3(c)(2), where if X, Y, and Z hold a joint power and one dies, the power will pass to the other two

members jointly. Treas. Reg. § 20.2041-3(c)(2). Because the deceased member is not replaced and the surviving members will each increase their share, the members have an incentive not to allow other members to exercise their power when alive. The example further provides that if the deceased member's power does not pass to the remaining members jointly, then they are not considered to have an adverse interest. *Id.* In applying this reasoning to the facts of Revenue Ruling 76-503, the Service found that the members of the distribution committee had “no interest in the subject property other than as co-holders . . . ,” and because of this there did not exist an adverse interest. Rev. Rul. 76-503, 1976-2 C.B. 275.

The apparent inconsistency between the Revenue Rulings and the PLRs can be attributed to the fact that the trust provisions considered by the Service in the Revenue Rulings and the PLRs were different, and therefore yielded opposing results. The greatest difference between the revenue rulings and the PLRs is that the trust in the revenue rulings allowed committee members to appoint a relative as a successor should he or she die. While this may not seem too impactful on the surface, it makes sense that a committee member who can decide who will follow in his or her position (and who will most likely actually distribute the trust property), is exercising a power of appointment. The ABA also thought this difference relevant, as it not only “left little opportunity for any trustee to gain economic advantage,” but also allowed the appointed relatives to act as “alter egos” and still make distributions in the decedent's favor. ABA Comments: *Incomplete Gift Response.*

The Service's comments in the regulations also imply that succession to the interest of a deceased committee member is only one example of an additional economic interest which is considered adverse. The ABA refers to the X, Y, Z example listed above as “simply an illustration,” and asserts that if the Service intended that the only way to achieve adversity was

through succession to power it would have “simply stated this as a requirement.” *Id.* In further support of the idea that one can be adverse without succeeding to power, the ABA points to examples 1 and 2 of the regulation for section 2514 (the gift tax counterpart to section 2041). In both of these examples, the co-holders have other economic interests in the trust which by themselves make the co-holders adverse. *Id.*

Despite the fact that the distribution committee members of the trust in the present case do not succeed to power upon the death of another committee member, they are still adverse. Succession is merely one way to prove adversity, and is not a requirement in order to reach the conclusion that there is no general power of appointment. Unlike the distribution committee in the revenue rulings, the distribution committee of Mr. Pleat’s trust cannot appoint a relative as a successor, and therefore an economic interest remains in the surviving members. The distribution committee members could decide to cooperate with one another and each take a one-third share, but they each have the additional option of making an agreement with the Grantor through which one of committee members could receive at least one-half of the trust property. Since one member of the distribution committee may be able to secure at least part of the interest belonging to the other members, there exist adverse interests.

Because a member of the distribution committee can only make decisions with the consent of the Grantor or with the unanimous consent of the others members of the distribution committee who have a substantial and adverse interest in the trust property, there is no general power of appointment.

**II. THE TAX ASSESSED ON MS. PLEAT’S ESTATE WAS IMPROPER BECAUSE THE GRANTOR’S GIFT WAS INCOMPLETE.**

The tax assessed on Ms. Pleat’s estate was improper because the Grantor’s gift was incomplete. The Grantor did not complete the gift because he retained control over the trust property, and a general

power of appointment cannot exist until the transfer of the property subject to the power of appointment is complete for gift or estate tax purposes. Because the Grantor's gift was not complete, the trust property was includable in the Grantor's estate. If Ms. Pleat was considered to have a general power of appointment, the trust property would also be includable in her estate and this would be inequitable because the same piece of property would be taxable to two or more persons at the same time. Since the grantor did not complete the gift to the trust, Ms. Pleat did not have a general power of appointment and it was improper for the Commissioner to assess a deficiency against her estate. The appellate court's ruling should be affirmed and no part of the trust property's value should be included in Ms. Pleat's estate.

