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## Trusts - Interchangeability of the Inter Vivos Trust and the Will - Various Tests of Trust Validity

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TRUSTS—INTERCHANGEABILITY OF THE INTER VIVOS TRUST AND THE WILL—VARIOUS TESTS OF TRUST VALIDITY—Assuming interchangeability, an inter vivos trust used in place of a will may bring numerous advantages.<sup>1</sup> Although there is no tax saving,<sup>2</sup> the inter vivos trust, unlike a will, provides expert management of the trust property during the life of the settlor,<sup>3</sup> avoids delay and expense incident to probate proceedings,<sup>4</sup> avoids the continuing necessity of approval of accounts in a "court" trust, and obviates the necessity of ancillary proceedings where the property is located in several states.<sup>5</sup> In addition, it may be possible by use of the inter vivos trust to avoid certain statutory restraints on the freedom of testamentary disposition.<sup>6</sup> In view of these and undoubtedly other advantages, the practical potentiality of the inter vivos trust in estate planning is obvious.

The use of this appealing dispositive arrangement in lieu of a will, however, is impeded by the immense difficulty in discerning with any preciseness the degree to which the inter vivos trust and the will may be used interchangeably. The feature of a will which distinguishes it from other methods of disposition is that it remains ambulatory until the death of the testator.<sup>7</sup> In order,

<sup>1</sup> See, generally, 1 BOWE, *ESTATE PLANNING AND TAXATION* 183-188 (1957); CASNER, *ESTATE PLANNING*, 2d ed., 87-106 (1956); Heffernan and Williams, "Revocable Trusts in Estate Planning," 44 *CORN. L.Q.* 524 at 531-542 (1959); King, "Trusts as Substitutes for Wills," 14 *ROCKY MOUNTAIN L. REV.* 1 (1941). The use of an inter vivos trust in place of a will does not necessarily presuppose that the testamentary method of disposing of property at death is dispensed with entirely. An inter vivos trust may be utilized to dispose of part of the estate while a will is used conjointly to dispose of the rest.

<sup>2</sup> See CASNER, *ESTATE PLANNING*, 2d ed., 99 (1956); Heffernan and Williams, "Revocable Trusts in Estate Planning," 44 *CORN. L.Q.* 524 at 531-537 (1959).

<sup>3</sup> See CASNER, *ESTATE PLANNING*, 2d ed., 99 (1956). If the settlor should afterward become incompetent, the trust will still be operative to dispose of his property at his death, whereas the advent of his incompetency would render subsequent testamentary disposition open to attack. In addition, the inter vivos trust gives the settlor the reassurance of seeing his dispositive machinery in operation and having opportunity to defend it if attack is made on it during his lifetime. The possibility of an attack on the trust during the settlor's lifetime, however, is rather remote. See note 9 *infra*.

<sup>4</sup> See CASNER, *ESTATE PLANNING*, 2d ed., 100-102 (1956); Heffernan and Williams, "Revocable Trusts in Estate Planning," 44 *CORN. L.Q.* 524 at 538-539 (1959); King, "Trusts as Substitutes for Wills," 14 *ROCKY MOUNTAIN L. REV.* 1 at 3-4 (1941). For a comparison of the relative over-all costs of the inter vivos and testamentary trust, see 1 BOWE, *ESTATE PLANNING AND TAXATION* 186-187 (1957). Of course, whether the inter vivos trust would be less expensive may depend upon how long the settlor lives after executing it. In addition to avoiding delay and expense incident to probate proceedings, the use of the inter vivos trust avoids notoriety as to the dispositive arrangement.

<sup>5</sup> See CASNER, *ESTATE PLANNING*, 2d ed., 102 (1956); Heffernan and Williams, "Revocable Trusts in Estate Planning," 44 *CORN. L.Q.* 524 at 539 (1959).

<sup>6</sup> E.g., the spouse's election statute and the mortmain statute. Whether or not it is and should be possible to avoid these statutes by use of the inter vivos trust in place of a will is considered more fully later in this comment.

<sup>7</sup> *National Shawmut Bank v. Joy*, 315 Mass. 457 at 470, 53 N.E. (2d) 113 (1944).

therefore, for an inter vivos trust to take the place of a will, the settlor must reserve to himself some of the principal rights and powers of ownership.<sup>8</sup> The reservation of these rights and powers by the settlor adds to the trust, in varying degree, the ambulatory feature which is characteristic of a will. Emerging from the great body of litigation in this area, however, are limitations on the degree to which an inter vivos trust may be made ambulatory and still remain a valid trust.<sup>9</sup> This comment will be devoted to an examination of various tests of trust validity in this setting and their relative utility as tools for analysis.

### I. A TESTAMENTARY TEST

Where the validity of an alleged inter vivos trust is in issue, it appears anomalous to analyse the problem from the standpoint of whether the disposition is testamentary, that is, whether it is a will.<sup>10</sup> When an owner of property intends and attempts one type of disposition, to say that he has effected an entirely different type of disposition seems to be a needlessly roundabout way of saying that he has failed to accomplish his purpose. An underlying rationale for the indirect approach, however, may be found in the notion that it is inexcusably evasive to accomplish by one method of disposition that which has traditionally been done by another method governed by a different set of rules. According to this notion, a court, in order to prevent evasion, should look to the substance rather than the form of the transaction. The question to be examined is whether there is any room for this kind of reasoning in the setting of the inter vivos trust used in place of a will.

