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Subject: Policy Proceeds Are Includible In Gross Estate of Insured Who Retained Right to Change Beneficiary

Major References: [*Estate of Coaxum v Commissioner, T.C. Memo 2011-135*](#)

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The U.S. Tax Court, in Estate of Coaxum v Commissioner, T.C. Memo 2011-135), has determined that a decedent retained incidents of ownership in six life insurance policies, causing their proceeds to be includible in his gross estate under Internal Revenue Code section 2042. In addition, the Court held that the value of certain annuities owned by the decedent were similarly includible in the gross estate, but, in this instance, pursuant to section 2039.

The life of the decedent (“Decedent”), was insured by seven insurance policies that provided death benefits. One of these policies had no value when Decedent dies and therefore was not involved in this litigation. Decedent possessed the power to change the beneficiaries on all six of the remaining insurance policies until he died. At his death, Decedent also owned annuities with a value of \$472,956.

Decedent’s estate tax return, which was tardily filed (more than two and a half years after his death), initially reported that the values of the six insurance policies were includible in the gross estate at the following values:

Life Insurance Co. of North America	\$500,000
Metropolitan Life Insurance Co.	\$56,000

Life Insurance Co. of North America	\$116,000
State Farm Life Insurance Co.	\$51,077
Monumental Life Insurance Co.	\$227,500
<u>Metropolitan Life Insurance Co.</u>	<u>\$336,000</u>
Total	\$1,286,577

The return reported that the annuities were includible in the gross estate at a value of zero.

In the notice of deficiency, the government determined that the six insurance policies should be included in the gross estate using the values reported, with relatively minor dollar amount variances. The notice of deficiency thus stated that the includible value of insurance on the decedent's life was \$1,283,184. The notice of deficiency also determined that the annuities owned by the decedent at his death should be included in his gross estate at a value of \$472,956.

In an amended petition subsequently filed with the Tax Court, Decedent's estate - apparently having second thoughts - claimed (in addition to contesting the inclusion of the annuities) that the insurance policies should not have been included in the estate.

The Court ruled that the Decedent retained an "incident of ownership" in the six policies through his retention of the right to change the beneficiaries. Under section 2042(2), life insurance proceeds are includible in the estate of the insured to the extent that the insured possessed, directly or indirectly, one or more incidents of ownership in the policy. Under applicable Treasury regulations, the power to change the beneficiary is such an incident of ownership.

The Court also determined that the annuities (with a value of \$472,956) were includible in Decedent's gross estate under section 2039(a). The Court noted the Taxpayer's argument that the beneficiary of the annuities (Decedent's brother), who included the annuity payments in gross income as "income in respect of a decedent," should be able to deduct the amount of Federal estate tax paid on the annuities as an offset against his income tax. It refused to so rule, however, because it had no jurisdiction over the income tax liability of that beneficiary.

The Court also assessed a "failure to file" penalty equal to 25 percent of the net estate tax due.

Any AALU member who wishes to obtain a copy of *Estate of Coaxum v. Commissioner* that is noted in our "Major References" description may do so through the following means: (1) use hyperlink above next to "Major References," (2) log onto the AALU website at www.aalu.org and enter the *Member Portal* with your last name and birth date and select *Current Washington Report* for linkage to source material or (3) email Anthony Raglani at raglani@aalu.org and include a reference to this *Washington Report*.

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