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ANNUITIES - RIGHT OF LEGATEE, FOR WHOSE BENEFIT THE PURCHASE OF AN ANNUITY IS DIRECTED, TO RECEIVE THE PRINCIPAL IN LIEU THEREOF

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COMMENTS

ANNUITIES — RIGHT OF LEGATEE, FOR WHOSE BENEFIT THE PURCHASE OF AN ANNUITY IS DIRECTED, TO RECEIVE THE PRINCIPAL IN LIEU THEREOF — The rule has become well established in England

that, where a testator bequeaths an annuity for life to his beneficiary and directs his executor or trustee to purchase the annuity with assets of the estate, the annuitant[1] has an option to demand the purchase money in lieu of the annuity.[2] The direction to purchase the annuity is clothed by the courts with a power to change the mere gift of an annuity into a gift in the alternative of the principal or the annuity. This direction indicates the will of the testator that a fund representing the principal of the annuity should be severed completely from the bulk of his estate and devoted to the sole benefit of the annuitant.[3] As a consequence of such severance the fund is considered to be wholly within the control of the legatee. The result follows with equal precision whether testator gives a definite sum of money to his executor and directs him to devote it to an annuity of such amount as may be bought therewith,[4] or directs the executor to purchase an annuity of stipulated amount and to use such money as will be required.[5] Although the problem has been squarely presented to the American courts on but few occasions, those occasions have resulted in the adoption of the English rule without hesitation or comment.[6] In view, however, of the comparative originality of the problem in American jurisdictions, it would appear worthwhile to question whether the English rule should be further followed in this country.

One of the principal arguments upon which the rule finds support is based upon the alienability of annuities. In *Barnes v. Rowley*,[7] the earliest authority for the annuitant's right of election, the court ex-

[1] The annuitant must be sui juris in order to exercise his election. It is, of course, required that the annuitant have sole and absolute interest in the annuity. Grove's Trusts, 1 Giff. 74, 65 Eng. Rep. 831 (1859); Wright v. Callender, 2 De G. M. & G. 652, 42 Eng. Rep. 1027 (1852); 33 L. R. A. (N. S.) 979 (1911).

[2] In re Brunning, [1909] 1 Ch. 276; In re Robbins, [1906] 2 Ch. 648; In re Mabbett, [1891] 1 Ch. 707; Wakeham v. Merrick, 37 L. J. Ch. 45 (1867); In re Browne's Will, 27 Beav. 324, 54 Eng. Rep. 127 (1859); Ford v. Batley, 17 Beav. 303, 51 Eng. Rep. 1051 (1853); 2 JARMAN, WILLS, 7th ed., 1109 (1930).

[3] In re Oakley's Estate, 142 Misc. 1, 254 N. Y. S. 306 (1931); In re Proctor's Will, 235 App. Div. 6, 255 N. Y. S. 722 (1932); In re Adriance's Estate, 158 Misc. 857, 286 N. Y. S. 936 (1936).

[4] Barnes v. Rowley, 3 Ves. Jun. 305, 30 Eng. Rep. 1024 (1797).

[5] Ford v. Batley, 17 Beav. 303, 51 Eng. Rep. 1051 (1853).

[6] Parker v. Cobe, 208 Mass. 260, 94 N. E. 476 (1911); Reid v. Brown, 54 Misc. 481, 106 N. Y. S. 27 (1907); Estate of Cole, 219 N. Y. 435, 114 N. E. 785 (1916); In re Bertuch's Will, 225 App. Div. 773, 232 N. Y. S. 36 (1928); 29 COL. L. REV. 370 (1929).

[7] 3 Ves. Jun. 305, 30 Eng. Rep. 1024 (1797). The earlier case of Yates v. Compton, 2 P. Wms. 309, 24 Eng. Rep. 743 (1725), is frequently cited in support of annuitant's right of election; but in that case annuitant was also residuary legatee and so her estate would have received the principal in any event, and it is probable that the real issue involved an aspect of the doctrine of equitable conversion.