<sup>8</sup> Those most typically reserved are the right to income for life, the power to revoke, amend or modify, and the power in some form to control the administration of the trust without being a trustee.

<sup>9</sup> Theoretically, a trust may have been invalid from the start for the reason that title did not pass to the trustee, or because an agency rather than a trust relationship was created incident to an effective transfer of title. On the other hand, a trust may be invalid only after the death of the settlor. The usual example of the latter situation is where no interest passed *in praesenti* to the remainderman-beneficiary at the time of the creation of the trust. The instrument is not effective to pass an interest at the time of the settlor's death, because presumably it was not executed in accordance with the requirements of the statute of wills. For practical purposes, however, since an attack on the trust almost invariably comes after the death of the settlor, the words "valid" and "invalid" will be used in this comment to refer generally to whether the trust may be given operative effect after the death of the settlor, and not specifically to whether the trust was invalid *ab initio* or only at this later time.

<sup>10</sup> Although the courts and writers commenting on their decisions often conclude rather loosely that an alleged inter vivos trust is "testamentary," it is clear that what is meant is that the instrument does not effect a valid inter vivos disposition, and not that it is a will.

More specifically, do the rules which govern testamentary dispositions reflect policies of such importance that they should not be permitted to be "evaded" by the use of the inter vivos trust as a substitute for a will? Do they require a court to look behind the form to the substance of the transaction? To the extent to which these questions are answered in the affirmative, the indirect approach which places primary emphasis on whether the disposition is testamentary may be justified.

### A. *The Surviving Spouse*

One of the most significant and widespread rules governing testamentary disposition is found in statutes giving the surviving spouse an election to take against the will of the deceased spouse.<sup>11</sup> Although the majority of courts refuse to apply a different test for determining the validity of an inter vivos trust simply because the attack on the trust is by the surviving spouse,<sup>12</sup> there is merit in the argument that the policy behind the spouse's election statutes dictates that a more stringent test be employed. The substitutionary potentiality of the inter vivos trust should not be so complete as to provide a device whereby the surviving spouse can, in practical effect, be disinherited entirely.<sup>13</sup> Perhaps the easiest and most practicable solution, in light of the majority view, would be corrective legislation,<sup>14</sup> but unfortunately this solution has not been, and does not seem likely to be, generally adopted. In the absence of statutory aid, a minority of courts have offered solutions which have made inroads on the law governing inter vivos trusts. Some of these courts hold the trust voidable where there is proof of intent to deprive the spouse of the statutory share.<sup>15</sup> Others hold the trust void as to the spouse where it can be shown that the transfer was illusory.<sup>16</sup> The obvious defect in these solutions lies

<sup>11</sup> See statutes cited in 2 SCOTT, TRUSTS, 2d ed., §146A, n. 1 (1956).

<sup>12</sup> See, e.g., *Ascher v. Cohen*, 333 Mass. 397, 131 N.E. (2d) 198 (1956); *Rose v. Union Guardian Trust Co.*, 300 Mich. 73, 1 N.W. (2d) 458 (1942). These cases uniformly apply what will be referred to later in this comment as a "quantitative test" to all the inter vivos trust cases in this area regardless of who is making the attack on the trust. See also 1 TRUSTS RESTATEMENT SECOND §57, comment c (1959).

<sup>13</sup> See SIMES, PUBLIC POLICY AND THE DEAD HAND 25-31 (1955).

<sup>14</sup> See Simes, "Protecting the Surviving Spouse by Restraints on the Dead Hand," 26 UNIV. CIN. L. REV. 1 at 15-16 (1957); comment, 37 CORN. L.Q. 258 at 270 (1952) (recommending a legislative solution of this problem in the setting of the Totten trust); note, 40 GEO L.J. 109 at 121 (1951). See also Pa. Stat. Ann. (Purdon, 1950) tit. 20, §301.11, one of the few attempts which have been made to deal with this problem by legislation.

<sup>15</sup> *Martin v. Martin*, 282 Ky. 411, 138 S.W. (2d) 509 (1940); *Merz v. Tower Grove Bank & Trust Co.*, 344 Mo. 1150, 130 S.W. (2d) 611 (1939).

