

In the

Supreme Court of the United States

UNITED STATES OF AMERICA,

Petitioner,

vs.

MARIAN A. BYRUM, EXECUTRIX
UNDER THE LAST WILL AND
TESTAMENT OF MILLIKEN C. BYRUM,
deceased,

Respondent.

No. 71-308

Washington, D. C.
March 1, 1972

Pages 1 thru 41

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Washington, D. C.,

Wednesday, March 1, 1972.

The above-entitled matter came on for argument at
1:40 o'clock, p.m.

BEFORE:

WARREN E. BURGER, Chief Justice of the United States
WILLIAM O. DOUGLAS, Associate Justice
WILLIAM J. BRENNAN, JR., Associate Justice
POTTER STEWART, Associate Justice
BYRON R. WHITE, Associate Justice
THURGOOD MARSHALL, Associate Justice
HARRY A. BLACKMUN, Associate Justice
LEWIS F. POWELL, JR., Associate Justice
WILLIAM H. REHNQUIST, Associate Justice

APPEARANCES:

MATTHEW J. ZINN, ESQ., Assistant to the Solicitor
General, Department of Justice, Washington, D. C.
20530; for the Petitioner.

LARRY H. SNYDER, ESQ., Chamblin, Snyder and Casey,
209 South High Street, Columbus, Ohio 43215; for
the Respondent.

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Matthew J. Zinn, Esq.,
for the Petitioner

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In rebuttal

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Larry H. Snyder, Esq.,
for the Respondent

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P R O C E E D I N G S

MR. CHIEF JUSTICE BURGER: We will hear arguments next in No. 71-308, United States against Byrum.

Mr. Zinn.

ORAL ARGUMENT OF MATTHEW J. ZINN, ESQ.,

ON BEHALF OF THE PETITIONER

MR. ZINN: Mr. Chief Justice, and may it please the Court:

State planners have long sought a method whereby majority owners of closely held corporate stocks could maintain control of their corporations throughout their lifetimes, but nevertheless be able to pass on their businesses at death, without payment of an estate tax.

This Federal estate tax case presents an attempt which has thus far been successful to achieve these two most desirable goals. Here the method employed is a transfer of a portion of the majority owner's stock to a trust, with the owner retaining assured lifetime control of his corporations by reserving the right to vote the stock he transferred in trust, and the right to veto any sale of that stock by the trustee.

We brought this case here on certiorari to the Court of Appeals for the Sixth Circuit because of our concern with its effect on the administration of the Federal estate tax laws.

The specific facts are these: The decedent, Mr. Byrum, owned controlling stock interests in three corporations. Late in 1958 he created an irrevocable trust naming a bank as trustee, to which he thereafter transferred stock in the three corporations. The trustee had power, until Mr. Byrum's youngest child reached age 21, to distribute trust income and principal to the beneficiaries in its discretion. When the youngest child reached age 21, separate trusts were to be established for each child, or for the surviving issue of any deceased child.

Each child's separate trust was to terminate when that child reached age 35.

The trust instrument specifically provided that Mr. Byrum would retain for his lifetime the right to vote all unlisted stocks, such as the stock in the three corporations he transferred, and the right to veto any sale of that stock by the trustee.

On page 4 of our opening brief there appears a small chart, showing the percentage of each corporation's stock owned by Mr. Byrum and by the trust at the time of Mr. Byrum's death.

In the case of the first corporation, which is Byrum Lithographing Company, you can see that the total originally owned by Mr. Byrum was 71 percent of the corporation stock. He transferred 12 percent of the stock in trust, and retained

59 percent in his own name.

Q Did he still retain it at his death?

MR. ZINN: Yes, sir, he did.

Q Was there ever any instance -- I suppose there wasn't -- where a sale was proposed and there was a veto?

MR. ZINN: This case came on on cross motion for summary judgment, Mr. Justice Blackmun, and the record doesn't reveal any such instance.

The situation that obtained with Byrum Lithographing then, so far as the record discloses, is that at all times Mr. Byrum owned the -- was able to vote 71 percent of the stock of the corporation and, at all times until his death, was in control of the corporation.

Looking at the second and third corporations, Graphic Realty and Bychrome, the situation is the same. He originally owned 83 and 88 percent of the stock of those corporations; transferred a portion in trust. And, by retaining the right to vote that stock for his lifetime and the right to veto any sale of the stock, was assured lifetime control of those corporations as well as Byrum Lithographing.

Q The trust had been in existence less than six years at the time of his death?

MR. ZINN: The trust was created in December 1958.

Q And he died in September of '64.

MR. ZINN: That's right.

Q And these were a series of transfers, it wasn't just one transfer in trust.

MR. ZINN: That's correct.

Q It was creation of the trust in '58 and then a series of transfers over the ensuing years until his death.

MR. ZINN: That's correct.

Q And how would the case stand if the trust had lasted -- if he'd lived another ten years and had transferred all of this closely held trust to the -- closely held stock in these corporations to the trust at the time of his death, but had retained of course the same, that the trust had had the same provisions?