A. A Gift Is Not Complete Until The Donor No Longer Has Control Of The Trust Property.

A gift is not complete until the donor no longer has control of the trust property. The Supreme Court of the United States held that a donor's gift is not complete, for the purposes of the gift tax, when the donor has reserved the power to determine those others who would ultimately receive the property. *Sanford's Estate v. Comm'r*, 308 U.S. 39, 43 (1939). This ruling is in line with regulations to the Internal Revenue Code, which provide that the gift must be completed before a gift tax is imposed; i.e. the donor must have parted with dominion and control so as to leave in him no power to change the disposition of the gift. Treas. Reg. § 25.2511-2(b). The regulations further explain that a gift is incomplete if the donor reserves a power to name new beneficiaries or to change the interests of the beneficiaries as between themselves unless the power is a fiduciary power limited by a fixed or ascertainable standard. Treas. Reg. § 25.2511-2 (c). According to the regulations, the donor's relinquishment of a power to change the beneficiaries of transferred property, occurring otherwise than by death of the donor, is regarded as the event which completes the gift and causes the gift tax to apply. Treas. Reg. § 25.2511-2(f)

The Service applied the above regulations in private letter rulings when it concluded that a transfer to a trust was not a complete gift where the taxpayer retained limited powers to appoint the trust property to family members excluding himself. I.R.S. P.L.R. 9536002 (May 12, 1995). An irrevocable

transfer to the trust was not a completed gift because the taxpayer continued to possess dominion and control over the property transferred to the trust. The Service explained that the gift would be complete upon the occurrence of any of the following events:

1) Taxpayer's or Spouse's exercise (to any extent) or relinquishment of (to any extent) his or her power of appointment; 2) any action by the trustees that would effectively terminate Taxpayer's or Spouse's power of appointment with respect to any part of the Trust property (including the trustees' distribution of income or principle to anyone other than Taxpayer and Spouse); and 3) any action or failure to act by the trustees with respect to any part of the Trust property whereupon it is no longer accounted for in the Trust.

*Id.* If none of these events occurred, a gift is not complete and it would be improper to consider the property as belonging, and thus taxable, to any member of the distribution committee.

The Grantor's gift was not complete under the first event specified in P.L.R. 9536002 because he did not relinquish his control over the property held in trust. The above private letter ruling is consistent with the Supreme Court's holding in *Burnet v. Guggenheim*, 288 U.S. 280 (1933). In *Guggenheim*, a taxpayer created a trust but reserved for himself the power of revocation. Later the taxpayer relinquished his power to revoke, but this relinquishment occurred after Congress had passed the Revenue Act of 1924, which included a tax upon gifts. The Commissioner assessed a gift tax upon the transfer to the trust, and the taxpayer responded that the gift was complete prior to the passage of the gift tax, and therefore it was improper for the tax to be so assessed. The court held that, for taxation purposes, the crux is the command over the property, and that while the taxpayer had the power to revoke, the gift was imperfect. The gift did not become complete until the taxpayer relinquished his power of revocation. *Id.* at 283-284.

Like the trust in *Guggenheim*, the trust property in Ms. Pleat's estate was still subject to the power of the Grantor. The Grantor retained not only the right to distribute the income and principal of the trust if he acted in conjunction with only one member of the distribution committee, but also the right to limit the class of allowable beneficiaries. (R. at 3). By retaining such powers, the Grantor effectively had the right of revocation since he could restrict the class of beneficiaries or he could, in conjunction with one member of the distribution committee, pay out the entire corpus of the trust. The Grantor never relinquished these reserved powers, and therefore the gift was never complete.

Though the distribution committee did have the power to act without the Grantor, this power to act required the unanimous agreement of all its members. Since the grantor retained the ability to distribute the trust property with the agreement of only one member of the distribution committee, his power was much greater than that of the distribution committee's members.

The gift was also not complete under the second or third events named in P.L.R. 9536002 because there was no action by the trustees that terminated the Grantor's power over the trust property, nor did the trustees act or fail to act in a way that caused the trust property to no longer be accounted for in the trust. In fact, the trustees did not have the ability to terminate the Grantor's power over the trust property. According to the terms of the trust, the trustees had only the power to manage and pay the income and principal of the trust as the distribution committee by unanimous agreement appointed, or as the Grantor with a member of the distribution committee agreed. (R. at 2-3). Since there was no power in the trustees to terminate the Grantor's power over the trust and the property remained accountable in the trust, the gift could not have been made complete by action of the trustees.