<sup>16</sup> *Harris v. Harris*, 147 Ohio St. 437, 72 N.E. (2d) 378 (1947); *Newman v. Dore*, 275 N.Y. 371, 9 N.E. (2d) 966 (1937).

in the often insurmountable difficulty of proving intent to deprive the spouse of the statutory share or illusoriness of the transfer. In addition, it is doubtful whether these rules do more than partially solve the problem. The policy behind the spouse's statutory share, if deemed applicable to transactions effected during the lifetime of the deceased, is not logically limited to transactions where there is an intent to evade it. It is aimed rather at ensuring that the surviving spouse will be provided for regardless of whether the decedent intends not to provide or fails to do so inadvertently. Nor is the policy behind the statutory share logically limited to illusory transfers. Moreover, this type of transfer is so ill-defined and apparently so infrequent that the inroad on the usual standard of validity is of dubious significance.<sup>17</sup> In view of these considerations, it would seem that a testamentary test of some sort could justifiably be applied. The following suggestion is made. If the inter vivos trust was used as a substitute for a will, it should be treated as a will at the instance of the surviving spouse, wholly without regard to the validity of the trust, on the ground that the policy of the spouse's election statute requires this result. The form of the transaction should be completely disregarded, and the court should look solely to its substance. The principal question, of course, is whether the trust was used as a substitute for a will. The determination of this question could be left to a vague approach as broad as the question itself, but this would do nothing to alleviate the defects inherent in the fraudulent intent and illusory transfer tests referred to above. To obtain predictable results, the analysis should turn upon some reservation of powers which gives the inter vivos trust to a substantial degree the ambulatory feature characteristic of a will. The test suggested here is reservation of the power to revoke, or its equivalent, and the right to receive income for life.<sup>18</sup> It could then be stated as a rule of simple and just application that the surviving spouse may elect to treat the remaining corpus of a "revocable" inter vivos trust with income for life to the decedent as part of his estate for the purpose of

<sup>17</sup> Compare *Newman v. Dore*, 275 N.Y. 371, 9 N.E. (2d) 966 (1937) with *Matter of Halpern*, 303 N.Y. 33, 100 N.E. (2d) 120 (1951). See Simes, "Protecting the Surviving Spouse by Restraints on the Dead Hand," 26 *UNIV. CIN. L. REV.* 1 at 7-15 (1957).

<sup>18</sup> The power to revoke and the right to income for life are not suggested at random. The settlor, when he uses an inter vivos trust in place of a will, almost invariably reserves the power to revoke or some related power which gives him the same control, such as a general power of appointment, because without such a power he does not have the ultimate means with which to effectuate a complete change of heart up to the time of his death. The additional reservation of a beneficial life interest means that the settlor in substance, although perhaps not in form, has given up nothing during his lifetime.

determining the statutory share. This standard of inter vivos trust validity would seem superior to other standards which have been suggested as solutions to this problem. The adoption by analogy of the standards applicable in the setting of federal estate taxation<sup>19</sup> has the undeniable virtue of certainty in view of the frequent interpretation which they have received, but the application of such far-reaching standards would have the undesirable effect of elevating the status of the surviving spouse to that of ward of the state. It is probable that the policy of freedom of alienation and stability of transfer would wither before such an encroachment. The solution offered by the Pennsylvania legislature<sup>20</sup> probably comes the closest to the standard suggested in this comment, but, as previously noted, it appears unlikely that other state legislatures will follow suit. The judicial solution seems more plausible, especially in view of the modern tendency to uphold the trust regardless of an overwhelming reservation of powers by the settlor, a tendency to be given more attention later in this comment. Suffice it to say here that as greater reservations of powers are permitted, there will be increasing pressure upon the courts to carve out an exception to the usual standards of validity in order to avoid the policy of protecting the widow from disinheritance.

### B. *Creditors' Rights*

Another familiar rule governing testamentary disposition is that the creditors at the death of the testator have a claim on his estate superior to that of the beneficiaries under his will.<sup>21</sup> The use of the inter vivos trust in place of a will presents the problem of whether the creditors at the death of the settlor have or should have a claim on the trust property superior to that of the remainderman-beneficiary. This problem has been resolved by statute in many states. One type of statute provides that if the settlor reserves a power of revocation, he shall be treated as absolute owner of the trust property so far as the rights of creditors are concerned.<sup>22</sup> Another statute allows a court of equity, at the suit of the creditors, to compel the settlor to exercise the power of revocation.<sup>23</sup> For obvious reasons, this statute has been held in-

<sup>19</sup> See Simes, "Protecting the Surviving Spouse by Restraints on the Dead Hand," 26 *UNIV. CIN. L. REV.* 1 at 15-16 (1957).

<sup>20</sup> Pa. Stat. Ann. (Purdon, 1950) tit. 20, §301.11.

<sup>21</sup> *ATKINSON, WILLS* 77 (1937).

<sup>22</sup> E.g., 49 N.Y. Consol. Laws (McKinney, 1945) §145; Ind. Stat. Ann. (Burns, 1951) §56-610.

