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Series E Bonds--Ownership--Transferability and Creditors' Rights--Taxation

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NOTES

SERIES E BONDS[1] — OWNERSHIP — TRANSFERABILITY AND CREDITORS' RIGHTS — TAXATION. — The federal government, through the agency of the Treasury Department, is pursuing a fundamental fiscal and social policy by the continuing sale to the public of savings bonds, particularly Series E. The government has two primary aims: (1) to check inflation and (2) to spread ownership of the national debt among as many members of the public as possible.[2] The effectuation of that policy has been hindered in part by discordant conclusions as to the precise nature of the legal interests created in the bonds and in part by judicial nullification of the treasury regulations governing them, both of which have impaired the attractiveness of the bonds by subjecting them to increasing litigation. It is the purpose of this note to

1. Although the following discussion proceeds in terms of Series E bonds, it is, of course, applicable to all series of savings bonds to the extent that they are governed by the same regulations.

2. Speaking of Bonds, United States Savings Bonds Division, Treasury Department (June, 1946), 2.

discuss briefly the various problems which arise concerning ownership, transferability and creditors' rights, and taxation.

I. Ownership

United States savings bonds are issued under the authority of Section 22 of the Second Liberty Bond Act, as amended.[3] Pursuant to the provision therein that "The various issues and series . . . shall be issued in such manner and subject to such terms and conditions . . . as the Secretary of the Treasury may from time to time prescribe," the Treasury Department has issued regulations[4] referred to in the bonds and forming a part thereof. Savings bonds are issued only in registered form, and the form of registration is considered to be conclusive of the ownership and interests therein,[5] except as otherwise specifically provided by the regulations.[6] A purchaser of Series E bonds may register them in the name of a sole owner, two coowners, or an owner and a beneficiary.[7] Payment to the owner upon his separate request terminates any interest of the coowner or the beneficiary in the bond.[8] If the owner dies prior to presentation and surrender of the bond for payment or authorized reissue, sole and absolute ownership of the bond vests in the other named survivor.[9]

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3. 40 Stat. 288, § 22 (1917), as amended, 31 U. S. C. § 757c (Supp. 1946).

4. Treas. Dept. Cir. No. 530, 6th Revision, Feb. 13, 1945, 31 Code Fed. Regs., Part 315 (Supp. 1945). Numbering of the sections has varied from year to year and from regulation to regulation. To avoid confusion in the discussion of cases the writer has converted all section numbers to correspond with those of the regulations now in effect.

5. 31 Code Fed. Regs. § 315.2 (Supp. 1945).

6. The only qualification of § 315.2 appears in § 315.13 in which it is provided that conflicting claims as to ownership will be recognized when established by valid judicial proceedings. But see infra note 8 and text to note 69.

7. 31 Code Fed. Regs. § 315.4(a) (Supp. 1945). The Series E bond may be registered only in the names of natural persons, adults or minors. The coownership form permits the naming of two and only two persons in the alternative as coowners.

8. 31 Code Fed. Regs. § 315.45(a) (Supp. 1945). "During the lives of both coowners the bond will be paid to either coowner upon his separate request without requiring the signature of the other coowner; and upon payment to either coowner the other person shall cease to have any interest in the bond."

Section 315.46(a): "The bond will be paid to the registered owner during his lifetime upon his properly executed request as though no beneficiary had been named in the registration."

9. 31 Code Fed. Regs. § 315.45(c) (Supp. 1945). "If either coowner dies without the bond having been presented and surrendered for payment or authorized reissue, the surviving coowner will be recognized as the sole and absolute owner of the bond and payment or reissue, as though the bond were registered in his name alone, will be made only to such survivor."

Section 315.46(c): "If the registered owner dies without having presented and surrendered the bond for payment or authorized reissue and is survived by the beneficiary, upon proof of such death and survivorship, the

Where a private obligation is made payable to a beneficiary upon the death of a primary obligee, a deepseated conflict finds some courts ruling that the so-called beneficiary acquires an enforceable interest[10] and other courts holding that the obligation becomes part of the estate of the obligee because there is no valid gift, declaration of trust, or testamentary disposition.[11] Two conflicting theories have likewise arisen as to whether the provisions of the Treasury regulation for payment or reissue of Series E bonds to a coowner or beneficiary are modified by state law pertaining to wills and descent and distribution.

One view, represented by *Decker v. Fowler*,[12] is that the decedent's estate is entitled to the proceeds of the savings bond rather than the named beneficiary upon the theory that the rights of such beneficiary turned upon the question of whether there had been a valid execution of a gift inter vivos or causa mortis. The court in the *Decker* case justified the application of state transfer law by a narrow construction of the Treasury regulation, reasoning that the regulations were designed for the convenience of the government in making payments and not as a final determination of the rights of the parties to the proceeds.[13] Support for the *Decker v. Fowler* interpretation is sought from the apparent analogy to state banking laws authorizing payment of a joint deposit by banks to the survivor, which laws are intended for the protection of the banks and do not purport to determine the right to the money in the deposit.[14] This analogy, however, is only an apparent one. The

beneficiary will be recognized as the sole and absolute owner of the bond, and payment or reissue, as though the bond were registered in his name alone, will be made only to such survivor."

