

THE EFFECT OF SAVINGS BOND REGULATIONS ON INTER VIVOS GIFTS BETWEEN CO-OWNERS

The problem of how to make a valid inter vivos gift of United States Savings Bonds has troubled the courts for some time.¹ This problem often arises when an individual purchases United States Savings Bonds during his lifetime and has them issued in co-ownership form,² that is, in his name "or" another's. Subsequently, the individual delivers possession of these bonds either to the other registered co-owner or to a third party, fully intending to make an irrevocable gift. The bonds are never surrendered or re-issued in the manner prescribed by the Treasury regulations.³ Thereafter, the donor dies. The question is thus presented as to whether these bonds are taxable in the individual's estate.

The issue to which this article is addressed is narrow: What is the effect of the Treasury Department Regulations governing United States Savings Bonds upon inter vivos gifts of bonds between co-owners? More specifically, can a co-owner of United States Savings Bonds divest himself of sufficient rights of ownership to exclude the bonds from his estate at death by an inter vivos manual delivery of the bond to the other registered co-owner with the intention of making an irrevocable gift?

The I.R.S. takes the position that the bonds can be transferred, so as to remove them from the donor's estate, *only* by surrendering the bonds and having them reissued in the name or names of the other joint owners in accordance with the Treasury Department Regulations which are a part of the contract between the government and the purchaser of United States Savings Bonds.

The taxpayer argues that the regulations which require surrender and reissuance of the bonds govern only the rights of the holder of the bonds as against the government. The taxpayer points out that when bonds are issued in co-ownership form, each co-owner becomes vested with a present interest in the bonds and has a right of survivorship. Either co-owner can obtain the proceeds from the bonds at any time since both names appear on the bonds. In addition, the taxpayer argues that the Treasury Depart-

1. See 40 A.L.R.2d 788 (1955).

2. 31 C.F.R. § 315.7(a)(2) (1966) provides: "Coownership form—two persons (*only*). In the alternative as coowners. Examples: John A. Jones 123-45-6789 or Mrs. Ella S. Jones. Mrs. Ella S. Jones or John A. Jones 123-45-9876. No other form of registration establishing coownership is authorized."

3. 31 C.F.R. § 315.61 (1966).

ment Regulations do not regulate the rights of co-owners as between themselves.

The focal point of controversy revolves around a 1958 Third Circuit Court of Appeals decision, *Silverman v. McGinnes*.⁴ In that case, the decedent, during his lifetime, bought some United States Savings Bonds which were issued each in the amount of \$1,000. Some of the bonds were registered as payable to him and his wife as co-owners; others were payable to him and one or the other of his children as co-owners. The decedent delivered the bonds to his wife stating that they were outright gifts to her and the children respectively. He confirmed this gift to her in writing. However, the bonds were never re-issued in the names of the respective donees. The district court held the bonds includible in his estate on the theory that the registration created a conclusive presumption of their ownership.

The court of appeals reversed and concluded that the transaction was the equivalent of an express trust even though trust terms were not used.⁵ The gross estate of a trustee does *not* include property over which he holds mere title without the right to beneficial enjoyment.⁶ The decedent had given up all economic interests in the bonds prior to his death "and in the words of the Internal Revenue Code of 1939, the extent of the interest therein held by the decedent was nothing."⁷ Therefore, the taxing statute was not applicable.⁸

The bond regulations applicable to the controversy state that "the registration used or issue or reissue must express the actual ownership of and interest in the bond and . . . will be considered as conclusive of such ownerships and interest."⁹ The bonds "are not transferrable and are payable only to the owners named thereon, except as specifically provided in the regulations, and then only in the manner and to the extent so provided."¹⁰ "Conflicting claims as to ownership of, or interest in, such bond as between co-owners . . . will be recognized, when established by valid judicial proceedings . . ."¹¹ However, "[n]o judicial determination will be recognized which would give effect to an attempted voluntary

4. 259 F.2d 731 (3rd Cir. 1958).

5. *Id.* at 734.

6. *Reed v. Commissioner*, 36 F.2d 867 (5th Cir. 1930); *LOWNDES AND KRAMER, FEDERAL ESTATE AND GIFT TAXES* 33 (1956).

7. 259 F.2d at 734-35.