<sup>23</sup> Ohio Rev. Code (Baldwin, 1958) §1335.01.

applicable after the death of the settlor.<sup>24</sup> Still another type of statute renders a transfer into trust for the use of the transferor void as against the creditors of the transferor.<sup>25</sup> It has been held that reservation of a power to revoke brings the transfer within the statute,<sup>26</sup> but the better view is that the statute does not apply if a beneficial interest resides in a person other than the transferor.<sup>27</sup> Finally, under the National Bankruptcy Act,<sup>28</sup> the trustee in bankruptcy may reach all powers which the bankrupt might have exercised for his own benefit. It would seem that this would include the power to revoke. Where these statutes apply to the inter vivos trust used in place of a will the result, in practical effect, is the application of a testamentary test of validity. The statutes broaden the definition of a will for the benefit of creditors, and the alleged inter vivos trust is approached from the standpoint of whether it falls within the statutory definition of a testamentary disposition.<sup>29</sup>

Absent an applicable statute the conveyance may still be regarded as a fraud on the creditors of the settlor, and therefore void at their election, if it was made with the intent to place property beyond the reach of either present or future creditors.<sup>30</sup> However, if there is no applicable statute and no fraud, the great weight of authority is to the effect that the creditors may not reach the interest of the remainderman-beneficiary.<sup>31</sup> Whether a testamentary test of the sort suggested in connection with the discussion of the statutory share of the surviving spouse should be applied for the benefit of creditors is a close question. It may be argued that the res of a revocable trust is substantially an asset in the hands of the settlor and should therefore be available for payment

<sup>24</sup> Schofield v. Cleveland Trust Co., 135 Ohio St. 328, 21 N.E. (2d) 119 (1939).

<sup>25</sup> E.g., Kan. Gen. Stat. Ann. (Corrick, 1949) §33-101; Wash. Rev. Code §19.36.202.

<sup>26</sup> Herd v. Chambers, 158 Kan. 614, 149 P. (2d) 538 (1944). However, this case is distinguishable on the ground that the settlor reserved a general power of appointment in addition to a power to revoke.

<sup>27</sup> See Van Stewart v. Townsend, 176 Wash. 311, 28 P. (2d) 999 (1934) (where the whole beneficial interest was in persons other than the settlor).

<sup>28</sup> 30 Stat. 544 (1898), as amended, 11 U.S.C. (1958) §110(a). In addition, the Bankruptcy Act provides that a transfer without consideration made by the bankrupt within one year of bankruptcy may be set aside in the bankruptcy proceedings. 11 U.S.C. (1958) §107(d)(2).

<sup>29</sup> This is also the practical effect of the federal estate tax statutes. See I.R.C., §§2036, 2038(a). No attempt has been made to include in this comment a discussion of the relation of the tax laws to the inter vivos trust used as a substitute for a will, because the tax laws so clearly reflect a policy which takes precedence over that of promoting free alienability.

<sup>30</sup> See 1 GLENN, FRAUDULENT CONVEYANCES AND PREFERENCES, rev. ed., §§316-340 (1940). Note the analogy here to some of the surviving spouse cases. See note 15 supra.

<sup>31</sup> See 1 PERRY, TRUSTS AND TRUSTEES, 7th ed., §96, p. 117 (1929). See also 92 A.L.R. 282 (1934).

of his just debt. On the other hand, it may be argued that persons who extended credit after the creation of the trust should be held to have contracted with respect to existing security. In the case of prior creditors, rebuttal of the creditors' argument by the trust beneficiary is more difficult. However, the plight of the creditor does not seem analogous to that of the surviving spouse, who may, for all practical purposes, be disinherited by the use of an inter vivos trust. The spouse can do nothing to obtain "security," whereas the creditor is generally in a position to refuse credit to one whom he considers a poor risk. The policy favoring those who cannot help themselves is stronger than that favoring those who can. In addition, the prevalence of statutes in this area indicates it is probably more sensible to conclude that the matter should be left to legislative discretion.<sup>32</sup>

### C. *Mortmain Statutes*

Another rule governing testamentary dispositions which should be briefly examined is the one embodied in so-called mortmain statutes. One type provides that a testator cannot devise or bequeath for charitable purposes more than a certain proportion of his property.<sup>33</sup> Another type precludes a testator from devising or bequeathing property for charitable purposes by a will executed within a specified period immediately prior to his death.<sup>34</sup> The question presented is whether the use of the inter vivos trust as a substitute for a will may or should avoid the operation of these statutes. The courts in general have been unwilling to apply a special test of validity where the inter vivos trust works a disposition which would have been invalid under the mortmain statutes if attempted by will.<sup>35</sup> There is at least one statute, however, which would require a contrary result if the trust is executed within one month before the settlor's death.<sup>36</sup> Assuming that a testamentary test or its statutory equivalent would be applied on behalf of the surviving spouse, the question is reduced to whether the expectancy of the children, parents and descendants should be protected as against an otherwise valid inter vivos trust for chari-

<sup>32</sup> Cf. note, 39 Ky. L.J. 131 at 134-135 (1950).

<sup>33</sup> E.g., 13 N.Y. Consol. Laws (McKinney, 1949) §17.

<sup>34</sup> E.g., Ohio Rev. Code (Baldwin, 1958) §2107.06.

<sup>35</sup> *Cleveland Trust Co. v. White*, 134 Ohio St. 1, 15 N.E. (2d) 627 (1938); *City Bank Farmers Trust Co. v. Charity Organization Society*, 238 App. Div. 720, 265 N.Y.S. 267 (1933), *affd. mem.* 264 N.Y. 441, 191 N.E. 504 (1934); *President of Bowdoin College v. Merritt*, (N.D. Cal. 1896) 75 F. 480.