plained that the annuitant's power to sell the annuity after it has been purchased for him renders it wholly useless for the court to require the annuitant to accept the annuity if he would prefer its purchase price. This same explanation is repeated without discussion in the other early English cases, and *Barnes v. Rowley* is cited as conclusive on the subject.[8] Nor could a testator circumvent the rule by stipulating that the annuity should not be alienable; the courts simply dismissed the stipulation as ineffective.[9] Long before the annuity cases came before the English courts it had been established that, where a testator directed his executor to sell specific property and turn over the proceeds to a legatee, the legatee had a right to demand the specific property if he so desired; or, if a testator bequeathed a sum of money to his executor with a direction to purchase certain property and turn over such property to a legatee, the legatee might elect to receive the money in lieu of the property.[10] This class of cases rested upon the futility of requiring an execution of the conversion against the wishes of the beneficiary; the futility was explained by the alienability of the property as soon as it should reach the hands of the beneficiary. Thus, if a testator directed his executor to sell certain land and turn over the proceeds to the beneficiary, the beneficiary may buy in the land himself and immediately receive back as proceeds the purchase price he has paid; if a testator directed his executor to utilize a certain fund to buy land for the beneficiary, the beneficiary may sell the land immediately after he receives it and there will be no reason why he should not realize the sum set aside by testator, for the land will presumably be worth the price for which it was so recently purchased. It is difficult to raise any objection to the election in this class of cases, and the legatee's power of alienation is a sound argument for the result. It is possible that the English courts assumed that the cases involving annuities were but members of the same class and presented merely another aspect of the same problem. The English cases contain no express reference to such an approach, nor are cases of the type mentioned cited in support of the

[8] Bayley v. Bishop, 9 Ves. Jun. 6, 32 Eng. Rep. 501 (1803); Palmer v. Craufurd, 3 Swans. 483, 36 Eng. Rep. 945 (1819); Dawson v. Hearn, 1 Russ. & M. 606, 39 Eng. Rep. 232 (1831); Ford v. Batley, 17 Beav. 303, 51 Eng. Rep. 1051 (1853).

[9] Woodmeston v. Walker, 2 Russ. & M. 197, 39 Eng. Rep. 370 (1831); Brown v. Pocock, 2 Russ. & M. 210, 39 Eng. Rep. 374 (1833). The same argument is made here as in the case of disabling restraints upon the alienability of land, viz., the restraint is repugnant to the absolute interest given.

[10] Benson v. Benson, 1 P. Wms. 130, 24 Eng. Rep. 324 (1710); Seeley v. Jago, 1 P. Wms. 389, 24 Eng. Rep. 438 (1717); Attorney-General v. Weymouth, 1 Amb. 20, 27 Eng. Rep. 11 (1743); Seamer v. Bingham, 3 Atk. 54, 26 Eng. Rep. 834 (1743). These are early cases in the development of the doctrine of equitable conversion and reconversion. See annotation at 130 A. L. R. 1379 (1941).

annuity doctrine; however, *Parker v. Cobe*,[11] the leading American case, hints at a similarity between the two situations. Whether or not the English doctrine relating to an annuitant's right of election was derived from the already established doctrine of equitable reconversion, the dissimilarity between the two types of case makes manifest the fallacy of basing an annuitant's right of election upon the power of the annuitant to sell or assign his annuity.

The fundamental assumption of the rule allowing a legatee to elect between a specific article and the fund set aside for its purchase is that the article may be sold by the legatee for a sum equal to its purchase price. But such an assumption should not be made when the article to be bought is an annuity. The annuitant will be able to sell his annuity only at a price considerably less than the principal. It is extremely unlikely that the annuitant will find a purchaser who will bear the risk of the annuitant's death before the period of his life expectancy is completed for the same price that an annuity company will bear the risk of the annuitant outliving his normal life expectancy. The purchaser will protect himself by buying at a discount because he cannot protect himself by utilization of the law of averages. The annuity, unlike other articles, will terminate at the death of the annuitant; [12] this introduces an element of uncertainty which must reflect in its market value. It is extremely doubtful that purchasers would be willing to invest in this type of property without a substantial reduction from the original purchase price even if this element of uncertainty were not present.If alienation will not realize a sum equal to the principal of the annuity, how can the power of alienation be an adequate reason for allowing the annuitant to receive the principal? Further, the necessity of a sacrifice sale will operate to some extent as an inherent restraint upon the alienability of the annuity. It is not correct to allow an annuitant to receive the principal for the sole reason that he might accomplish the result by his own action if the election were to be denied.

[11] 208 Mass. 260, 94 N. E. 476 (1911). This case also tries to bring the annuity question within a general doctrine respecting a bequest of an absolute legacy accompanied by an admonition that legatee use it for a particular specified purpose. It is difficult to see the similarity between such a case and the annuity problem; the English cases never used such an approach.