MR. ZINN: So far as the United States is concerned, Mr. Justice Stewart, the case would be precisely the same.

Q I thought you would say that; I just wanted to be sure.

MR. ZINN: Indeed, that may have been the plan.

Q Yes.

MR. ZINN: In order to obtain the maximum gift tax exclusion.

Q So if the entire 71 percent and 83 percent and 88 percent, respectively, had, at the time of Mr. Byrum's death, been in the hands of the trustee, your case would still be the same, and your submission would still be the same, would it not?

MR. ZINN: Yes, it would. And I would suggest that that would be a panacea for State planners, because --

Q Well, -- yes. That is what you're now suggesting, but --

MR. ZINN: That's right.

Q -- but the fact that the majority was still in his hands at the time of his death doesn't make your case any stronger, really, does it?

MR. ZINN: That's only true in the case of the first corporation.

Q All right, that a large percentage was still in his hands. Does it?

MR. ZINN: We don't rely on a distinction between whether the stock retained in his own name was enough to control, or whether the combined right to vote the transferred stock --

Q If there had been a complete transfer of all of this stock, given to the trust in 1958, your submission would still be basically the same, wouldn't it?

MR. ZINN: We'd still be here, yes, sir.

Q Yes.

Q Suppose he had transferred, not to the trust, but had just sold to unaffiliated interests all or a substantial percentage of the shares he retained initially; would that make a difference?

MR. ZINN: Sold the stock?

Q Sold the stock he retained, to outside people.

Suppose he had?

MR. ZINN: In other words, suppose that he didn't have control?

Q Right.

MR. ZINN: Well, in the case of the first corporation if he got below 50 percent -- 50 percent ownership, we might still be here if we could show that he had, in substance had control, even with a smaller interest.

Q Your case rests on control, then, does it not?

MR. ZINN: Yes, it does.

Q Effective control?

MR. ZINN: Effective control, that's right. And if it were less than 50 percent, it still might be effective control. We'd have to look at the particular facts.

Q Well, this is the point I was leading up to. You rest on control, and it may or may not exist, depending on whether he had 50 percent or more?

MR. ZINN: Right. But in this case we don't have that problem, Mr. Justice Powell, because there's no question of control.

Q I understand. I understand.

Q Mr. Zinn, is the term "effective control" one that's used in the statute or in the regulation?

MR. ZINN: No, it is not, Mr. Justice, I'm going to get to the statute in just one moment, if I may.

Q Are you going to give us, somewhere along the line, the definition of "effective control", and why it is the controlling principal?

MR. ZINN: No, because we don't think we have to rely on effective control in this case. He had actual control. That's not disputed.

But the District Court and the Court of Appeals, and I think the respondent, concedes that Mr. Byrum was in control of this corporation for his lifetime.

Q But I took it, in your answer to the question of Mr. Justice Powell, that you said effective control would be equally good, it might be a weaker case in some respects, but I take it the rationale of your argument must embrace both actual control and effective control?

MR. ZINN: Yes, sir.

We will -- I hope to demonstrate why this was in effect a testamentary transfer because of the retention of control. In this case legal control; perhaps in another effective control.

After Mr. Byrum's death in September of 1964, the Commissioner asserted estate tax deficiencies against his estate, on the ground that the stock transferred in trust was includible in his gross estate under both Section 2036(a)(1)

and 2036(a)(2) of the Code.

The estate of course had included in the gross estate only the stock retained by Mr. Byrum in his own name.

The statute is set out on pages 2 and 3 of our opening brief, and reads as follows:

"The value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, under which he 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:

"(1) the possession or enjoyment of, or the right to the income from, the property, or

"(2) the right, either alone or in conjunction with any persons, to designate the persons who shall possess or enjoy the property or the income therefrom."

On cross motions for summary judgment in the District Court, the District Court granted the estate's motion and a divided Sixth Circuit affirmed.

We begin any discussion of Section 2036 with this Court's decision in the O'Malley case six years ago, and more recently in the Grace Estate case in 1969.

In 1966, in O'Malley, Mr. Justice White, speaking

for the Court, stated that the predecessor of Section 2036 was, and I quote, "an important part of the legislative policy of subjecting to tax all property which has been the subject of an incomplete inter vivos transfer."

In Grace Estate, Mr. Justice Marshall, writing for the Court, explained that the purpose of the predecessor of Section 2036, and I quote now from 395 U.S., at 320, "was to include in a decedent's gross estate transfers that are essentially testamentary, i.e., transfers which leave the transferor a significant interest in or control over the property transferred during his lifetime." Unquote.

Q Was that a case involving reciprocal trust?

MR. ZINN: Yes, that was the cross trust.

Q Because I didn't sit in that case then.

MR. ZINN: Judged by these statements of purpose of Section 2036, we think that these transfers must be considered incomplete until the time of Mr. Byrum's death, that is essentially testamentary.