10. Krell v. Codman, (1891) 154 Mass. 454, 28 N. E. 578, 14 L. R. A. 860 and note; Kansas City Life Ins. Co. v. Rainey, (1944) 353 Mo. 477, 182 S. W. 2d 624, 155 A. L. R. 168 and note.

11. Clark v. Young, (1944) 246 Ala. 529, 21 So. 2d 331; McCarthy v. Pieret, (1939) 281 N. Y. 407, 24 N. E. 2d 102, rehearing denied, (1940) 282 N. Y. 800, 27 N. E. 2d 207, 24 Minn. L. Rev. 1009.

12. (1939) 199 Wash. 549, 92 P. 2d 254, 131 A. L. R. 961 and note; accord, Sinift v. Sinift, (1940) 229 Iowa 56, 293 N. W. 841; cf. Deyo v. Adams, (1942) 178 Misc. 859, 36 N. Y. S. 2d 734, (1944) 182 Misc. 459, 48 N. Y. S. 2d 459, (1943) 27 Minn. L. Rev. 401.

13. This interpretation was necessary to distinguish Warren v. United States, (1929) 68 Ct. Cl. 634, cert. denied, (1930) 281 U. S. 739, where, in an action brought to compel the Secretary of the Treasury to pay the proceeds of certain Treasury savings certificates to the executrix of the decedent's estate, it was held that payment could be made only to the beneficiaries.

14. See Sinift v. Sinift, (1940) 229 Iowa 56, 88, 293 N. W. 841: "The purpose of the Secretary and the remedy sought were the same as induced the enactment of such legislation as Code section 9267 [joint deposits]. It permits the Treasury department to pay strictly, in accordance with the terms of the bond, and avoids the inconvenience, delay and burden of ascertaining the rights of the parties respecting title or ownership as between themselves, or anyone else."

purpose of such state banking law provisions is solely to protect the banks.[15] The savings bond regulations, on the other hand, were not enacted primarily for the government's protection, but rather must be construed in the light of their purpose as part of a comprehensive social scheme, i.e., inducement of bond purchases by the small investor through the privileges of registration.[16] Where the government has appeared as amicus curiae, it has asserted that by the import of these words, "sole and absolute owner," the bonds were enforceable only in accordance with their tenor.[17] To avoid the undesirable results incurred by invoking the local laws of transfer, three states, Washington,[18] New York,[19] and California,[20] subsequently enacted declaratory legislation making the provisions of the Treasury regulations determinative of the rights of the beneficiary and coowner.

The rule generally adopted by decisions since 1943,[21] and made

15. Marshall & Ilsley Bank v. Voigt, (1934) 214 Wis. 27, 252 N. W. 355; New Hampshire Sav. Bank v. McMullin, (1936) 88 N. H. 123, 185 Atl. 158.

16. See Note, (1943) 52 Yale L. J. 917, 918. See dissenting opinion, Decker v. Fowler, (1939) 199 Wash. 549, 558, 92 P. 2d 254, 131 A. L. R. 961 and note, contending that a heretofore attractive form of government security now ". . . will prove but a snare to those who rely upon it.", and Matter of Deyo, (1943) 180 Misc. 32, 40, 42 N. Y. S. 2d 379, pointing out that the attempted construction of the regulations as being only for the protection of the government accomplished a result never contemplated by the Treasury Department nor by the millions of bond purchasers.

17. See Harvey v. Rackliffe, (1945) 141 Me. 169, 41 A. 2d 455, 161 A. L. R. 296, 298. Argument of counsel appears only in the American Law Reports.

18. Wash. Laws 1943, c. 14.

19. Pers. Prop. Law § 24. "Where any United States savings bond is payable to a designated person, whether as owner, co-owner, or beneficiary, and such bond is not transferable, the right of such person to receive payment of such bond according to its terms, and the ownership of the money so received, shall not be defeated or impaired by any statute or rule of law governing transfer of property by will or gift or an intestacy, provided, however, that nothing herein shall limit article ten of the debtor and creditor law or section one hundred twenty-four of the decedent estate law."

It will be observed, however, that the New York statute does not admit the supremacy of the Treasury regulations, and the hedging last clause thereof may conflict with the restricted creditors' rights of §§ 315.11-315.15, discussed infra. Under the New York statutes a beneficiary or coowner who has not given consideration is denied any interest as against a creditor, trustee in bankruptcy, or receiver of an insolvent estate.