<sup>36</sup> Pa. Stat. Ann. (Purdon, 1939) tit. 10, §12.

table purposes. A prominent writer has argued that what in effect would amount to a testamentary test should be judicially applied, citing as an analogy the problem as it arises with respect to the statutory share of the surviving spouse.<sup>37</sup> Since the expectancy of the children, parents and descendants may as easily be defeated by devise or bequest to a stranger, however, regardless of when the will is drawn or what percentage of the testator's property it involves, the analogy to the surviving spouse situation is not too well drawn. The policy behind the type of statute which prevents a devise or bequest to a charity within a certain period before the death of the testator would not seem to be primarily to prevent disinheritance. It appears aimed rather at preventing the bitterness or senility that sometimes accompanies old age from obscuring in the eyes of the testator the natural objects of his bounty. The policy behind the statutes which limit the percentage of property which may be devised or bequeathed to charity is probably in part aimed at preventing the same thing, even though the fact that it is applicable to a will which is drawn at any time during the life of the testator might indicate that the emphasis is on preventing disinheritance. Whatever the policy, in view of the fact that it may so easily be avoided either by outright gift to a charity during the life of the deceased or by devise or bequest to a stranger, it would hardly seem justifiable to apply a testamentary test to an inter vivos trust which may be availed of to accomplish a similar objective. Indeed, the limited effectiveness of the mortmain statutes suggests a legislative intent to confine their application to strictly testamentary dispositions.

#### D. *Inter Vivos Trusts in General*

The rules of most uniform application to testamentary dispositions, of course, are those contained in the statute of wills. Are the policy considerations which underlie the statute of wills such as to justify a testamentary test of the validity of inter vivos trusts in general when they are used in place of wills? The purpose of the statute of wills is to avoid fraudulent claims and otherwise to assure that a testamentary disposition is in accordance with the intention of the testator.<sup>38</sup> But is this purpose any different

<sup>37</sup> See 4 SCOTT, TRUSTS, 2d ed., pp. 2612-2613 (1956).

<sup>38</sup> See comment, 51 N.W. UNIV. L. REV. 113 (1956). The statute of wills seeks to provide assurance as to the intention of the testator not only to prevent fraudulent claims, but also to be assured that the testator meant his expressions to be given formal effect when he dies.

from that underlying the rules governing inter vivos conveyances? The answer must be negative. The stringency of the requirements for a valid will as compared to the requirements for a valid inter vivos disposition is explained by the fact that the testator, unlike an inter vivos conveyancer, is not present to defend and explain his intentions when they are sought to be given effect.<sup>39</sup> It is true that the attack on an inter vivos trust used in place of a will almost invariably comes after the death of the settlor, but, unlike the maker of a will, he has had an opportunity to see his dispositive arrangement in operation and presumably to revoke it if it is not in accordance with his intention. If there was ever thought to have been a policy underlying the statute of wills which was *sui generis*, it now seems clear that the courts no longer recognize it. The 1947 revision of section 57 of the *Restatement of Trusts* stated that if an interest passes to the beneficiary during the life of the settlor, a trust will not be held testamentary merely because certain types of powers are retained, "unless the terms are so informally stated and the power of control reserved is so great that it would violate the policy of the Statute of Wills to enforce it." The latest edition of the *Restatement* omits this quoted passage<sup>40</sup> and thereby supports the inference that the policy underlying the statute of wills is no longer regarded as inconsistent with informality and reservation of a large quantum of control. Virtually uncontradicted cases have declared that the fact that the settlor's intent was to evade the statute of wills is irrelevant to the question of the validity of an inter vivos trust.<sup>41</sup> Certainly if an evasive intent is the only basis upon which the strictest of courts will invalidate an otherwise valid inter vivos trust in the setting of the statutory share of the surviving spouse and of creditors' rights, it would follow a fortiori that the policy of the statute of wills does not justify application of a testamentary test to inter vivos trusts in general when they are used in place of wills. As applied to inter vivos trusts in general, then, the notion that it is inexcusably evasive to accomplish by one method of disposition that which may also be accomplished by another method is unsound. There is no

<sup>39</sup> In some particulars it may even be said that the requirements for a valid inter vivos disposition are stricter. Consider, for example, the requirement of delivery in the law of gifts. See BROWN, *PERSONAL PROPERTY*, 2d ed., §§38-45 (1955).

<sup>40</sup> See 1 *TRUSTS RESTATEMENT SECOND* §57 (1959).

<sup>41</sup> E.g., *Denver Nat. Bank v. Von Brecht*, 137 Colo. 88, 322 P. (2d) 667 (1958); *National Shawmut Bank v. Joy*, 315 Mass. 457, 53 N.E. (2d) 113 (1944); *Whalen v. Swircin*, 141 Neb. 650, 4 N.W. (2d) 737 (1942).

evasion which would justify a court's looking to the substance in disregard of the form of the transaction.

These considerations indicate that the testamentary test has limited utility as a tool of analysis. Bearing in mind the small areas in which it may be a justifiable test of the validity of an inter vivos trust used in place of a will, it is necessary to proceed to a consideration of the relative merits of two additional tests as applied to the larger residual area.