Since the Grantor retained control over the property held in trust and there was no action by the trustees that either took away the Grantor's power or depleted the property held in trust, the Grantor's gift was not complete, and therefore it was improper to find that Ms. Pleat had a general power of appointment and to include the trust property's value in her estate.

**B. Only One Person May Be Taxed At One Time With Respect To Ownership In Specific Property.**

Only one person may be taxed at one time with respect to ownership in specific property. For Ms. Pleat's estate to be taxed, it must not be taxable to another individual at the same time. If a transfer is not considered complete for gift tax purposes, but each distribution committee member is treated as having a general power of appointment, trust property would be includable in the estates of two or more people simultaneously. N.Y. City Bar Comments of Gift Tax Consequences of Trusts Employing Distribution Committee, Doc 2007-23077, 2007 TNT 200-10 (Oct. 16, 2007). Since the trust property

was still under the control of the Grantor, it was taxable to his estate and therefore could not have been taxable concurrently to Ms. Pleat's estate.

It is logical to only tax one person at a time on a specific piece of property since it would not be equitable for a person to have to pay taxes on property which cannot be enjoyed because it is under the control of another person. This concept is supported by the Internal Revenue Code in provisions relating to estate tax, gift tax, and in other areas of tax law. Since the Grantor retained control over the trust property it should not have been included in Ms. Pleat's estate.

I.R.C. § 2040(a), which discusses joint interests under estate law, provides that a gross estate must only include the portion of interest that the decedent had in the property. A joint tenant does not need to include in his or her estate the part of the joint tenancy that may be shown to have originally belonged to another person and never to have been acquired by the joint tenant for consideration. In a situation where A jointly owned property with B and A predeceased B, A does not need to include the value of the property if A furnished no part of the purchase price of the property, but must include the entire value of the property if A furnished the entire purchase price, or the portion of the value equal to the portion of the purchase price that A furnished. Treas. Reg. § 20-2040-1(c)(1)-(3). The rule is sensible, since it would not be equitable for a person to be taxed on property that he or she did not own.

Gift tax law states that the event that completes a gift and causes the tax to apply is the grantor's relinquishment of the power to change the disposition of the property so gifted. Treas. Reg. § 25-2511-2(f). This regulation also follows the principals of equity, since it would not be fair for the donee to be taxed on a gift over which the donor could still exercise control.

Other areas of tax law also support the principle of only one individual being responsible for taxes on a specific piece of property at one time. The Internal Revenue Code states that no other person shall be treated as the owner of trust property if the grantor of the trust is treated as the owner. I.R.C. § 678(b). The important issue is deciding ownership, and once the owner of the property is determined, only the owner can be taxed for the value of the property.

Although an I.R.S. revenue ruling concerning a defeasible remainder interest left to an individual who later died has been relied on to support a conclusion that a specific piece of property may be taxed to more than one person at the same time, this interpretation is in error. Rev. Rul. 67-370, 1967-2 C.B. 324. The grantor of the defeasible interest later revoked it after the donee died, but the value of the interest was included in the donee's estate nonetheless. This revenue ruling involves circumstances where the interest is clearly identifiable because only the fair market value of the defeasible interest was included in the deceased's estate. The value of a defeasible interest would naturally be less than the value of a fee simple interest. Because the value of the defeasible interest is automatically adjusted in the free market, it may be bought and sold with the understanding that the grantor may subsequently revoke. The gift of a defeasible interest was complete and it was only the value of the defeasible interest that was taxed. As such, the defeasible interest was always separate property from the grantor's right of revocation and so this revenue ruling does not contradict the principle that only one person may be taxed for one piece of property at a time.

*Johnstone v. Commissioner*, 76 F.2d 55 (9th Cir. 1935), discusses a trust created by a mother leaving to her son a general power of appointment over the trust corpus. The son predeceased his mother and the court ruled that the value of the trust was includible in the deceased's estate despite the fact that the mother had reserved the right to modify the trust instrument. *Id.* at 56, 59. *Johnstone*, however, did not hold that the same piece of property could be taxable to two people consecutively. Rather, since the mother did not reserve the right to revoke the trust and the trust document required that the corpus be distributed at the son's death according to his will, the gift was complete at the son's death. *Id.* at 56. Because there was a completed gift, the property would no longer be within the mother's control and therefore would not be includible in her gross estate.