20. Cal. Laws 1943, c. 51.

21. The first case to uphold the right of the coowner or beneficiary according to the terms of the bond was Meyer v. Mercier, (1938) 102 Colo. 422, 80 P. 2d 332. United States v. Dauphin Deposit Trust Co., (M.D. Pa. 1943) 50 F. Supp. 73, the only savings bond case involving ownership to come before the federal courts, has served as an impetus for subsequent cases, e.g., Conrad v. Conrad, (1944) 66 Cal. App. 2d 280, 152 P. 2d 221; Edds v. Mitchell, (1945) 143 Tex. 307, 184 S. W. 2d 823. See McLellan, The Ownership, Taxation and Transfer of United States Savings Bonds, 1946 Annual Meeting State Bar Association of North Dakota 39, 42.

statutory in some jurisdictions,[22] is that the beneficiary does acquire an interest under such bonds and is entitled to them upon the death of the owner. Although these decisions rest on both contract and constitutional grounds, they have a rational basis in the law of contracts aside from the controlling constitutional grounds. The rationale is that upon creation of the obligation (issuance of a bond) there is immediately created in the named parties certain rights in accordance with the tenor of the bonds and of applicable regulations, i.e., there is a contract entered into between the United States Government and the registered owner providing that the government will recognize the beneficiary's interest upon the occurrence of the owner's death.[23] Inasmuch as there is capacity in the parties to enter into this type of contract, resort need not be had to property law to determine the rights of the parties, and testamentary problems regarding transfers are eliminated. Unfortunately, the reasoning frequently seized upon to support the contract theory[24]—that the beneficiary of a bond acquires a vested interest from the moment of issuance (with merely the right to enjoyment postponed until the death of the owner) because the owner cannot cut off the beneficiary's interest without his consent if the owner desires to retain rather than cash the bond[25]—confuses property law with contract law. Resort to such reasoning is unnecessary. Under the principles of contract law, if the owner were entitled to a reissue upon his separate request to eliminate the named coowner or beneficiary, the beneficiary should still be entitled to the bonds on the death of the owner in the event there has been no such reissue. Indeed the writer suggests that the regulations be amended to allow such reissue, for under the present law[26] redemption before maturity results in a loss of increment in value due to the accelerating rate of yield. In any event the denomination of the interest of an owner or coowner in possession simply as a primary interest and that of a beneficiary or coowner not in possession as a secondary interest would be an aid to clarity in the avoidance of confusing property terms. Commentators[27] find

22. See supra notes 18, 19, and 20.

23. See 2 Williston, Contracts (rev. ed. 1936) 1139; (1943) 27 Minn. L. Rev. 401.

24. See Matter of Staheli, (1945) 57 N. Y. S. 2d 185, aff'd, (1946) 66 N. Y. S. 2d 271; Matter of Deyo, (1943) 180 Misc. 32, 42 N. Y. S. 2d 379.

25. See 31 Code Fed. Regs. §§ 315.45(b), 315.46(b) (Supp. 1945).

26. See table of redemption values and investment yields, 31 Code Fed. Regs. § 316.11 (Supp. 1943).

27. Gammon, War Savings Bonds and State Succession Laws, (1943) 17 Tenn. L. Rev. 928, 931; Note, (1943) 4 Mont. L. Rev. 70, 74; (1943) 56 Harv. L. Rev. 1007.

the situation of such a beneficiary analogous to that of the named beneficiary of a life insurance policy wherein the insured reserves the privilege of changing the beneficiary. However, the decisive factors (recognized in the more recent savings bond decisions) which compel the acceptance of the contract theory, i.e., that the borrowing power of the federal government necessarily includes the power to fix the terms of its obligations[28] and that the federal law overrides any state law to the contrary,[29] are not applicable to forms of private obligations.

The courts are agreed that the Treasury regulations governing issuance and redemption of savings bonds are within the scope of granted authority and have the effect of federal law.[30] No state law can vary the terms of federal obligations nor detract from their full enforceability.[31] If, however, the interpretation of savings bond contracts were to be controlled by state decisions applying general law, *Warren v. United States*[32] would lose its force for it might be distinguished, restricted, or nullified in forty-eight different manners.[33]

Where Congress has left interstices to be filled by judicial determination, the extent and nature of the legal consequences of a federal statute must be derived from the federal policy behind such statute; conflicting local law and policy must yield.[34] Similar considerations prevail where, as here, gaps remain in regulations enacted pursuant to an enabling statute. *Erie R. R. v. Tompkins*[35] is to be distinguished. The motivation for the *Erie* decision lay in the desire and need for uniformity within each of the forty-eight jurisdictions concerning matters in which local law and policy were the primary considerations. But it is nationwide, not merely statewide, uniformity which is not only desirable but also imperative to the success of the Series E bond program. In other fields the

28. United States v. Dauphin Deposit Trust Co., (M.D. Pa. 1943) 50 F. Supp. 73; Franklin Washington Trust Co. v. Beltram, (1943) 133 N. J. Eq. 11, 29 A. 2d 854; Davies v. Beach, (Cal. App. 1946) 168 P. 2d 452; Meyer v. Mercier, (1938) 102 Colo. 422, 80 P. 2d 332.