Nothing changed with regard to corporate operations following the transfers. Mr. Byrum was in control as he had been previously. All that the beneficiaries had after the transfers were (1) the right to receive such dividends as Mr. Byrum, as controlling stockholder, determined should be paid, (2) the right to receive the proceeds of a sale of the stock if Mr. Byrum agreed that the stock should be sold, and

(3) the right to the proceeds on liquidation of any of the corporations if Mr. Byrum voted in favor of the liquidations.

Q Well, what they had was the -- whatever rights beneficial stockholders have in any corporation, then, am I correct? Whether the owner was Mr. Byrum or Mr. Smith or Mr. Jones. What the beneficiaries of the trust had were what the beneficial owners of shares in a corporation have.

Correct?

MR. ZINN: I'm not sure I understand the --

Q Well, whatever those rights are is what they had.

MR. ZINN: Well, the statute doesn't tax all of the rights, all such interest, Mr. Justice, but it taxes them where they're transferred to trust and the transfer, in effect, is testamentary, as it is here.

Q Well, you said the beneficiaries of the trust, you were implying that they got very little because --

MR. ZINN: That's right.

Q -- Mr. Byrum controlled, his control over what they got --

MR. ZINN: They got whatever he said they should.

Q Well, they got whatever shareholders -- whatever right shareholders have; beneficial shareholders.

MR. ZINN: Well, I would draw a distinction, I think, between --

Q And this would be true whether Mr. Byrum were the owner of the majority of the stock or whether Mr. Jon Smith were?

MR. ZINN: That's right. Section 2036 taxes such transfers, we believe, where the transferor isn't controlling.

Q Of course we're now talking about the taxability of Mr. Byrum's estate, but --

MR. ZINN: Correct.

Q -- you implied that somehow or another, since he was the owner of the corporation, that the beneficiaries of the trust got less. I didn't follow that argument.

Q Could he have originally given the voting rights to someone else, other than retaining them?

MR. ZINN: He could have given them to the trustee, Mr. Chief Justice.

Q Well, I'm speaking of a third person; could he have given them to a third person?

MR. ZINN: He could have given them to a third person. And then you're going to ask me whether -- what the tax consequences would be? In the case of the first corporation --

Q I don't know whether I am or not.

MR. ZINN: In the case of the first corporation, we'd still be here, because he retained in his own name.

Q Doesn't your position assume improper decisions on his part to withhold the payment of dividends?

MR. ZINN: Not at all. We think fully within the scope of this fiduciary duty he could have determined that all of the money should be returned to the corporation.

Q Well, there are limits on that, aren't there?

MR. ZINN: Very scanty ones, Mr. Chief Justice. We think the record in this case shows clearly enough how little did go on. If you will refer to page 25 and 26 of the record, you will see that the dividends that were paid on the transfer of stock from the time of creation of the trust until Mr. Byrum's death totaled \$303.50.

Q What had it been in a comparable period before that?

MR. ZINN: We don't know that. But we do know in the period immediately after Mr. Byrum's death the dividends went up from ten cents a share on each of the stock to two dollars a share; a twentyfold increase. And that the dividends in the first year after his death were \$1,498, which was some five times what they had been in the preceding six years.

Q I suppose you would agree that conceivably, possibly, that was a very unwise -- could have been a very unwise dividend decision?

MR. ZINN: Right. But the fact of the matter is, Mr. Chief Justice, that so long as directors act in good faith in determining dividend policy, there's virtually no check on them.

Q Doesn't that apply before just as well as after?

MR. ZINN: Yes, sir. But that was precisely the limitation on the grantor in the O'Malley case, in which this Court held that the power to accumulate income constitutes the right to designate within the meaning of Section 2036.

Q I didn't understand that as a holding of the Court, because that wasn't the issue in that case. What it was was an apparent approval of what the Court recognized to be a rule of long standing; isn't that right? I just read the opinion.

MR. ZINN: I would say that it's something -- I would agree with you -- that technically it's not holding on the other --

Q But that's not the issue?

MR. ZINN: On the other hand, I would have to say it's something more than dictum, because it was essential to what the Court did hold, in the sense -- on the question whether accumulated income was transferred. That holding presupposes that --

Q As necessary income support.

MR. ZINN: Yes. So I think it's something more than dictum but perhaps something less than square holding.

Q Because that was not the issue, that had not been questioned --

MR. ZINN: That's right.

Q -- by the other party in that case?

MR. ZINN: That's right.

In any event, our point here is that the grantor in the O'Malley case also had to act in good faith, despite the broad grant of power that he retained to withhold or distribute income to the beneficiaries. If it was shown that he was acting out of his private interest rather than out of the beneficiaries' interest in exercising that power, we think a court of equity would have stepped in and could have required a distribution. Every trustee has a duty of good faith and a duty of good motive. But in order to establish an objective limitation on the power to designate, we think there has to be a more specific duty.

And nothing in respondent's brief or, for that matter, in amici's brief suggests that there is any objective standard by which a corporate director's exercise of discretion is limited. They can -- if they decide to return all of the corporation's profits into the business, there's no way that a court can step in and do anything about it, unless you could show that the director had a bad motive.