8. Int. Rev. Code of 1939, § 811(e), 26 U.S.C. 811(e) (1948).

9. 31 C.F.R. § 315.5 (1966).

10. 31 C.F.R. § 315.15 (1964).

11. 31 C.F.R. § 315.20(a) (1964).

transfer inter vivos of a bond or would defeat or impair the rights of survivorship conferred by the regulations upon a surviving co-owner or beneficiary"¹²

The issue thus becomes clear. What is the effect of the regulation stating that "no judicial determination will be recognized which would give effect to an attempted voluntary transfer inter vivos of a bond"?¹³

There has been substantial agreement that the regulations do not purport to provide the manner in which controversies are to be determined between persons interested in the disposition of the bonds.¹⁴ Indeed, the regulations relate "to payment by the United States Government and [have] nothing to do with the ultimate rights of the parties to the funds."¹⁵ If the government makes payment to either of the joint owners, this discharges the government from further liability. However, the rights of the owners of the bonds, as between themselves, remain unaffected.¹⁶

"The contract between the Government and the purchaser of the Government bonds fixes legal title to the bonds for the purpose of protecting the Government against suits involving title, but does not and should not affect other legal rights of third parties or change settled rules of law not necessary to effectuate its purpose."¹⁷ The regulations are designed for the convenience and protection of the government. They are only for the purpose of facilitating and handling matters between a bond holder and the department.¹⁸ "It seems clear that the federal laws and regulations are not intended to interfere with the positive act of two co-owners of bonds by which one conveys her interest in them to the other."¹⁹

"The Treasury commonly has no concern with the funds or their disposition once it has paid them to the registered owner. Its contract has then been fulfilled."²⁰ The Supreme Court of Wisconsin has noted that "[t]he regulations do not extend to the use

12. *Id.*

13. *Id.*

14. *Moore v. Brodrick*, 123 F. Supp. 108 (D. Kan. 1959), *aff'd*, 226 F.2d 105 (10th Cir. 1965); *In re Prevost's Est.*, 172 N.Y.S.2d 924 (1958); *Tonner v. Ervin*, 250 N.C. 602, 109 S.E.2d 460 (1959); *Byer v. Byer*, 180 Kan. 258, 303 P.2d 137 (1956).

15. *In re Est. of Spitters*, 24 Utah 2d 372, 472 P.2d 426, 427 (1970).

16. *See In re Neglia's Est.*, 403 Pa. 464, 170 A.2d 357 (1961).

17. *Moore v. Brodrick*, 123 F. Supp. 108, 109 (D. Kan. 1954), *aff'd*, 226 F.2d 105 (10th Cir. 1955).

18. *Byer v. Byer*, 180 Kan. 258, 303 P.2d 137 (1956).

19. *In re Hendricksen's Estate*, 159 Neb. 463, 56 N.W.2d 711, 719 (1953).

20. *District of Columbia v. Wilson*, 216 F.2d 630, 633 (D.C. Cir. 1954).

of the proceeds of the bonds but stop with payment."²¹ The "Treasury department regulations . . . have not, by their terms or in necessary effect, granted the bonds or their proceeds immunity from the implied trust doctrine. . . ."²² In light of this reasoning, courts have often imposed a trust on proceeds from bonds.²³

Although there is survivorship between co-owners of savings bonds,²⁴ which is characteristic of a common law joint tenancy, it is clear that ownership of savings bonds is not a pure form of joint ownership. One co-owner has the power at any time to unilaterally terminate the complete interest of the other co-owner by simply cashing the bonds.²⁵ This characteristic seems to give jointly owned savings bonds some of the earmarks of joint bank accounts.²⁶

Between two co-owners of a bond it is a question of fact as to the extent of property interest of each co-owner.²⁷ "One co-owner may as a matter of fact be the sole owner of a bond; he may be a half owner; he may have some other fractional ownership."²⁸ Each co-owner holds a present vested though defeasible interest.²⁹ However, it is a question of fact and not law³⁰ that the extent of a co-owner's property interest is to be determined by the courts.³¹

When courts are dealing with inter vivos gifts of bonds, the rule set out by the *Silverman* court is often recognized.³² However, the estate always has the burden of showing an irrevocable divestiture of the potential right of survivorship by the decedent.

21. *In re Massouras' Estate*, 16 Wis. 2d 304, 114 N.W.2d 449, 452 (1962).