[12] It is possible to create a perpetual annuity as well as an annuity for life, but the creation of a perpetual annuity requires explicit evidence that such is the creator's intent. It seems proper to construe the gift of a perpetual annuity as a gift of the principal. But the English cases have arrived at the conclusion that bequest of an annuity accompanied by direction that the annuity be purchased out of the estate is a perpetual annuity because the annuitant has the right to receive the principal. Kerr v. Middlesex Hospital, 2 De G. M. & G. 576, 42 Eng. Rep. 996 (1852). It is circular, therefore, to explain the annuitant's election by saying that he was given a perpetual annuity. In the question under consideration testator has expressly directed purchase of an annuity for life.

A more fundamental argument for the English rule of election is adduced from the annuitant's sole and absolute ownership of the annuity. If the annuitant is the only person interested in the legacy, who has a right to object if he wishes to take the principal dedicated to his welfare rather than the annuity? There is no such person other than himself: there is no other legatee owning an interest in the principal; the executor can derive no benefit if the right of election be denied; and the estate of the testator will be diminished to the extent of the principal whether an annuity is bought or the principal is given to the annuitant. But can it be doubted that the intention of the testator is completely disregarded if his gift becomes a gift of the principal in place of a gift of an annuity? The English cases make it quite clear that the testator's intention is not material by declaring void an express stipulation by the testator that his beneficiary shall have no right to receive the principal in lieu of the annuity.[13] The frustration of testator's intent is strikingly illustrated by those cases in which the annuitant dies before the annuity has been purchased. In such event the principal is awarded to the annuitant's estate on the theory that his legacy really amounted to a gift of the principal.[14] From that starting point it is only necessary to apply the law relative to any legacy which has vested in interest before the death of the legatee. It is not even required that the annuitant should survive the time when the annuity was directed to be bought.[15] In justification of this result it could be argued that the annuitant's personal incompetencies no longer constitute a barrier to outright payment of the principal, but would it not be more in accord with testator's intention to declare the legacy failed and permit the

[13] Stokes v. Cheek, 28 Beav. 620, 54 Eng. Rep. 504 (1860); In re Nunn's Trusts, L. R. 19 Eq. 331 (1875). But testator may prevent an election by annuitant where he imposes forfeiture of the annuity with gift over to third persons in the event of alienation by the annuitant. Power v. Hayne, L. R. 8 Eq. 262 (1869); Hatton v. May, 3 Ch. D. 148 (1876); In re Draper, 57 L. J. Ch. 942 (1888); 33 L. R. A. (N. S.) 979 (1911). Two reasons are given for recognition of this type of restraint: first, the intent of testator that annuitant shall not receive the principal if manifest, and, second, the principal must be withheld if the executor is to be able to pay over to a third person on happening of the event.

[14] Barnes v. Rowley, 3 Ves. Jun. 305, 30 Eng. Rep. 1024 (1797); Bayley v. Bishop, 9 Ves. Jun. 6, 32 Eng. Rep. 501 (1803); Palmer v. Craufurd, 3 Swans. 483, 36 Eng. Rep. 945 (1819); Dawson v. Hearn, 1 Russ. & M. 606, 39 Eng. Rep. 232 (1831); In re Robbins, [1906] 2 Ch. 648; In re Brunning, [1909] 1 Ch. 276. It would seem debatable whether annuitant has a right of election because the direction to purchase constitutes an outright legacy of the principal, or whether the direction to purchase constitutes an outright legacy of the principal because annuitant has the right of election. As far as historical development reveals, the early cases (such as Barnes v. Rowley) found an outright legacy of the principal on the ground that annuitant had an election; and the later cases (such as Ford v. Batley) supported the right of election by citation of Barnes v. Rowley, etc.

[15] In re Robbins, [1906] 2 Ch. 648.

principal to fall back into his own estate? [16] The legacy must have been intended as a gift personal to the annuitant or an annuity limited to his life would not have been prescribed. Further, if an anuity has been bought in fact, no part of the principal would be due the annuitant's estate at death.