But that's a subjective standard.

Q Well, there can be federal income tax consequences, can there not?

MR. ZINN: In this particular case?

Q If there is an unreasonable accumulation of

earnings?

MR. ZINN: Yes.

Q Which motivates directors not to do so, if they're going to run that race.

MR. ZINN: I would say a couple of things about that. First of all, there's a \$100,000 exemption from the Section 531 tax.

Q Yes.

MR. ZINN: And secondly, that still doesn't prevent a reinvestment of all the earnings. There's no way that the Section 531 tax can check -- can be a check on --

Q If you reinvest --

MR. ZINN: -- the policy. If you reinvest in the business --

Q -- in the plant.

MR. ZINN: -- it's only if you sit on it.

Q Right. Right.

MR. ZINN: And again, we fail to see any distinction between the limitation on the power here, and the limitation on the power in O'Malley. It's roughly the same thing. And for that reason we think that the trust assets are taxable under Section 2036(a)(2), because Mr. Byrum retained the right to designate.

Q Mr. Zinn.

MR. ZINN: Yes, sir.

Q I'd like to be sure I understand your position. Suppose the stock placed in the trust had no voting rights at all? Let's assume it were nonvoting stock. So, with respect to that trust, no problem, no issue with respect to voting. But the grantor had retained control of the corporation through retention of voting stock. Would your position be the same?

MR. ZINN: We'd be here, Mr. Justice. That's pretty close to Revenue ruling that --

Q Would you still be here --

MR. ZINN: -- Chief Judge Phillips relied upon in his dissenting opinion in the Court of Appeals, Revenue ruling 67-54.

Q 67-54?

MR. ZINN: Yes, and it's reprinted beginning at page 48 of the record Appendix.

Mr. Justice, our concern here is not with the formalities, but ever since this Court decided the Hallock case, it has consistently held that estate tax clause to be determined by the realities of the situation. The realities are precisely the same, whether the grantor transfers non-voting stock in trust or whether he transfers voting but retains control of the corporation.

Q Suppose there had been no limitation on the sale of the stock transferred to the trustee, would that make a difference?

MR. ZINN: I think that might make a difference, Mr. Justice, if the trustee had the power to sell, and if the stock was marketable, and if it could be shown that there was no understanding off the record, whether express or implied, between the grantor and the trustee; then I think that the government would not raise this kind of question.

Q But it might, if in fact the trustee had not sold?

MR. ZINN: It might, but I would point to --

Q But only if no dividends had been paid?

MR. ZINN: No, that wouldn't make any difference. I think that helps our case, Mr. Justice White.

Q Well, I know, but in the example. I mean if the trustee doesn't sell, the only reason he doesn't sell is because dividends have been paid.

I mean, he's probably under a duty to sell if this isn't a good investment.

MR. ZINN: Well, he might be under a duty to sell.

Q Might be? What trustee do you know of that can hold an unproductive voting common stock for any length of time?

MR. ZINN: Well, the trustee in amici's case did precisely that, Mr. Justice White.

Q Without a waiver in the trust, allowing him to hold the family stock?

MR. ZINN: Well, the grantor in amici's case was the trustee, and while the facts aren't of record yet, the deficiency notice just hadn't issued. That stock was transferred in trust in 1948, and the decedent there died in 1967.

The government has asserted that the value of the stock transferred, at the date of the decedent's death, was \$24.5 million. Now, that's subject to question, of course, that's the government's valuation.

But I don't think it's subject to question that only \$300 of dividends was paid on that stock in the twenty years it's been held.

Q Well, let's assume -- and maybe this is the case I want to put to you: Suppose the grantor transfers to a bank and to himself as trustee, --

MR. ZINN: Right.

Q -- 100 percent of the stock of a corporation.

MR. ZINN: Right.

Q And he becomes a trustee, but the trustees are under a duty to distribute all of the income that they receive.

MR. ZINN: Right.

Q But they happen to be, between the two of them, 100 percent owners of the corporation. And as trustees they have the control we've been talking about.

MR. ZINN: Yes.

Q Does this make a difference?

MR. ZINN: We'd be here.

Q You'd be here, even though -- even though the trustees are under a fiduciary duty as trustees that this taxpayer in this case is not?

MR. ZINN: We question whether they have more than fiduciary duty in those circumstances, more than the good faith fiduciary duty. Because --

Q Well, at least they have whatever fiduciary duty a trustee's got?

MR. ZINN: Well, --

Q To produce the kind of income for beneficiaries that trustees are supposed to produce.

MR. ZINN: Well, maybe they're supposed to produce it, Mr. Justice, but the fact of the matter is that they just don't produce it. And I don't think amici's case is atypical, when you have a situation like this.

Q So you say that any time the owner of stock makes a transfer, whether he remains as a -- whether he's a trustee or whether he's not a trustee --

MR. ZINN: Well --

Q -- as long as he's got control, whether as a trustee or as not, the same result?

MR. ZINN: Well, I'm saying that unless the -- unless he has a duty to sell the stock, if a determination is made that

no dividend should be paid, in the exercise of his power as director he may determine that there shouldn't be any dividend.