22. *Id.*

23. *Anderson v. Benson*, 117 F. Supp. 765 (D. Neb. 1953); *In re Neglia's Est.*, 403 Pa. 464, 170 A.2d 357 (1961); *In re Chase's Est.*, 82 Ida. 1, 348 P.2d 473 (1960); *Alexander v. Mermel*, 27 Ill. App. 2d 281, 169 N.E.2d 569 (1960); *Tanner v. Ervin*, 250 N.C. 602, 109 S.E.2d 460 (1959); *Roman v. Smith*, 228 Ak 833, 314 S.W.2d 225 (1958); *Tharp v. Besozzi*, 144 N.E.2d 430 (1957); *Bell v. Killian*, 266 Ala. 12, 93 So. 2d 769 (1957); *In re Barletta's Estate*, 2 Misc. 2d 135, 150 N.Y.S.2d 479 (1965).

24. 31 C.F.R. § 315.62 (1964).

25. 31 C.F.R. § 315.60 (1964).

26. *In re Barletta's Estate*, 150 N.Y.S.2d 479, 484 (1956).

27. *Keyes v. Keyes*, 171 So. 2d 489 (1965).

28. *In re Hayes*, 407 F.2d 1031, 1035 (6th Cir. 1969).

29. *Broderick v. Moore*, 226 F.2d 105 (10th Cir. 1955); *Succession of Weis*, 162 So. 2d 791 (1964).

30. *In re Hayes*, 407 F.2d 1031 (6th Cir. 1969).

31. *United States v. Stockyards Bank of Louisville, Kentucky*, 231 F.2d 628 (6th Cir. 1956).

32. *Estate of Chrysler v. C.I.R.*, 361 F.2d 508 (2d Cir. 1966); *Estate of Chrysler*, 44 T.C. 55 (1965); *Estate of Avery*, 40 T.C. 392 (1963); *Estate of Boogher*, 22 T.C. 1167 (1954).

Where the taxpayer fails to prove this intention, unconditional delivery alone is insufficient.³³

In 1969, the *Silverman* rule was rejected by the Sixth Circuit Court of Appeals in *Estate of Curry v. United States*.³⁴ The *Curry* case was factually on all fours with *Silverman*. It is the position of the Government and the *Curry* court that the reasoning and conclusion of *Silverman* flies in the face of the federal regulations dealing with United States Savings Bonds.³⁵

Unfortunately the *Curry* court did not elaborate on the position set out above, but based its disagreement with *Silverman* upon a previous rule set out in the Sixth Circuit in *Guldager v. United States*.³⁶ The previous rule was that rights and estates in the United States Savings Bonds were created by federal contract and were, therefore, controlled by federal law.³⁷ It should be noted that the *Guldager* rule does not conflict in the least with the *Silverman* rule. Moreover, the *Silverman* decision recognizes the fact that federal law regulates the matter.³⁸ In any event, the *Curry* decision has created a split of authority in the circuit courts—a result which is most unsettling to the taxpayer.

There was no indication by the *Curry* court that co-owner transactions between themselves differed from bond owner transactions with parties not named on the bonds themselves. The cases relied upon by the Sixth Circuit in support of its decision

33. *Estate of Avery*, 40 T.C. 392 (1963); *Estate of Boogher*, 22 T.C. 1167 (1954).

34. 409 F.2d 671 (6th Cir. 1969).

35. The government relies mainly on the following provisions of the Treasury Regulations:

1. "The [form] of registration used . . . must express the actual ownership of and interest in the bond" 31 C.F.R. § 315.5.
2. "The [form of] registration . . . will be considered as conclusive . . . [of the registered co-owner's] ownership and interest [in the bond]" 31 C.F.R. § 315.5.
3. "Savings Bonds . . . are payable only to the owners named thereon. . . ." 31 C.F.R. § 311.5.
4. "Savings bonds are not transferrable" 31 C.F.R. § 315.15.

The government further argues that the reissuance provisions of the regulations provide the sole manner in which a decedent may divest himself of his rights of ownership in the bonds during his lifetime. See also, Brief for Appellant, *Chandler v. United States*, Civ. No. 26,085, at 31-40, 54-55.

36. 204 F.2d 487 (6th Cir. 1953).

37. *Id.* at 489.