This disregard of testator's intention is consistent with the general trend of English law. The broad policy of English law is to give complete power and control over property to the person who owns the sole and absolute interest therein. This policy is illustrated by the doctrine which permits a cestui que trust to terminate the trust without regard to the intention of the testator.[17] But the American courts, before the annuity cases were first encountered, had adopted a contrary policy, the policy of allowing a testator to make such disposition of his property as he wished and lending the aid of the courts to enforcement of the disposition after it has been made. As established by the leading case of *Claflin v. Claflin*,[18] the fact that a beneficiary held an absolute and sole interest was not sufficient to defeat the intent of the testator. Having established such a policy, it becomes difficult to explain why the American courts retreated in the annuity case. As Professor Scott says, "It is, however, more remarkable that the American courts should disregard the intention of the testator." [19] The Massachusetts court did recognize the existence of such a doctrine when it decided *Parker v. Cobe*,[20] but dismissed it with the words: "The case at bar is not a case where $75,000 was left upon the trust that the income of it should be paid to Ruth H. Cobe during her life, but it is a case where the $75,000 was to be laid out by the trustees in the purchase of an annuity for Ruth H. Cobe during her life. For that reason it is not a case within the rule of *Claflin v. Claflin*. . . ." Now, it may be true that the *Claflin* doctrine only extends to a trust in the technical sense, but if the *Claflin* doctrine is an expression of a general policy to effectuate the intention of the testator wherever possible there is no reason to restrict the policy to cases involving a technical trust. In substantial effect a

[16] Any arrears in annuity payments which have accrued should, nevertheless, be paid into the annuitant's estate. In those cases where the estate proves insufficient to pay all legacies and annuities, the annuity will abate proportionately with the other legacies. In such a case there is justification for payment of the principal to the annuitant rather than requiring purchase of an annuity with the remaining capital; testator's plan of disposition has been thwarted anyway, and the court cannot carry out his exact intention. Chemical Bank & Trust Co. v. Barnett, 114 N. J. Eq. 4, 168 A. 173 (1933).

[17] Josselyn v. Josselyn, 9 Sim. 63, 59 Eng. Rep. 281 (1837); Saunders v. Vautier, 4 Beav. 115, 49 Eng. Rep. 282 (1841).

[18] 149 Mass. 19, 20 N. E. 454 (1889). See 3 SCOTT, TRUSTS, § 337.3 ff. (1939).

[19] 3 SCOTT, TRUSTS § 346, pp. 1898-1899 (1939).

[20] 208 Mass. 260 at 263, 94 N. E. 476 (1911).

gift of an annuity for life will work out in a manner similar to a trust for the payment of income if the annuitant is not permitted to disrupt the testator's plan by taking the principal in lieu of the annuity. It is certainly no answer to say that testator could have created a technical trust if he wanted to prevent the annuitant from taking the principal; nor is it an answer to say that testator must have intended a gift of the principal inasmuch as he is presumed to know that the law will give the annuitant a right to elect to receive the principal.[21]

It is to be hoped that American courts in the future will examine the annuity problem more critically and will not be content with mere citation of *Parker v. Cobe, Estate of Cole,* and the English cases. If the annuity case calls for application of a policy different from that underlying the *Claflin* doctrine, perhaps the reason therefor will be explained in the future. But, in New York at least, the inconsistency of the annuity doctrine has been recognized and acted upon by the legislature.[22] The annuity presents a very simple method whereby a testator, without use of the more complicated and expensive trust device, may insure the future welfare of his beneficiary and also eliminate anxieties aroused by his beneficiary's facility in disposing of property. Its usefulness should not be impaired without a substantial reason for so doing.

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[21] Reid v. Brown, 54 Misc. 481, 106 N. Y. S. 27 (1907); Estate of Cole, 219 N. Y. 435, 114 N. E. 785 (1916).

[22] 13 N. Y. Consol. Laws (McKinney, Supp. 1942), "Decedent Estate Law," § 47-b: "If a person hereafter dying shall direct in his will the purchase of an annuity, the person or persons to whom the income thereof shall be directed to be paid shall not have the right to elect to take the capital sum directed to be used for such purchase in lieu of such annuity except to the extent the will expressly provides for such right, or except to the extent that the will expressly provides that an assignable annuity be purchased." See In re Geis' Estate, 167 Misc. 357, 3 N. Y. S. (2d) 770 (1938), and In re Fischer's Estate, 261 App. Div. 252, 25 N. Y. S. (2d) 140 (1941); both of these cases were decided prior to the effectiveness of the 1941 amendment to the statute.

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