Q That's right.

MR. ZINN: He may determine that the corporation has a cash shortage.

Q That's right.

MR. ZINN: Now, nobody is going to sell -- nobody sells this kind of stock in closely held corporations, Mr. Justice, they hold onto it. And so there's a conflict in duties here. And we say that the way that that conflict is resolved is: yes, the trustee has a duty of good faith; yes, the trustee has a duty of pure motive; but he has no duty in those circumstances to fairly apportion --

Q You say trustees never sell unproductive stock in closely held corporations. Well, I don't know about that.

MR. ZINN: Well, as I say, in this case one could make the same argument as in amici's case; but the fact that they didn't sell.

Q Well, in this case he had the duty not to sell, except for the --

MR. ZINN: The trustee?

Q -- except with the permission of the grantor. That was a trust instrument under which he was operating.

MR. ZINN: This is an easier case for the government,

but I would not be prepared to concede amici's case. I think the facts in that case are so bizarre that it's a stronger case for the government.

Q Well, you don't need to concede it or argue it, I guess.

MR. ZINN: One last word, Mr. Justice Powell, with regard to the question of where the power to sell is given to the trustee, I will refer you to the Beckwith case, which is cited in the footnote on page 19 of our brief, involving a situation largely like the one that you raised.

Q May I ask this question, while I've interrupted you: Getting back to control, you're familiar, I'm sure, with the presumption applied by the SEC to the effect that a 10 percent owner is presumptively a controlling stockholder? Would you carry your doctrine that far?

MR. ZINN: I might if the rest of the stock was 45/45, and the other two people were at loggerheads.

Mr. Chief Justice, I should like to reserve my remaining time.

MR. CHIEF JUSTICE BURGER: Very well, Mr. Zinn.

Mr. Snyder.

ORAL ARGUMENT OF LARRY H. SNYDER, ESQ.,

ON BEHALF OF THE RESPONDENT

MR. SNYDER: Mr. Chief Justice, and may it please the Court:

The facts of this case are relatively simple, and, to my knowledge, they're not in dispute. However, I think there is some danger that some of the more important facts may be obscured by rather extensive citations of previous cases in some of the arguments.

So, at the risk of repeating some of the facts that are before you, I would like to outline briefly some of the more important elements of the Byrum trust.

Counsel has told you it's an irrevocable trust for the children of the decedent, and that a national banking corporation is trustee.

The trust instrument provides that until the youngest of these minor children reaches 21, no distributions from either -- let's put it this way, that the distributions from either corpus or income are entirely within the discretion of the trustee, having due regard for the education and the maintenance and the care for the children.

Upon the youngest child's reaching 21, the terms of the trust provide that the trust corpus is to be divided into separate trust funds for each of the living or deceased children of the decedent, and that each such fund is to continue until that beneficiary reaches the age of 35.

If, prior to reaching age 35, a beneficiary has an emergency such as an extended illness or some other need, the trustee is authorized to pay to or on behalf of that

beneficiary, from either corpus or income. Otherwise the income is to be accumulated and to be distributed at the termination of the trust.

Decedent did retain the right to vote the stock, the unlisted stock held in the trust corpus. And it's true that there was, at the time of the decedent's death, unlisted stock in three corporations, and that the right to vote this stock, together with the right to vote the stock owned by the decedent, gave him the majority voting interest in these three corporations.

Q Mr. Snyder, does the record show who drew this trust instrument?

MR. SNYDER: No, sir. But I know who did, if the Court's interested. My law partner did, before I joined them.

Q Before what?

MR. SNYDER: Before I was associated with my law partner.

Q Was Mr. Byrum an officer of the corporation?

MR. SNYDER: Yes, I believe he was an officer of all three corporations.

Q Salaried officer?

MR. SNYDER: Yes.

The government has made the principal issue in this case a question of whether this right to vote stock --

Q Incidentally, let me follow through: Was Mr.

Byrum a director of the trustee bank?

MR. SNYDER: No.

Q Was he a customer otherwise, than a trust customer?

MR. SNYDER: I'd have to guess at that; I don't know.

Q The record doesn't show?

MR. SNYDER: I didn't know Mr. Byrum. I doubt very much -- I know he wasn't a director; but I'm in no position to know whether he was a customer of that bank or not.

As I started to say, the government has made the principal issue in this case the question of whether this reserved power to vote this stock constituted the right to designate the persons who shall possess or enjoy this property, or the income from the property, the stock, within the meaning of Section 2036(a)(2).

The argument is, of course, that the right to vote this stock gave him the right to dictate the corporate dividend policies of these three corporations, and therefore to regulate the flow of dividend income to the trust.

Now, assuming for the moment that decedent had this absolute right to dictate a corporate dividend policy, it by no means follows under the circumstances of Byrum, at least, that he had the power to shift the income of this stock to beneficial enjoyment said by the cases to be the basis for tax under Section 2036(a)(2).