38. 259 F.2d at 733. "It is not denied that these regulations which are of long standing have the force of law. The question, however, is the scope of their application [T]he question to be faced is whether these regulations include not only the rights of the holder of the bond as against his Government, the debtor, but also whether they determine the rights of individual citizens against each other arising out of transactions with these Government bonds." (emphasis added).

involved situations in which the decedent had attempted to make a gift to a person who was not one of the "owners named thereon."³⁹ This distinction is important when the regulations are read as a whole.⁴⁰

The majority of state court decisions dealing with inter vivos gifts of bonds involve attempted transfers to persons who were not named on the bonds,⁴¹ in other words, transfers to strangers to the bonds. The vast majority of these cases hold that the attempted gift is ineffective.⁴² However, there is authority to the contrary.⁴³

Of the state court decisions dealing directly with the question of transactions exclusively between co-owners,⁴⁴ the majority hold in favor of the taxpayer.⁴⁵ In *Littlejohn v. County Judge*,⁴⁶ savings bonds were registered in the name of the decedent "or" his daughter as co-owners. The decedent delivered possession of these bonds to his daughter. His daughter then placed them in a safety deposit box which was registered in her name only. The decedent had no access to the bonds, and they were intended to be a gift to the daughter for her use whenever she needed them. The court said that "[f]rom the time of delivery the decedent had no right to or interest in the bonds which he might legally enforce."⁴⁷ "There is nothing in the regulations to prohibit the transfer from one co-owner to the other of his interest in the

39. 31 C.F.R. 315.15 (1964).

40. See *Chandler v. United States*, 312 F. Supp. 1263 (N.D. Cal. 1970), at 1268.

41. *O'Dell v. Garrett*, 82 N.M. 240, 478 P.2d 568 (1970); *In re Touchstone's Est.*, 18 Misc. 2d 966, 191 N.Y.S.2d 9 (1959); *Moore's Adm.'r v. Marshall*, 302 Ky. 729, 196 S.W.2d 369 (1946); *Bunch v. Hulsey*, 302 Ky. 763, 196 S.W.2d 373 (1946); *Gans v. Gans*, 277 App. Div. 903, 98 N.Y.S.2d 466 (1950); *Hatfield v. Buck*, 193 Misc. 1041, 85 N.Y.S.2d 613 (1948); *In re Tonkin's Est.*, 65 N.Y.S.2d 484 (1946); *In re Nettle's Est.*, 91 N.Y.S.2d 255 (1949); *In re Hackett's Est.*, 113 N.Y.S.2d 688 (1952); *In re Cook's Est.*, 193 Misc. 261, 82 N.Y.S.2d 755 (1948); *Collins v. Jordan*, 110 N.E.2d 825 (1949).

42. *Id.*

43. *In re Klarfeld's Est.*, 237 N.Y.S.2d 424 (1963).

44. *In re Prevost's Est.*, 11 Misc. 2d 725, 172 N.Y.S.2d 924 (1958); *In re Brown's Est.*, 122 Mt. 451, 206 P.2d 816 (1949); *Weeks v. Johnson*, 146 Me. 371, 82 A.2d 416 (1951); *Littlejohn v. County Judge*, Pembina County, 79 N.D. 550, 58 N.W.2d 278, 39 A.L.R.2d 690 (1953); *In re Hendricksen's Estate*, 159 Neb. 463, 56 N.W.2d 711 (1953).

45. In favor of taxpayer: *In re Prevost's Est.*, 11 Misc. 2d 725, 172 N.Y.S.2d 924 (1958); *In re Hendricksen's Estate*, 159 Neb. 463, 56 N.W.2d 711 (1953); *Littlejohn v. County Judge*, Pembina County, 79 N.D. 550, 58 N.W.2d 278, 39 A.L.R.2d 690 (1953); *In re Brown's Est.*, 122 Mt. 451, 206 P.2d 816 (1949); Against the taxpayer: *Weeks v. Johnson*, 146 Me. 371, 82 A.2d 416 (1951).

46. 79 N.D. 550, 58 N.W.2d 278, 39 A.L.R.2d 690 (1953).