29. See note 28 supra.

30. In re Estate of Murray, (1945) 236 Iowa 807, 20 N. W. 2d 49; Succession of Tanner, (La. App. 1946) 24 So. 2d 642; Franklin Washington Trust Co. v. Beltram, (1943) 133 N. J. Eq. 11, 29 A. 2d 854.

31. See McCulloch v. Maryland, (U.S. 1819) 4 Wheat. 316, 436; United States v. Dauphin Deposit Trust Co., (M.D. Pa. 1943) 50 F. Supp. 73, 77.

32. (1929) 68 Ct. Cl. 634, cert. denied, (1930) 281 U. S. 739. See supra note 13.

33. See supra note 13 and text.

34. See Sola Electric Co. v. Jefferson Co., (1942) 317 U. S. 173, 176; Deitrick v. Greaney, (1940) 309 U. S. 190, 200-201.

35. (1938) 304 U. S. 64, 114 A. L. R. 1487 and note.

Supreme Court has already developed a doctrine limiting the scope of the *Erie* case by applying "federal common law" to fill these areas where the sweep of the statute compels its implementation in all its aspects by a broad federal policy, whether action is brought in a state or a federal court.[36] That savings bonds in all their consequences involve purely federal questions has been recognized in *United States v. Dauphin Deposit Trust Co.,*[37] the only savings bond case dealing with the problem of ownership yet to come before the federal courts.

II. Transferability and Creditors' Rights

The two paramount objectives of the Treasury's uninterrupted drive to sell Series E bonds are, as has been stated above,[38] (1) restriction of inflation within reasonable bounds and (2) promotion of a widespread ownership of the public debt with the incidental positive result that all manner of people will realize they are part of their national government and will consequently constitute a more fully-participating, alert citizenry. Series E bonds are attractive because of the high rate of yield,[39] not elsewhere obtainable without the addition of a risk factor, and because of the simplicity of registration; they will lose none of this attractiveness if the uniformity of decision sought by the Treasury is secured, as discussed in the preceding section. But the Treasury's objectives cannot be adequately served if the money value represented by the bonds can, without redemption, be made readily available to the credit structure of the nation.[40] Restrictions have therefore been placed on

36. See D'Oench, Duhme & Co. v. F. D. I. C., (1942) 315 U. S. 447, 26 Minn. L. Rev. 899; Garrett v. Moore-McCormack Co., (1942) 317 U. S. 289; Note, (1946) 59 Harv. L. Rev. 966. Although ownership cases decided since 1943 are generally in accord with the broad federal policy behind the savings bond regulations, numerous cases involving transferability are seemingly in conflict with the policy. See infra Section II. TRANSFERABILITY AND CREDITORS' RIGHTS.

37. See (M.D. Pa. 1943) 50 F. Supp. 73, 77: "Application to the issue and sale of these securities of state law would lead to a great diversity of rules regulating title and redemption and would subject the entire financing plan of the Federal Government to exceptional uncertainty by making identical transactions subject to the vagaries of the several states. This constitutes another example in the constantly increasing list of cases where application of the doctrine of Erie R. v. Tompkins, supra, will lead to more confusion in the Federal law."

38. See supra note 2 and text.

39. The investment yield on Series E bonds, if held to maturity, is about 2.9% per annum, compounded semi-annually. 31 Code Fed. Regs., § 316.2(b) (Supp. 1943). Comparable rates on Series F and G, the government bonds having the next most attractive yield, are respectively 2.53% and 2.5%. 31 Code Fed. Regs. § 318.2(c)(d) (Supp. 1944).

40. See Moore's Adm'r v. Marshall, (1946) 302 Ky. 729, 196 S. W. 2d 369, 372; Matter of Owens, (1941) 177 Misc. 1006, 1008, 32 N. Y. S. 2d 747.

transferability of and creditors' rights in savings bonds. 31 Code Fed. Regs. § 315.11 (Supp. 1945) provides:

"Savings bonds are not transferable and are payable only to the owners named thereon, except in case of the disability or death of the owner, authorized reissue, or as otherwise specifically provided. . . . A savings bonds may not be hypothecated or pledged as collateral for a loan or used as security for the performance of an obligation, except as provided in Section 315.12."