As indicated earlier, the income from this stock did not vest, in the sense that it was not payable as earned, it was to be accumulated unless there were certain emergencies or other conditions shown, at which time it was with the discretion of the trustee to pay this income.

If that condition or those conditions did not exist, then the income was accumulated, added to the corpus of the trust, and paid to the beneficiary on the termination.

We submit that this indirect conditional power to effect distributions of income from the trust does not constitute a right to designate who shall receive the trust income.

The right to designate, the term "right to designate" we feel implies some sort of a permissive choice between potential income beneficiaries --

Q Well, do you accept the proposition that a trustee's power to accumulate or not is equivalent -- is the right to designate within the meaning of the statute?

In other words, the O'Malley -- what O'Malley has said to stand for by the government. Do you accept that as a standard for it?

MR. SNYDER: I accept that, yes.

Q You do?

MR. SNYDER: I think O'Malley is distinguishable.

O'Malley was a direct power.

Q Yes.

MR. SNYDER: In O'Malley, as I recall O'Malley, the set-law trustee had the --

Q -- power to accumulate. And the Court said that was the power to designate within the meaning of the statute.

MR. SNYDER: There it was the conscious, the permissive choice. Set-law had the power to --

Q You do being by accepting that, but then you distinguish this situation?

MR. SNYDER: I'd like not to accept it, but it's law.

Q You think you're stuck with it?

MR. SNYDER: I think I am.

So we submit that there isn't in this case, and the facts of Byrum, this right to designate which predicates tax under Section 2036(a)(2), at least if the terms of the statute are to have any meaning at all.

Q Mr. Snyder, I've fallen off the wagon along the way some place. Prior to age 21, there is no accumulation direction, I take it?

Prior to age 21 --

MR. SNYDER: No, sir. Prior to age 21 -- well, it --

Q Everything is discretionary distribution?

MR. SNYDER: It's a discretionary distribution, that's

right.

Q After the youngest reaches 21, then there is the direction to accumulate except in conditions of emergency.

MR. SNYDER: Yes, sir. But the discretion to distribute income from -- or corpus from the trust before the youngest child reaches 21, you will further read in this: "with due regard .. for education, maintenance and care" of the child or children.

So the question has not arisen under the Byrum trust that -- it would seem to me that under the -- and I think this is the way it's interpreted, that it is accumulated unless the trustee determines in its discretion that there is a need for distribution of either income or corpus for educational needs or for maintenance or for care of that child or the children.

Q I suppose that if the stock had been given, but the trust instrument had said: I retain the income from the stock for my lifetime -- that stock would be includable in his estate?

MR. SNYDER: As far as I'm concerned, it would be, yes.

Q And if the trust instrument said: I will pay to you what part of the income from the stock that I feel inclined to pay you; I may pay you 100 percent of it or I may pay you 50 percent of it. That would be the same result,

wouldn't it?

MR. SNYDER: Are you talking now -- who is the trustee in this instance?

Q Well, an independent trustee. Mr. Byrum gives this stock to the bank as trustee, but says: I'm going to --

MR. SNYDER: Oh, the terms of the --

Q -- how much of the income I keep is up to me.

MR. SNYDER: Mr. Byrum has reserved this power to determine what amount --

Q Or he says: I may pay you 100 percent all the time, but --

MR. SNYDER: Or it may not be. I would say under those terms that it was taxable, and includible in the estate of the decedent.

Some may not agree with me, but I don't see how that could be held not to be taxable in that case.

Speaking here whether the income is definitely --

Q Well, he said: I won't keep any of it for myself, but I retain the power to have some of it channeled to somebody else besides you, Mr. Trustee.

MR. SNYDER: Well, of course, we keep narrowing that. I would think, even in that case, it would be still a taxable transaction.

Q Yes.

MR. SNYDER: But here he's unequivocally desparted

from any interest in this income in this stock whatsoever.

Q But he does have to retain the power to direct that the money shall be used in the corporation?

MR. SNYDER: Well, he does have a majority voting interest in the corporations, and I think that's a point that should be considered. Because, contrary to the position of the government in this case, I disagree that this gives, or gave Mr. Byrum the right to dictate dividend policies to suit his personal interest.

Under the law of Ohio and under the general corporation law, he stood in a fiduciary relationship to these corporations and to all the stockholders of the corporations, and significantly in all three of these corporations there was a minority stockholder outstanding -- or minority stock interest outstanding, who was not related to Mr. Byrum, was not a member of his family.

We submit that he could not have regulated the dividend flow from these corporations to suit his personal interest, his private purpose, without violating his position of trust.

And the question arose as to what objective standard is there to hold the majority stockholder and the directors to; and the objective standard is this, I think quite clearly, and this is corporation law, is that the stockholders are entitled to the profits of the corporation other than those profits

which are reasonably needed for the business.

And the question of what profits are reasonably needed for the business is a question that's answered constantly by the courts. And it is, of course, the very question which is involved in the corporate accumulated earnings tax, which was referred to by Justice Stewart.