## II. A QUANTITATIVE TEST

By far the most frequently employed test of inter vivos trust validity in this residual area may be characterized as a "quantitative test." According to this test, the validity of the trust after the death of the settlor depends upon the cumulative effect of the powers which he has retained over the trust property and its management. If the settlor has kept back too many of the incidents of ownership, the trust will fail because<sup>42</sup> (1) no interest may be deemed to have passed *in praesenti* to the remainderman-beneficiary,<sup>43</sup> (2) no effective transfer has been made to the trustee,<sup>44</sup> (3) the trustee is merely the agent of the settlor,<sup>45</sup> or (4) the disposition is testamentary in nature.<sup>46</sup> In applying a quantitative test the court hypothesizes a never-defined line of demarcation fixing the outer limits of the extent to which an inter vivos trust may be used in place of a will. Each case requires a weighing of the total powers retained by the settlor, and if the scales are tipped, the trust is declared inoperative after his death.

Two basic objections can be made to a quantitative approach. First, since the line of demarcation is never defined, but only hy-

<sup>42</sup> The reasons given for the failure of the trust should not be mistaken for the test which is employed. The former are merely conclusions of law while the latter is the tool used for analysis. But see 1 TRUSTS RESTATEMENT SECOND §57 (1959), which says: "Where an interest in the trust property is created in a beneficiary other than the settlor, the disposition is not . . . invalid . . . merely because the settlor reserves a beneficial life interest or because he reserves in addition . . . [various powers]." It would seem, however, that the creation of an interest in a beneficiary other than the settlor is not intended to be made a determinant of trust validity. The cases relied upon by the reporter generally apply what has been referred to here as a quantitative test. See 3 TRUSTS RESTATEMENT SECOND §57 (Reporter's Notes) (1959).

<sup>43</sup> See 1 SCOTT, TRUSTS, 2d ed., §56 (1956).

<sup>44</sup> Atlantic Nat. Bank v. St. Louis Union Trust Co., 357 Mo. 770, 211 S.W. (2d) 2 (1948).

<sup>45</sup> Smith v. Simmons, 99 Colo. 227, 61 P. (2d) 539 (1936). An alleged trustee may have acquired legal title and still remain the agent of the settlor. See 1 SCOTT, TRUSTS, 2d ed., §57.2, p. 450 (1956).

<sup>46</sup> Application of Cerchia, 279 App. Div. 734, 108 N.Y.S. (2d) 753 (1951). See note 10 supra.

pothesized, the test does not produce maximum predictability, a desirable effect of a rule of law. This does not mean, of course, that the decided cases have no precedent value. For example, it is well settled that an inter vivos trust is not invalid where the settlor transfers in trust, reserving a beneficial life estate and a power to revoke, amend or modify the trust.<sup>47</sup> The same is true where the settlor declares a trust reserving the same incidents of ownership.<sup>48</sup> The precedent value of the decided cases, however, is derived from a comparison of the facts involved, rather than resting upon a definitive rule of law of more general application. This point is emphatically illustrated by reference to the most contentiously litigated reservation of power in this area—the power to participate in the administration of the trust without being a trustee. The modern cases accept the general proposition that some measure of control over the administration of the trust may be retained,<sup>49</sup> but even this assurance was hard won at the cost of much needless litigation.<sup>50</sup> The modern cases are in confusion, however, over the extent of control which is permissible.<sup>51</sup> This confusion is inherent in the test which is employed. Depending as it does upon a degree standard, a quantitative test gives no definite answer to questions posed by the multitudinous types of control which might be retained over the administration of the trust. A separate answer must be given as to the propriety of each type of control. Thus, the conclusion seems inescapable that a quantitative test is not sufficiently informative to the estate planner who must know to what extent the inter vivos trust and the will may be used interchangeably.

The second objection to a quantitative test is more fundamental. Like a testamentary test, although admittedly to a lesser degree, a quantitative test is founded upon the notion that the

<sup>47</sup> *Denver Nat. Bank v. Von Brecht*, 137 Colo. 88, 322 P. (2d) 667 (1958); *Ascher v. Cohen*, 333 Mass. 397, 131 N.E. (2d) 458 (1956). For further cases, see 1 SCOTT, TRUSTS, 2d ed., §57.1, n. 1 (1956).

<sup>48</sup> *Ridge v. Bright*, 244 N.C. 345, 93 S.E. (2d) 607 (1956); *Farkas v. Williams*, 5 Ill. (2d) 417, 125 N.E. (2d) 600 (1955). For further cases, see 1 SCOTT, TRUSTS, 2d ed., §57.6, n. 2 (1956).

<sup>49</sup> *Denver Nat. Bank v. Von Brecht*, 137 Colo. 88, 322 P. (2d) 667 (1958); *Rippon v. Mercantile-Safe Deposit & Trust Co.*, 213 Md. 215, 131 A. (2d) 695 (1957); *Estate of Steck*, 275 Wis. 290, 81 N.W. (2d) 729 (1957); *Ridge v. Bright*, 244 N.C. 345, 93 S.E. (2d) 607 (1956).