The exception provided for in 31 Code Fed. Regs. § 315.12 (Supp. 1945) permits only a negligible transferability not calculated to affect adversely the avowed purpose of the savings bond program in that such bonds may be pledged only with the Secretary of the Treasury. Here again, unfortunately, numerous courts are reducing the effectiveness of the program by finding in Section 315.11 a transferability clearly not contemplated. In *Marshall v. Felker*[41] it was held that Series E bonds may, notwithstanding the fact that they are marked "not transferable," be the subject of a valid gift inter vivos so long as the federal statutes, rules, and regulations under which they are issued contain no express prohibition against a transfer by gift. A gift causa mortis was sustained in *Matter of Borchardt*[42] with the explanation that there was nothing contained in the regulations which expressed or implied a prohibition against gifts causa mortis of savings bonds and that the common law was therefore controlling.[43] The only exception, other than that in Section 315.12, by which Series E bonds in the hands of the public may be made transferable is provided for in 31 Code Fed. Regs. § 315.13 (Supp. 1945):

"Judicial Proceedings (Judgment Creditors, Trustees in Bankruptcy, Receivers of Insolvents' Estates and Conflicting Claimants).—A claim against an owner or coowner of a savings bond and conflicting claims as to ownership of or interest in such bond as between coowners or the registered owner and a designated beneficiary, will be recognized when established by valid judicial

41. (1945) 156 Fla. 476, 23 So. 2d 555, 161 A. L. R. 167 and note. To the same effect, Hausfelder v. Security-First Nat. Bank, (Cal. App. 1946) 176 P. 2d 84.

42. (1942) 179 Misc. 456, 38 N. Y. S. 2d 987. To the same effect, Dietzen v. Am. Trust & Bkg. Co., (1939) 175 Tenn. 49, 131 S. W. 2d 69. In upholding a gift causa mortis of postal savings certificates an Illinois court has taken the extreme position that the legal meaning of "not transferable" was the same as that of "not negotiable." Blair v. Kirchner, (1943) 319 Ill. App. 348.

43. The persuasiveness of such holdings as this is illustrated by Marshall v. Felker, (1945) 156 Fla. 476, 478, 23 So. 2d 555, 161 A. L. R. 167 and note, wherein the executor conceded a transferability causa mortis, merely resisting the gift as inter vivos.

proceedings and payment or reissue will be made, upon presentation and surrender of the bond, except as follows:

(a) No such proceedings will be recognized if they would give effect to an attempted voluntary transfer inter vivos of the bond or would defeat or impair the rights of survivorship conferred by these regulations upon a surviving coowner or beneficiary.

(b) A judgment creditor, a trustee in bankruptcy or a receiver of an insolvent's estate will have the right to payment (but not to reissue)....

(c) If a debtor, or bankrupt, or insolvent, is not the sole owner of the bond, payment will be made only to the extent of his interest therein, which must be determined by the court or otherwise validly established. . . ."

Section 315.13 (a) clearly contains a prohibition of gifts inter vivos in that it permits only involuntary transfers inter vivos in favor of creditors.[44] The black-letter heading would seem to restrict the judicial proceedings provided for to creditors or their representatives and to conflicting claimants. A "conflicting claimant" is limited to a named registeree in the bond. In any event, the Florida court in *Marshall v. Felker* makes clear that only an empty right is created by decisions allowing transfers by gift by pointing out that it is only the right of the donee against the donor's estate that is being passed upon and that the donee may yet experience frustration in the attempt to procure the proceeds of the bonds from the government when they are presented for payment.[45]

In *Cook v. Marks*,[46] where the coowner and the defendants schemed to evade the prohibition of Section 315.11 and made the bonds security for a loan to the coowner, the court held the transaction void as against public policy but applied the clean hands doctrine and dismissed the owner's suit for return of the bonds. The practical result of this decision was to leave possession of the bonds in the hands of the creditor. This is in clear contravention of the regulations and serves to create confusion, for such possession gives the creditor no right to cash the bonds.

The public policy served by the retention of Series E bonds by the original registered owners is recognized by the recent case of

44. Id. at 479, simply states, however, that this provision is not to be construed as making unlawful such transfer, as between a donor and donee.

45. Ibid. Thus, the resultant futility and confusion of these holdings is the same as that involved in Decker v. Fowler, (1939) 199 Wash. 549, 92 P. 2d 254, 131 A. L. R. 961 and note, purporting to deprive registered coowners and beneficiaries of any ownership interest.

46. (1942) 302 Mich. 55, 4 N. W. 2d 465, 140 A. L. R. 1429 and note.

Moore's Adm'r v. Marshall[47] in which the court set aside a gift inter vivos. The court pointed out that a contrary holding ". . . would open the door for evasion of plainly expressed restrictions on transfer."[48] A similar recognition of the purpose of savings bonds prompted a New York court in *Matter of Owens*[49] to rule out an attempted inter vivos gift of savings bonds and to indicate that a gift causa mortis would also be prohibited. The first decision to hold squarely against gifts causa mortis of Series E bonds is the recent case of *Fidelity Union Trust Co. v. Tezyk.*[50] The character of Series E bonds as thrift securities, negating any suggestion of voluntary transferability, is further made out by provisions for an accelerating annual yield[51] and for payment of such increment in value only upon redemption.[52]

The intent of the Treasury Department to impose restrictions on creditors' rights is apparent, but the extent of the limitation, as expressed in the regulations,[53] is spelled out with something less than clarity.

No difficulties are encountered insofar as Series E bonds registered in only one name are concerned. Personal property in general is subject to attachment and supplementary proceedings,[54] and in the absence of a provision exempting savings bonds registered in one name, such bonds are similarly subject to these proceedings.