So there very definitely is an objective standard to which a majority stockholder is held. Indeed, in many respects I think it's more objective, more restrictive than is some of the -- are some of the standards supposedly imposed upon trustees.

Quite clearly, it is not a matter of the good faith of the majority stockholder or of a majority or of the board of trustees. There's an objective standard. They are obligated to pay out the profits of the corporation, unless there is a reason, a business need, to retain these profits.

Q Mr. Snyder, what do you think was the purpose of Mr. Byrum in retaining these powers?

MR. SNYDER: Well, I think the purpose of Mr. -- quite frankly, I think the purpose of Mr. Byrum -- understand, I did not know him and was not around when the trust was created -- I think his purpose was to attempt to hold the corporation together. I think a small corporation is at an extreme disadvantage for an owner having an interest in small corporations over a larger corporation. You can give extensive

stock to the large listed corporation away without the danger of having the corporation collapse.

This was a small, everyday kind of a business, and I think he was concerned about the business judgments the bank would make or a successor trustee, which would have to be a corporation.

So in answer to your question, I think he was concerned about the business judgments that might occur if the right to vote his stock is given to the national bank.

Frankly, I don't agree with him, I think that -- I don't know how it is other places, but in Columbus, Ohio, he probably didn't have to do that. I'm sure the bank would have called him and said, Mr. Byrum, how do you want us to vote this stock?

But that isn't our case, unfortunately, he did retain the right to vote this stock.

But focusing again on the statute, which we can't get away from, Section 2036(a)(2), I don't really think, in the circumstances of Byrum, that there is any shifting of corporate income, or rather of dividend income by the payment or the withholding of dividends.

If dividends are declared, they are paid, under the terms of this trust, unequivocally to the trust. Mr. Byrum had nothing to do with it. They were subject to being withdrawn under the terms of the trust, he had no control of that.

If dividends were withheld as a result of legitimate business decision, how can you say there's any shifting of income? If they were withheld partially or totally because of his private motives, then the minority stockholders had redress in the courts.

And, indeed, under those circumstances I think the trustee himself would be obligated to take action, because, after all, he is representing the stockholders and beneficiaries of this trust.

Q What if Mr. Byrum had been, himself, the trustee; would that have made your case stronger or weaker?

MR. SNYDER: In addition to the --

Q In addition to everything else, what if he had been a co-trustee?

MR. SNYDER: I don't think it would have changed my case. I don't think it would particularly help it; but I don't think it would damage it, either. Which is not a -- it's a rather equivocal answer.

Q No, well, I think you're probably --

MR. SNYDER: I don't see that the situation would change.

Q The government agrees with you on that.

MR. SNYDER: [Laughing] Yes.

Q It would bring us a little closer, factually, to the Reinecke v. Northern Trust case, wouldn't it?

MR. SNYDER: Yes, I think it would. And I think really that Byrum rises and falls on the Reinecke, because Byrum is, after all, no more than an administrative power. Byrum had no more than an administrative power. As a matter of fact, it was an indirect administrative power.

Q Of course Reinecke was under the old statute, wasn't it?

MR. SNYDER: Yes, it was. But the issue common to Byrum is this -- well, let me back up.

The specific question in Reinecke was whether these powers to settle or to supervise the investments of the trust or vote the stock held in trust, whether this constituted the gift of the corpus of the trust, a gift intended to take effect at or after death.

Now, the rule of Reinecke is that this kind of administrative power did not delay possession or enjoyment, did not delay the vesting of possession or enjoyment. The question is here, does the same kind of a power cause a shifting of possession or enjoyment. And by a parody of reasoning, if it does not constitute a delay of possession or enjoyment, it doesn't constitute a shifting of possession or enjoyment.

I think that Reinecke and all the cases, lower court cases that have been decided after Reinecke and followed Reinecke, stand as a complete bar to the position of the

government here. They have, as you point out, attempted to discount it because it was enacted before the predecessor to Section 2036(a)(2); but the fact of the matter is there's a common thread in Reinecke and in Byrum. And Reinecke cannot be dismissed.

Q One last question and I'll stop. Was there by any chance a reversion here in Mr. Byrum? What if he survived all of the issue?

MR. SNYDER: No, there wasn't. The --

Q All right. That's good enough.

MR. SNYDER: -- specific provision saying that there shall be no revision, I can't pick it out of the record for you now; but it's a part of the trust instrument --

Q I was having trouble finding it.

MR. SNYDER: -- and there is no possibility of a revert in this case.

To this point, discussion has been about the Section 2036(a)(2) issue. The government also raises the question of Section -- the applicability of Section 2036(a)(1). I think the argument in support of its position is unpersuasive on its face, and I don't intend, at this oral argument, to try to add to the briefs on this question, unless there are some specific questions.

I would like to direct attention just briefly to the government's reply brief. It seems to me in its reply brief

the government backs off from its earlier position.

They take a new tack and say that actually Byrum is disposed of by the precedents of three cases decided by this Court, the one being the O'Malley case that we've discussed here and the other is Commissioner vs. Estate of Holmes, and Lober vs. U.S., and also suggests, or so it seems to me, that we didn't cite these cases because we were trying to avoid them. And we didn't cite them; but we're not trying to avoid them. Because on this point we agree with the government, and think these three cases do invite comparison with Byrum.