<sup>50</sup> See *Warsco v. Oshkosh Savings & Trust Co.*, 183 Wis. 156, 196 N.W. 829 (1924), made obsolete by a statute making such a trust valid, Wis. Stat. Ann. (1957) §231.205; *Smith v. Ferguson*, 90 Ind. 229, 46 Am. Rep. 216 (1883) which was also probably made obsolete by a statute making such a trust valid, Ind. Stat. Ann. (Burns, 1953) §6-509.

<sup>51</sup> The similarity of fact situations which have brought contrary results in different jurisdictions employing the same test of validity is striking. For example, compare *Hanson v. Denckla*, (Fla. 1956) 100 S. (2d) 378, *revd.* on other grounds, 357 U.S. 235 (1958) with *Stouse v. First Nat. Bank of Chicago*, (Ky. 1951) 245 S.W. (2d) 914.

distinction between inter vivos and testamentary dispositions is one of substance rather than purely one of form. It is a general rule of conveyancing that a reservation of less than all that is conveyed, provided that it is in the form of a condition subsequent, will not invalidate the conveyance or the condition subsequent. This is a rule of form. There is an exception to this rule, of course, where a reservation of powers contravenes some established policy. This exception is concerned with the substance of the transaction. Leaving aside those instances discussed under the heading of "A Testamentary Test" where it was concluded that it was justifiable to look to the substance of the transaction, it is difficult to support any additional deviation from the general rule which is concerned only with form. No one is hurt whom it is the policy of the law to protect. No compelling reason exists why maximum effect should not be given the intention of the owner of property in making disposition thereof.<sup>52</sup> The conclusion is manifest, therefore, that a quantitative test as applied generally to inter vivos trusts used in lieu of a will is devoid of underlying justification.

In light of these criticisms directed at a quantitative test, it now remains to inquire whether there is another method of analysis which may produce greater predictability, and which is more capable of justification with regard to underlying rationale.

### III. FORM OF WORDS AS MEASURING VALIDITY

In formulating a more fruitful method of analysis, the guiding consideration should be that maximum effect be given to the intention of the donor insofar as it is consistent with formal rules of conveyancing and related public policy. The suggested standard is that the form of the words used by the settlor shall determine the validity of a trust not executed in compliance with the statute of wills. Under this test the relevant inquiry is whether the settlor intended a trust operative during his lifetime, as opposed to an agency relationship between himself and the alleged trustee.<sup>53</sup>

<sup>52</sup> See the discussion, *supra*, concerning whether or not the policy behind the statute of wills justifies the application of a testamentary test to the inter vivos trust in general. The same conclusions would apply with equal force to a quantitative test.

<sup>53</sup> It has been well stated that "The two relations, trust and agency, apparently grew from the same sources, but one developed in equity and the other in law. As a result there are, today, differences in legal incidents which attend the two relationships, but no determinant, save perhaps the intent of the parties, by which a particular arrangement may be recognized as one or the other." Comment, 14 WASH. AND LEE L. REV. 331 at 334-335 (1957).

This intent should be considered presumptively established by the words which the settlor employs in making the transfer. If he says "trust" and describes the legal incidents of a trust, these words should control, regardless of the quantum of reserved powers. But if it should appear that in actual operation the relationship between transferee and settlor was in fact inconsistent with trust, then it would be open by parol to rebut the presumption arising from the words employed.<sup>54</sup> It should not be supposed, of course, that this emphasis upon intent, of itself, is much of an innovation. In a number of cases it was thought to be of controlling importance whether the settlor intended to execute a trust operative during his lifetime.<sup>55</sup> Other cases which emphasize form in connection with the transfer reflect a similar consideration.<sup>56</sup> The novelty of the proposed test lies rather in the fact that it would exclude all other inquiries in the absence of facts calling into play an established policy of protecting surviving spouses or creditors or a policy against certain kinds of charitable bequests.

As indicated above, modern cases have been primarily concerned with the effect to be attributed to control retained over the administration of the trust. A quantitative test was seen to have hypothesized a line marking the number and significance of the duties which the trustee must be given to perform without necessity of deferring to the unbridled discretion of the settlor. What effect would the application of the proposed test have upon the retention of control by the settlor over the administration of the trust? The requirement that there be a manifestation of an intention to create a trust means that the owner of the property must intend to create the legal incidents of a trust.<sup>57</sup> One of the legal incidents of a trust is a trustee with duties to perform independent-

<sup>54</sup> See *Hanson v. Denckla*, (Fla. 1956) 100 S. (2d) 378 at 384, *revd.* on other grounds 357 U.S. 235 (1958), where the court thought it to be of importance that the settlor frequently exercised his reserved power to appoint beneficiaries, as bearing on whether he regarded the trust as ambulatory in nature. The parol evidence rule does not stand in the way, especially in view of the fact that the only real difference between an agency and a trust is the intention of the parties. Evidence of intent would seem to fall clearly within the ambiguous instrument exception to the parol evidence rule. See McCORMICK, *HANDBOOK ON THE LAW OF EVIDENCE* §220 (1954).