The tax on Ms. Pleat's estate is dissimilar to the tax applied in Rev. Rul. 67-370, as the interest that she had in the trust was not clearly set forth like that of the revenue ruling. Her interest in the estate could be quantified as one-third if considering her interest in relation to the other members of the distribution committee, or her interest could be quantified as one-half if considering her interest with

respect to that of the Grantor. Also, unlike a defeasible remainder, as considered in the revenue ruling, Ms. Pleat's membership in the distribution committee was not transferable by her. Since she could not sell her interest, it would have no determinable value and therefore, unlike the result of the revenue ruling, there would be no value to include in her estate.

Likewise, Ms. Pleat's estate is distinguishable from the estate in *Johnstone*. The control that the Grantor, Ms. Pleat's father, had over the trust property did not end with Ms. Pleat's death like the control of the grantor in *Johnstone*. Because the Grantor of Ms. Pleat's power still has the power to exercise control even after her death, this gift was not complete. Ms. Pleat's interest was not transferable and she had no control over the distribution of the property held in trust after her death. In fact, at her death the limited power that was granted to her transferred to the Grantor's then eldest living descendant who was not already a member of the distribution committee. (R. at 3). Had there been a completed gift like there was in *Johnstone*, Ms. Pleat's estate would have had control over the distribution of the property held in trust. Since there was no completed gift, Ms. Pleat's estate is distinguishable to the deceased's estate in *Johnstone*.

Since only one person may be taxed on the same piece of property at the same time, and since the Grantor's gift was not complete, the Grantor was still the owner of the trust property, and the trust property should not have been included in Ms. Pleat's estate.

**III. THE PRIVATE LETTER RULINGS RELIED UPON BY THE RESPONDENT, MAKING IT APPEAR THAT THE DECEDENT DID NOT HAVE A POWER OF APPOINTMENT, SHOULD BE CONSIDERED AND CANNOT BE DISREGARDED BY THE COURT DUE TO THE NEED FOR THE SERVICE TO BE CONSISTENT IN ITS DECISIONS.**

The principles set forth in the Private Letter Rulings, upon which the Grantor relied when drafting the trust, should not be disregarded in the present case, as they have been relied upon by the creators of trusts such as the one addressed in this brief. The IRS should be held to the same standards as both taxpayers and other government agencies, and as a result it should be required to be consistent in how it treats each individual taxpayer.

The concept of consistency is critical to the validity of the justice system. To be consistent is to be fair, which is why a taxpayer duty of consistency has developed over the years. The duty of consistency, as it applies to taxpayers, dictates that if the Commissioner relies on a representation made by a taxpayer, he can continue to rely on that representation after the statute of limitations has expired even if the original representation was incorrect. The premises underlying this rule are that “a taxpayer must normally accept the tax consequences of the way in which he deliberately chooses to cast his transactions,” and that “what is done in one tax year is sometimes projected into another where the same fact must govern. There being continuity, there ought to be consistency in treatment.” *Sterno Sales Corp. v. United States*, 345 F.2d 552, 554 (Ct. Cl. 1965); *Alamo National Bank of San Antonio v. Comm’r*, 95 F.2d 622, 623 (5th Cir. 1938). The duty of consistency was adopted by the Tax Court in *Estate of Ashman v. Commissioner*, 231 F.3d 541 (9th Cir. 2000). The Court held that “the duty of consistency not only reflects basic fairness, but also shows a proper regard for the administration of justice and the dignity of the law,” and that once a taxpayer has “transfigured” true facts, he cannot “reshape them at will.” 231 F.2d at 546.

Because the duty of consistency can be credited to the desire for fairness and justice, there is no reason why the IRS should not be held to the same standard. Yet the pattern of consistency displayed by the Service over the years can only be described as inconsistent. While the Sixth Circuit has held that the duty of consistency only applies against the taxpayer, the District Court for the Eastern District of New York has held that the Commissioner owes “a duty of consistency in his interpretation of the regulations until he has notified the taxpayer that a new rule will be applied . . . .” *Temple v. Comm’r*, 62 F. App’x 605, 609 (6th Cir. 2003); *Conway Import Co. v. United States*, 311 F.Supp 5, 14 (E.D.N.Y. 1969).