47. *Id.* at 283.

bond.”⁴⁸ “Our decision is . . . neither contrary to nor does it interfere with the regulations of the Treasury Department pertaining to the purchase, transfer, and payment of Series E and G Bonds.”⁴⁹

The key word in the co-ownership bond controversy appears to be “transferable.” The taxpayer contends that the term refers to a transfer “*by one or more of the registered co-owners to strangers to the bond, i.e., to persons who are not ‘owners named thereon.’*”⁵⁰ When one looks to the context in which the word is used in the regulations it appears that the taxpayer is correct. In the regulations, § 315.15 provides that “Savings Bonds are not transferable and are payable only to the owners named thereon. . . .” Clearly the term transfer refers to persons who are not “owners named thereon.”

In a recent case, *Chandler v. United States*,⁵¹ involving the same facts as both *Silverman* and *Curry*, the District Court for the Northern District of California noted that a transfer between co-owners was not a “transfer inter vivos of the bond.”⁵² Therefore, its judicial determination excluding the bonds from the decedent’s estate would not be giving effect to any such “transfer” as contemplated by the regulations.⁵³ The court went on to note that neither “would the judicial determination here involved ‘defeat or impair the rights of survivorship . . . [of] a surviving co-owner.’ On the contrary, the rights of the surviving registered co-owner are here recognized and effectuated”⁵⁴ Therefore, the decedent’s gift of the co-owned bond to the other co-owner was given effect and the bonds were held not to be subject to an estate tax.⁵⁵

“[T]he principle is firmly established that taxation is concerned with real ownership rather than with refinements of title.”⁵⁶ “The essence of a transfer is the passage of control over

48. *Id.*

49. *Id.* at 284.

50. *Chandler v. United States*, 312 F. Supp. 1263, 1268 (N.D. Cal. 1970) (emphasis added).

51. 312 F. Supp. 1263 (N.D. Cal. 1970).

52. *Id.* at 1268.

53. *Id.*

54. *Id.*

55. *Id.* “In short, we find nothing in either the language, or the history or the purpose of the regulations which reasonably calls for exacting an estate tax There is no relationship between exaction of such a tax and the purposes of the regulations. Any such relationship as might be conceived would be, at the most, and as stated by the Supreme Court in *Bank of America v. Rocco (Parnell)*, *supra*, so remotely or speculatively related to the purposes of the federal law . . . that . . . there is no justification for application of federal law”

56. *District of Columbia v. Wilson*, 216 F.2d 630, 631 (D.C. Cir. 1954).

the economic benefits of property rather than any technical changes in its title."⁵⁷ "[The] inquiry then—absent some countervailing consideration—must be concerned with real, rather than technical ownership."⁵⁸ Certainly, if one co-owner delivers a bond to the other co-owner, fully intending to make a complete gift, it cannot be said that the donor co-owner retains anything more than technical ownership. The donee co-owner can cash the bond at any time without the donor co-owner's consent and fully terminate any interest of the donor co-owner, technical or otherwise.⁵⁹

In re Hayes,⁶⁰ a 1969 decision from the Sixth Circuit Court of Appeals, the same circuit as *Curry*,⁶¹ concerned inclusion of a bankrupt co-owner's interest in United States Savings Bonds among the assets of the bankrupt's estate. The court noted that possession was one of the most important incidents of ownership of co-ownership bonds.⁶² The court also said that as "between two co-owner's . . . the extent of the property interest of each is a question of fact, not of law. One co-owner may as a matter of fact be the sole owner of the bond; he may be a half owner; he may have some other fractional ownership."⁶³

In the *Hayes* case, the bankrupt co-owner did not have possession of the bonds. The court said that what was possessed was an inchoate interest in United States Savings Bonds contingent upon two uncertain events: (1) the other co-owner dying first, and (2) the other co-owner not first cashing the bonds. The court concluded that "we must read . . . that this inchoate future interest was *valueless*"⁶⁴

When a co-owner of a bond transfers possession of the bond to the other co-owner, fully intending to make a complete and irrevocable gift of the bond, it is submitted that any interest he might have in the bond is valueless.⁶⁵ As in the *Hayes* case, any interest which the donor co-owner might have in the bond would be contingent upon two uncertain events. As a result, for estate

57. *Estate of Sanford v. Comm.*, 308 U.S. 39 (1939).

58. 216 F.2d at 631.

59. 31 C.F.R. § 315.60 (1964).

60. 407 F.2d 1031 (6th Cir. 1969).