47. (1946) 302 Ky. 729, 196 S. W. 2d 369, 372. To the same effect, Bunch v. Hulsey, (1946) 302 Ky. 763, 196 S. W. 2d 373, 375. In neither case was the Kentucky court called upon to decide the invalidity of a gift causa mortis, but the expression of purpose in the first case makes clear that such gift would also fail.

48. Moore's Adm'r v. Marshall, (1946) 302 Ky. 729, 196 S. W. 2d 369, 372. The court also recognized that the reference to gift taxes in the regulations, now Treas. Dept. Cir. No. 653, 2d Revision (1943), II(4), 31 Code Fed. Regs. § 316.2(d) (Supp. 1943), was merely a provision for the situation where the purchaser of a bond has it registered in the name of another person rather than an implication of transferability.

49. (1941) 177 Misc. 1006, 32 N. Y. S. 2d 747; accord, In re Tonkin's Estate, (1946) 65 N. Y. S. 2d 484. Similar considerations compelled the surrogate court to rule that veterans' adjusted service bonds could not be the subject of a valid gift causa mortis. Matter of Ballard, (1937) 161 Misc. 785, 293 N. Y. Supp. 31.

50. (N.J., Ct. Err. & App. 1947) 55 A. 2d 26. The court emphasized that the purport of the regulations indicates a clear intention that Series E bonds shall not be transferable except by the prescribed processes of registration and concluded that ". . . it cannot reasonably be assumed that these conditions . . . were intended to be subject to rules pertaining to the devolution of personal property in the various states, or to varying interpretations which might be accorded by the different state courts." See text to notes 34-37 supra.

51. 31 Code Fed. Regs. § 316.11 (Supp. 1943).

52. 31 Code Fed. Regs. § 315.20 (Supp. 1945).

53. 31 Code Fed. Regs. §§ 315.11-315.15 (Supp. 1945).

54. Glenn, Liquidation (1935) 465; Glenn, The Rights and Remedies of Creditors (1915) 22-23.

The United States, however, may not be made a party to such proceedings, nor will attachment or garnishment process or similar types of enforcement proceedings lie against it.[55] Before a creditor may obtain payment of the bonds, he must have established his claim by a judgment.[56] The government affords the creditor no assistance in supplementary proceedings in that the regulations nowhere provide a method by which the creditor may ascertain if any bonds have been issued to the debtor and, if so, whether or not they have been redeemed. A judgment creditor has the right to payment but not to reissue.[57] The owner may have reissue in authorized denominations in the amount of the excess after the judgment is paid,[58] and such remainder will bear the original issue date.[59]

The determination of the exemption status of coowner and owner-beneficiary type bonds is a more difficult matter. If an exemption is conferred at all, it is conferred by Section 315.13 of the regulations, quoted supra, and the draftsmanship of this section leaves one in doubt. Section 315.13 (a) provides that no judicial proceedings will be recognized if they would defeat or impair the rights of survivorship *conferred by the regulations*. Section 315.13 (c) states that the creditor is entitled to payment to the extent of the interest of the debtor, bankrupt, or insolvent.

The first uncertainty which arises is whether Subsections 315.13 (a) and 315.13 (c) were intended to qualify each other. It may be that the last clause of Section 315.13 (a) represents a precaution against possible judicial sanction of sub rosa transactions evading restrictions on transferability. But if the two subsections do operate on each other, then it is necessary to determine precisely what rights of survivorship are conferred by the regulations as against creditors. Section 315.46 (c) provides that payment will be made to a surviving beneficiary "If the registered owner dies without having presented and surrendered the bond" for payment or reissue.

Section 315.45 (c) provides that payment will be made to a surviving coowner "If [the other] coowner dies without the bond having been presented and surrendered" for payment or reissue. Is any significance to be attributed to the difference in wording, be it intentional or not? The immediately preceding revision of the

55. Buchanan v. Alexander, (U.S. 1846) 4 How. 20; Brooks Hardware Co. v. Greer, (1911) 111 Me. 78, 87 Atl. 889.

56. 31 Code Fed. Regs. §§ 315.14, 315.15 (Supp. 1945).

57. 31 Code Fed. Regs. § 315.13(b) (Supp. 1945).

58. This is deducible from 31 Code Fed. Regs. §§ 315.13 and 315.30 (Supp. 1945).

59. 31 Code Fed. Regs. § 315.36 (Supp. 1945).

regulations used the words, "without having presented and surrendered the bond," in both instances.[60] Because the language of the present revision would seem to require that the *owner* himself have presented and surrendered the bond for payment in order to defeat the rights of survivorship of the beneficiary, greater rights of survivorship seem to have been created in a beneficiary than in a coowner unless the reference to presentation and surrender can be said to include involuntary action in both cases. The sections on presentation and surrender[61] do not seem to provide any clue. In view of this uncertainty, it cannot be said that the regulations definitely determine the extent of the exemption, if any, which has been conferred on these types of bonds.