Perhaps the most well-known case pertaining to a duty of consistency for the IRS is *International Business Machines Corp. v. United States*, 343 F.2d 914 (Ct. Cl. 1965). In *IBM*, the IRS had granted a favorable ruling for a competitor of IBM but refused to issue a similar ruling in favor of IBM, which resulted in IBM having to pay \$11 million in taxes that its competitor was exempt from. The problem with the Service's determination was that it treated similarly situated taxpayers differently. In discussing the power of the Service to use its power of discretion, the court decided that the IRS needed to contemplate the "comparative or differential effect on the other taxpayers in the same class." 343 F.2d at 920. The court further remarked that "equality of treatment is so dominant in our understanding of justice that discretion, where it is allowed a role, must pay the strictest heed." *Id.*

Although subsequent cases held *IBM* to its facts and limited the duty of consistency, the Court of Federal Claims, in 2001, issued a decision broadening the notion of consistency when it held that "one situation in which the Commissioner's actions may constitute an abuse of discretion is when similarly situated taxpayers are treated differently without a rational basis for the disparate treatment." *Computer Sciences Corp. v. United States*, 50 Fed. Cl. 388, 393 (2001). This decision took *IBM* one step further, as it did not just find an abuse of discretion under section 7805 of the Internal Revenue Code, but in all cases where the IRS treated similarly situated individuals differently. Stephanie Hoffer, *Hobgoblin of Little Minds No More: Justice Requires an IRS Duty of Consistency*, Utah L. Rev. 317, 331 (2006). As with the *IBM* decision, subsequent cases limited the interpretation set forth in *Computer Sciences*, but the Second Circuit, in *Sirbo Holdings, Inc. v. Commissioner*, 476 F.2d 981, 987 (2d Cir. 1973), recognized the duty of consistency towards similarly situated taxpayers, as well as an entitlement "to a non-discriminatory administration of the tax laws."

In the present case, the respondent requests that the Court hold the Service to a duty of consistency as it pertains to private letter rulings. In describing the general principles behind private letter rulings, Duke University School of Law professor Lawrence Zelenak writes:

A taxpayer about to engage in a transaction can request a letter ruling to obtain the Service's view of its tax consequences. Since 1954, the Service has ordinarily permitted recipients of letter rulings to rely on those rulings. If the Service later determines the ruling was in error, it will exercise its discretion under 7805(b) to make its revocation of the ruling prospective only, thus protecting the reliance interest of the recipient of the ruling.

Lawrence Zelenak, *Should Courts Require the Internal Revenue Service to be Consistent?*, 40 Tax L. Rev. 411, 435 (1985). While prior to 1976 PLRs were kept confidential, the Tax Reform Act of 1976 and section 6110 provided for "public inspection of private letter rulings and other written determinations of the Service . . . ." 40 Tax L. Rev. at 436. Zelenak points out that private letter rulings since 1976 are "numerous, readily obtainable, thoroughly indexed, and represent the Service's considered views on the merits of the questions of law addressed." *Id.* at 434. Because the private letter rulings are so easily accessible, it seems that the Service is inviting taxpayers to rely on them to anticipate the way the Service will interpret specific Code provisions.

Despite the Internal Revenue Code's statement that a private letter ruling may not be used or cited as precedent, this does not mean that these rulings have no purpose nor does it mean that the courts do not consider them in ruling on cases. I.R.C. § 6110(k)(3). In *Hanover Bank v. Commissioner*, 369 U.S. 672 (1962), the Supreme Court considered private letter rulings as persuasive evidence and stated, "although the petitioners are not entitled to rely upon unpublished private rulings which were not issued specifically to them, such rulings do reveal the interpretation put upon the statute by the agency charged with the responsibility of administering the revenue laws." 369 U.S. at 686. The Supreme Court recognized private letter

rulings as having evidentiary value in *Rowan Companies, Inc., v. United States*, 452 U.S. 247 (1981). In deciding if an employee benefit should be considered income, the Court cited private letter rulings and held that while they did not have any precedential value, they could be used as “evidence of the Service’s actions.” 452 U.S. at 262 n.17. This proposition from *Rowan* was relied upon by the Ninth Circuit in *Niles v. United States*, 710 F.2d 1391 (9th Cir. 1983), when showing that the Service had not previously required allocation of damages. The Sixth Circuit also consulted private letter rulings to aid in deciphering the language of a trust in *Comerica Bank v. United States*, 93 F.3d 225 (6th Cir. 1996).