<sup>55</sup> *Dunham v. Armitage*, 97 Colo. 216, 48 P. (2d) 797 (1935) (striking down an alleged trust on the ground that no trust was intended); *American Bible Soc. v. Mortgage Guaranty Co.*, 217 Cal. 9, 17 P. (2d) 105 (1932) (upholding the trust on the ground that one was intended, without reference to the possibility of holding it testamentary).

<sup>56</sup> E.g., *Stouse v. First Nat. Bank of Chicago*, (Ky. 1951) 245 S.W. (2d) 914; *Sheasley Trust*, 366 Pa. 316, 77 A. (2d) 448 (1951); *Rose v. Union Guardian Trust Co.*, 300 Mich. 73, 1 N.W. (2d) 458 (1942).

<sup>57</sup> See 1 SCOTT, *TRUSTS*, 2d ed., §23 (1956).

ly of the discretion of the settlor.<sup>58</sup> Unlike a quantitative test, however, the proposed test is satisfied so long as there are any duties given the trustee, regardless of when they are to be performed or of how significant they may be.<sup>59</sup> The proposed test is not one of degree, but rather one of presence or absence of the formal requisites of a trust. Given any duties in the trustee, the only relevant evidence that would support a finding of invalidity is parol evidence that the settlor did not actually intend what he described, as where he actually did exercise an unbridled discretion over the administration of the trust without protest on the part of the trustee.<sup>60</sup>

As the above discussion illustrates, the proposed test will create a greater degree of predictability than others discussed. The court does not hypothesize an undefined line which allows it to pick and choose on the facts of each case between duties given and powers retained. Predictability is predicated on a definitive rule of general application rather than upon comparison of the facts of prior cases.

From the standpoint of underlying justification, the proposed test likewise seems to be on sounder ground. There is no artificial limit to the powers that may be reserved in the form of conditions subsequent in the absence of a policy which requires the application of an alternative testamentary test such as that discussed above. In short, by looking to form rather than substance maximum effect is given to the intention of the donor where there is no discernible reason why it should not be given effect.

It remains to be seen how and to what extent the new test fits into existing law. Is it a practical and logical evolution of existing law, or is it merely wishful thinking without any practicable possibilities? Even though the courts have, by virtue of the vagueness of the quantitative test now employed, retained power to strike down a trust, the definite trend of the cases over the past decade has been toward upholding trusts notwithstanding larger

<sup>58</sup> Even in the case of a declaration of trust, the declarer-trustee is not free to do with the property as he wishes, but is bound by the terms of the trust. 1 SCOTT, TRUSTS, 2d ed., §17.1 (1956).

<sup>59</sup> Of course, the proverbial "hard case" where the settlor reserves virtually all that was transferred presents theoretical difficulties. However, the writer does not feel that the hard case requires him to relent. From a practical standpoint, the really hard case almost never occurs for the reason that the settlor has no need of reserving such a large quantum of powers in order to accomplish his purpose. In addition, the admission of degree would leave the proposed test open to the same criticisms as those directed at a quantitative test.

<sup>60</sup> See note 54 supra.

and larger reservations of power.<sup>61</sup> It would seem that the logical extension of these cases and the ultimate result of the trend which they represent could be that the form of the transaction will control without regard to any substantive inconsistency suggested by the powers reserved. Having reached this point, if the courts continue to refuse to distinguish between an attack by a surviving spouse (and perhaps a creditor of the settlor) and an attack by a disappointed would-be legatee, it is reasonable to anticipate that legislation would be forthcoming to require them to do so. It would appear, therefore, that the law is moving toward the dual standards described in this comment as the testamentary test and the formal, or intent, test.

*Stephen B. Flood, S. Ed.*

<sup>61</sup> See, e.g., *Denver Nat. Bank v. Von Brecht*, 137 Colo. 88, 322 P. (2d) 667 (1958); *Rippon v. Mercantile-Safe Deposit & Trust Co.*, 213 Md. 215, 131 A. (2d) 695 (1957); *Estate of Steck*, 275 Wis. 290, 81 N.W. (2d) 729 (1957); *Ridge v. Bright*, 244 N.C. 345, 93 S.E. (2d) 607 (1956); *Farkas v. Williams*, 5 Ill. (2d) 417, 125 N.E. (2d) 600 (1955); *Stouse v. First Nat. Bank of Chicago*, (Ky. 1951) 245 S.W. (2d) 914; *Sheasley Trust*, 366 Pa. 316, 77 A. (2d) 448 (1951); *Leahy v. Old Colony Trust Co.*, 326 Mass. 49, 93 N.E. (2d) 238 (1950); *Merchants Nat. Bank v. Weinold*, 12 Ill. App. (2d) 209, 138 N.E. (2d) 840 (1956); *MacGregor v. Fox*, 280 App. Div. 435, 114 N.Y.S. (2d) 286 (1952), *affd. mem. sub nom. Matter of MacGregor*, 305 N.Y. 576, 111 N.E. (2d) 445 (1953); *Matter of Ford*, 279 App. Div. 152, 108 N.Y.S. (2d) 122 (1951), *affd. mem.* 304 N.Y. 598, 107 N.E. (2d) 87 (1952).