61. 409 F.2d 671 (6th Cir. 1969).

62. *See* 407 F.2d at 1035.

63. *Id.*

64. 407 F.2d 1031, 1036 (6th Cir. 1969) (emphasis added).

65. Professor Ralph S. Rice has noted in his text, *FEDERAL ESTATE AND GIFT TAXATION* (1966), at 93, that the government's position appears to be wrong "where delivery of the bonds was made unequivocally to the donee with the intent to make a completed gift."

tax purposes, "the extent of the interest therein held⁶⁶ by the donor co-owner would be valueless if he died before the donee co-owner.

It is interesting to note a problem that arises if, in the hypothetical situation noted above, the donee co-owner dies first. The bond would then belong to the donor co-owner. If a court would hold otherwise, it "would defeat or impair the rights of survivorship conferred by these regulations upon a surviving co-owner or beneficiary. . . ."⁶⁷ The estate tax regulations expressly provide that "if the decedent furnished no part of the purchase price, no part of the value of the property is [included in his gross estate]."⁶⁸ Thus if the donee co-owner had furnished no part of the purchase price, it appears at first glance that the estate would pay no tax on the bonds. The donor co-owner's estate pays no tax on the bonds if he dies first and neither does the donee co-owner's estate pay any tax on the bond if he dies first.

The donor co-owner in this situation receives the best of both worlds. If he dies first, his estate pays no estate tax. He pays no gift tax because the Treasury does not impose a gift tax on co-ownership bonds unless they are cashed.⁶⁹ And if the donee co-owner dies first, because of the survivorship provisions under the regulations,⁷⁰ the donor co-owner gets back the bonds with the donee co-owner's estate apparently not being required to pay an estate tax on the bonds.⁷¹ That such a windfall in favor of the taxpayer can long survive, is highly doubtful.

It appears that the joint interests⁷² section of the estate tax only applies to the hypothetical bond situation if a decedent furnished some of the consideration for the purchase of the bond. If the donee co-owner dies first, having furnished no consideration for the bond, it seems there would be no estate tax liability on the bond by virtue of joint interests section. However, the Government could probably successfully argue that under § 2033,⁷³ the donee co-owner's estate must pay a tax on the bonds as property

66. INT. REV. CODE of 1954, § 2040.

67. 31 C.F.R. § 315.20 (1954).

68. Treas. Reg. 20.2040-1(c)(3).

69. Rev. Rul. 269, 1968-1 CUM. BULL. 399. See also "Some Legal Aspects of United States Savings Bonds", a pamphlet published by the Treasury Department, Savings Bond Division.

70. 31 C.F.R. § 315.62 (1964).

71. This presumes the donee co-owner had not furnished any consideration for the bond.

72. INT. REV. CODE of 1954, § 2040.

73. INT. REV. CODE of 1954, § 2033.

in which the decedent had an interest at the time of his death. Thus, the benefit of the *Chandler* decision to the taxpayer is not as great as it might appear at first glance.

If the *Chandler* decision is upheld,⁷⁴ the I.R.S. will no doubt wish to reconsider its position upon gift taxation of co-ownership held savings bonds.⁷⁵ However, the results of any reconsideration of the Internal Revenue Service's position is beyond the scope of this article. It is certain that the I.R.S. will not be amenable to allowing such a gift tax free transaction.

If the Treasury is concerned about the loss of tax revenue, it could change the bond regulations in order to prohibit the relinquishment of the rights of survivorship between co-owners. However, such a motivation for a change does not seem to be justified. The regulations are to help the government legitimately exercise its power to borrow money.⁷⁶ They are "designed to protect the Treasury as against adverse claimants in paying interest and principal of the bonds to the registered owner."⁷⁷ They are designed "to make the bonds attractive to savers and investors."⁷⁸ They are not designed to help elicit tax revenue.

Richard L. Gordon '71

74. It is presently on appeal to the United States Court of Appeals for the Ninth Circuit.

75. See Rev. Rul. 269, 1968-1 CUM. BULL. 399.

76. *Free v. Bland*, 369 U.S. 663 (1962).

77. *District of Columbia v. Wilson*, 216 F.2d 630, 633 (D.C. Cir. 1954).

78. *Free v. Bland*, 369 U.S. 663, 669 (1962).