The Court of Claims also used private letter rulings in *Xerox Corp. v. United States*, 656 F.2d 659 (Ct. Cl. 1981). In ruling that the company could take a credit for its machines provided to governments and tax-exempt organizations, the court did not even mention section 6110(k)(3). Instead it stated, “we have the right to consider the Service’s rulings, both formal and informal, in the light of the facts we have found on this record.” 656 F.2d at 660. The court further noted that “[t]hough private letter rulings have no precedential force, they are helpful, in general, in ascertaining the scope of the ‘service’ doctrine adopted by the Service and in showing that that doctrine has been regularly considered and applied by the IRS.” *Id.* n.3.

Additional support for an IRS duty of consistency is that the Service itself relies on private letter rulings when it is deciding how to rule on current taxpayer inquiries. This practice began before the enactment of section 6110(k)(3), and it has continued after. 40 Tax L. Rev. at 439-440. Rulings considered to have “reference value for internal purposes” are kept in a reference file along with revenue rulings and court decisions, and then indexed. *Id.* at 439. IRS personnel consult and rely on these files to find “underlying authority and reasoning” when faced with similar situations. *Id.* If the Service is able to confer with its previously published private

letter rulings to aid in deciding current issues, it would seem illogical to prohibit taxpayers from consulting these rulings as an indication of the Service's position on a specific issue.

The IRS should be held to a duty of consistency for any decision, regulation, or ruling it issues. To hold differently would be both unfair and inefficient, as inconsistent decisions “injure the public's confidence in the Service” and “result . . . in inaccurate collection of revenue.” Utah L. Rev. at 345. Inconsistency makes it more difficult for taxpayers to understand an already complicated tax system, and if taxpayers are unable to rely on the published rulings of the IRS they may be discouraged from seeking the Service's advice. *Id.* Additionally, permitting inconsistency allows the Service's wrongs to go uncorrected, since “[w]here the service treats two similarly situated taxpayers differently, there is no question that it fails to uphold the revenue laws with respect to one of them.” *Id.*

Opponents of an IRS duty of consistency assert that the Service should not be held to previous decisions once it realizes that they are incorrect. But the IRS can be consistent and still renounce previous rulings, as the duty of consistency “should not be applied so rigidly as to prohibit an agency from correcting a mistake or making a reasoned change of policy.” 40 Tax L. Rev. at 413. As the Second Circuit stated, “If the Service is willing to renounce its inconsistent precedents, the goals of the consistency requirement have been achieved.” *Sirbo Holdings, Inc. v. Comm'r*, 509 F.2d 1220, 1222 (2d Cir. 1975). Because the Service is able to change its position if needed, the duty of consistency would not bind the IRS to previous rulings to its detriment.

In the case at hand, the decedent should be able to rely on the decisions included in the private letter rulings, as the Grantor most likely relied on these rulings in establishing the trust. Evidence in support of this assumption is that the language of the trust is identical or very similar

to that of the trusts in the PLRs. The fact that the trust in question was established in 2006 and the PLRs were published between 2005 and 2007 provides further evidence of reliance. Since the revenue rulings upon which the Commissioner based his decision to assess the deficiency against Ms. Pleat's estate were issued in the 1960s and 1970s, it would be logical for a taxpayer to rely on readily available, current rulings as opposed to those that are decades old in order to ascertain the Service's current position on the tax laws.

The PLRs gave the Grantor an expectation that the distribution committee members would not hold a general power of appointment and that the property in the trust did not constitute a complete gift. The Grantor was justified in his expectation and reliance because he adhered to the construction of the trusts exemplified in the PLRs and modeled the language so as to achieve a similar result. It would be an abuse of justice to allow the Service to change its position and subject Ms. Pleat's estate to unanticipated and unfair tax treatment.

### **CONCLUSION**

For the foregoing reasons the judgment of the Court of Appeals should be upheld, and the deficiency assessed against the Respondent's estate should be set aside.