The creditor has thus far prevailed over the coowner or beneficiary in all cases in which the owner-debtor was involved in bankruptcy or supplementary proceedings, but although the issue has been raised in most instances, the courts have shied away from a discussion of Section 315.13. *Saper v. Sussman*[62] held a bond in the possession of the beneficiary under a purported gift to be subject to replevy by the owner's trustee in bankruptcy, the court writing only a memorandum opinion. In *In re Wyche*[63] and *Morris Plan Industrial Bank v. Finn,*[64] both of which were cases involving the discharge of a bankrupt, the federal courts have assumed without deciding that such bonds, at least those in the possession of the bankrupt owner, were assets of the bankrupt estate. In the *Wyche* case the court stated that the bankrupt could not, for the purpose of denying discharge, be charged with bad faith in concluding that the bonds were exempt inasmuch as neither court nor counsel were able to cite authority for seizing and selling them.[65] The *Finn* case, however, suggests that a coowner in possession who has not contributed to the purchase price may have a right which cannot be defeated by the owner's creditor.[66] The most recent case, *In re Bartlett,*[67] offers little assistance, for the New York federal district court therein apparently relies on

60. See 31 Code Fed. Regs. §§ 315.36, 315.32(b) (Cum. Supp.); see also 31 Code Fed. Regs. §§ 315.32(c) (1944 Supp.).
61. 31 Code Fed. Regs. §§ 315.24, 315.28 (Supp. 1945).
62. (1945) 185 Misc. 277, 56 N. Y. S. 2d 377.
63. (W.D. La. 1943) 51 F. Supp. 825.
64. (C.C.A. 2d 1945) 149 F. 2d 591.
65. In re Wyche, (W.D. La. 1943) 51 F. Supp. 825, 828.
66. Morris Plan Industrial Bank v. Finn, (C.C.A. 2d 1945) 149 F. 2d 591,592: "[The referee] also found that the wife 'could have refused to convert the bonds into cash or allow the bankrupt control or custody of them,' which was perhaps literally true;".
67. (N.D. N.Y. 1947) 71 F. Supp. 514.

the memorandum decision of *Saper v. Sussman*[68] and concludes that the bonds were assets which could be reached by the trustee in bankruptcy because the beneficiary had no enforceable interest until the contingency of the purchaser's death had occurred. The court sought support for its conclusion by reference, not to Section 315.13, but rather to Section 315.11, supra, and Section 315.46 (a)[69] which provides that payment would be made only to the registered owner during his lifetime as if no beneficiary had been named.

Only one decision, *Iowa Methodist Hospital v. Long,*[70] has been found involving a supplementary proceeding in favor of a creditor. The Iowa court seems to decide that the bonds were wholly subject to the judgment creditor's claim on the basis of the intent of the named registrees.[71] In that case the owner-purchaser by his own testimony in court asserted full ownership in himself, thereby denying an intention to create a right in the coowner; the coowner neither testified contrarily nor asserted a claim of ownership. It would seem, however, that the introduction of the subjective element to determine rights in the bonds is neither desirable nor permissible. The inquiry should rather have been directed to whether the rights of the coowner as against the creditor were dependent on the fact of consideration contributed by her, or on the fact of registration as coowner considered apart from her contribution of purchase money.

The most compelling argument for upholding these decisions in favor of the creditor is the very uncertainty of the meaning of Section 315.13. Inasmuch as some fifty billion dollars worth of securities is involved and because of the absence of clear and uncontradictory language, one can easily understand the hesitation of the courts to rule that an exemption has been granted.

Other cases involving creditors have properly held that the interest of the surviving beneficiary of a bond could not be subordinated to the rights of creditors of a deceased owner-purchaser's estate.[72]

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68. (1945) 185 Misc. 277, 56 N. Y. S. 2d 377. It may be noted that the *Sussman* case was decided under the New York statute on savings bonds, supra note 19, which may be invalid to the extent that it seeks to preserve creditors' rights which would be applicable in the absence of the savings bond regulations.

69. See supra note 8.

70. (1944) 234 Iowa 843, 12 N. W. 2d 171, 150 A. L. R. 440 and note.

71. Id. at 849-850.

72. In re Briley Estate, (1945) 155 Fla. 798, 21 So. 2d 595; Matter of Hager, (1943) 181 Misc. 431, 45 N. Y. S. 2d 468. In the latter case the bonds were recovered from the administratrix who had possession, claiming they had been delivered to her in her personal capacity in payment of a debt due her from the decedent.