We've compared O'Malley. As you will recall, in Holmes and in Lober, the set law reserved the right to terminate the trust in those two situations before their specified termination date, and thereby to cut off the contingent remainder interest.

And as compared to Byrum, we think clearly here in Lober and in Holmes is the situation where the set law held a conscious, permissive, and open choice; he had an open power to directly affect the beneficiaries of those two trusts.

This is not the case in Byrum. The government has to look to some subjective consideration about stock manipulation or dividend manipulation in order to get to where it is now.

We submit that this ought not be made the basis of taxation.

The government has also, somewhere in one of its briefs, indicated that if Byrum was not reversed, that there will be a great deal of litigation to follow. I think, frankly, just the opposite is true. I think it's been demonstrated by the argument here today that Byrum is just one step in the government's plan to expand Section 2036. And I suppose then 2038.

Because if I understood correctly the argument here, I don't think even a trust will stand in the way of a government search to tax these transactions.

And I would simply say to you in conclusion that if these are situations, if Byrum represents a situation that, on equity, dictates that there should be a tax, I don't think it is, but assuming that that's true, then I submit to you it's for the Congress to enact the statutes to tax. It's not taxable under the present laws.

And I submit, in all due respect, it should not be made taxable by this Court; but should be left to the Congress.

Thank you.

MR. CHIEF JUSTICE BURGER: Thank you, Mr. Snyder.

Mr. Zinn, do you have anything further?

REBUTTAL ARGUMENT OF MATTHEW J. ZINN, ESQ.,

ON BEHALF OF THE PETITIONER

MR. ZINN: Yes, Mr. Chief Justice, I do.

Three points. First, if this Court affirms the

decision below, I venture to suggest that, in the absence of further legislative change, it will be a rare case indeed when stock in a closely held corporation is subject to the estate tax.

I don't think this is consistent --

Q Well, stock in a closely held corporation is transferred in trust to somebody else, you mean?

MR. ZINN: Well, if you can do it this way, Mr. Justice, and keep control throughout your lifetime, I don't see why you'd transfer it to an independent trustee.

I would suggest only that this is totally incompatible with the congressional intent. I would refer the Court to Section 303 of the Code, which provides a special redemption provision for the payment of death taxes and administrative expenses, and is usually applicable only in the case of stock of closely held corporations.

I would refer also to Section 6166 of the Code, which provides that where the bulk of an estate is made up of stock of a closely held corporation, the estate tax may be paid in ten installments, rather than 15 months after death.

I would like to return, if I may, to Mr. Justice White's query regarding the duties of trustees. I would agree with him that where the trustee has only those powers necessary under State law, that is that they be confined in investment to the legal list that he has the duty to apportion fairly

between the income beneficiaries and the remaindermen.

But you can take gradations of that case, and first you can give him the power to go beyond the legal list and that gives him some more latitude in shifting the beneficial enjoyment of income, as --

Q But just what if he's subject to the most prevailing rule that he has to act like a prudent trustee?

MR. ZINN: Well, I think it would, but these additional powers, Mr. Justice, are put into the trust instruments, and they go so far as to say --

Q Well, I understand that, but I just asked you about an ordinary trustee.

MR. ZINN: If he has only the powers to invest -- talking about the investment power -- to invest in property on the legal list, we wouldn't say that he has the right to designate. But when he can go beyond that, and go beyond --

Q I know, but however broad the powers you give in a trust, whether he has to go on a legal list or whether he has to take bonds or common stock, it's still subject normally, unless there's some specific provision in the trust instrument, to the prudent investment rule. Even if you got the power to invest 100 percent in common stock --

MR. ZINN: One hundred percent in --

Q -- that doesn't give any power to hold a worthless common stock.

MR. ZINN: Well, it may give power, I think that it could give power to invest, let's say, --

Q Well, we'll have to have an exchange of briefs under the State law sometime.

MR. ZINN: I would like to make one last point. We rely also on Section 2036(a)(1) of the Code. We say that the decedent here retained the enjoyment of the transferred property, and we think again the Court's realistic approach, that has been applied since Hallock, should be applied here.

If one has a bond of AT&T, obviously the essence of enjoyment of that bond is the income from the bond. If one has an oil painting, the essence of enjoyment of the oil painting is having it hang in one's home.

In the case of a closed corporation, the essence of enjoyment is controlling that corporation, setting one's own salary, setting one's own fringe benefits, within limits to be sure, but setting them nonetheless. And I would, in closing, refer the Court to the quotation from Professor O'Neal, which we have set out at some length on pages 24 and 25 of our brief.

Thank you, Mr. Chief Justice.

MR. CHIEF JUSTICE BURGER: Thank you, Mr. Zinn.

Thank you, Mr. Snyder.

The case is submitted.

[Whereupon, at 2:33 o'clock, p.m., the case was submitted.]