The foregoing discussion makes this much certain—a revision of the regulations directed at a clarification of Section 315.13 and of the sections which purport to set out the extent of the rights of survivorship is, at the very least, desirable.[73]

III. Taxation

Interest on government obligations issued on or after March 1, 1941, was made taxable by Section 4 of the Public Debt Act of 1941.[74] The increment in value represented by the difference between the purchase price of Series E bonds and their redemption value is considered as interest for tax purposes, and this interest is subject to such income and profits taxes as may be imposed by the United States. The bonds are also subject to federal and state estate, inheritance, gift, and other excise taxes, but are specifically exempted from all other taxation.[75]

An informational bulletin issued by the Commissioner of Internal Revenue[76] advises that no federal gift tax is imposed if, e.g., A purchases savings bonds with his own funds and has them registered in the names of "A or B" and keeps them in his possession, or in "A, payable on death to B," for A may at any time redeem the bonds and retain the proceeds for his own benefit. But there is a taxable gift at the time of purchase if registration is in the name "B" or "B, payable on death to A," for it is now B who may redeem the bonds. If A purchases and registers bonds in the names of "A or B," there is no gift for federal gift tax purposes unless and until B redeems the bonds after A has relinquished possession to him. While the failure to levy a gift tax at the time possession passes between coowners is logically inconsistent in view of the

73. The problem of retroactive operation of the changed regulations would not arise if such a change were construed as enlarging the scope of the exemption (thereby reducing the rights of creditors), for no provision of the constitution prohibits Congress from impairing the obligation of contracts. See Mitchell v. Clark, (1884) 110 U. S. 633, 643; Louisville Bank v. Radford, (1935) 295 U. S. 555, 589. Nor would it involve the deprivation of property without due process of law in violation of the Fifth Amendment, for section 315.11 precludes the acquisition by the creditor of substantive rights in specific bonds in the absence of a judgment having been obtained under section 315.13. Cf. Louisville Bank v. Radford, supra. If the change were construed as restricting the scope of the exemption, problems under the due process clause of the Fifth Amendment might arise.

74. 55 Stat. 7, § 4 (1941) as amended, 56 Stat. 189, § 6 (1942), 31 U. S. C. § 742a (Supp. 1946); see 26 Code Fed. Regs. § 29.22(b)(4)-4 (Supp. 1945).

75. 31 Code Fed. Regs. § 316.2(d) (Supp. 1943); see 26 Code Fed. Regs. § 81.13 (Cum. Supp.).

76. Bur. of Int. Rev., Mimeographed letter 5202 (instructions to Bureau field offices), Cum. Bul. 1941-2, 241. Cf. Inheritance Tax Div. v. Chamberlin Est., (1944) 21 Wash. 2d 790, 153 P. 2d 305.

rights of a coowner in possession, the Commissioner's approach to the problem is sound as a matter of practical tax administration. The extent to which the transfer of Series E bonds is subject to state taxes depends upon applicable state law.

No new problem concerning income and estate taxes arises when the bond is registered in one name only. The coowner and beneficiary type bonds, however, do raise problems. Where the bonds are taken out in the names of "A or B" interest is taxed as income of the person who contributed the purchase price; where both A and B have contributed to the purchase price, interest is divided proportionately.[77]

Treasury regulations recognize surviving beneficiaries and co-owners as sole and absolute owners of savings bonds,[78] and the bonds are free from probate proceedings on a deceased owner's estate.[79] It does not follow, however, that the present redemption value of the bonds is exempt from estate and inheritance taxes, for the status of the bonds for probate proceedings and their status for tax purposes are separate considerations having no relation to one another.[80] The order in which the names are registered on co-owner type bonds is of no import. The first person named is called the *owner* and the second the *coowner* for administrative purposes which affect neither the legal rights of coowners nor tax questions.[81]

The sale of Series E bonds is primarily directed at people of average means. For these people taxation does not enter into the picture except as to income from interest. Present federal law provides a specific gift tax exemption of $30,000[82] and an exemption for the additional estate tax of $60,000.[83] State exemptions will, in

77. Bur. of Int. Rev., Income Tax Office Dec. 3301, Cum. Bul. 1939-2, 75.

78. 31 Code Fed. Regs. §§ 315.45(c), 315.46(c) (Supp. 1945).

79. Release, Bur. of the Public Debt, June 14, 1944, Taxable Status of United States Savings Bonds for the Purposes of the Federal Estate Tax and State Estate, Inheritance and Legacy Taxes.

80. See 26 Code Fed. Regs. § 81.17 (Supp. 1945); 26 Code Fed. Regs. § 81.22 (Supp. 1945); In re Prifer Estate, (Pa. Orph. 1945) 7 Monroe L. R. 19, 10 Sch. Reg. 170. But cf. Succession of Tanner, (La. App. 1946) 24 So. 2d 642, which held that bonds registered in the names of husband and wife as coowners and purchased with community funds were not subject to the state inheritance tax upon husband's death, failing to distinguish ownership and tax status. The Louisiana court employed an analogy to the proceeds of insurance policies, which by a well-settled rule in that state are not subject to estate taxes.

81. Release, Bur. of the Public Debt, June 14, 1944, Taxable Status of United States Savings Bonds for the Purposes of the Federal Estate Tax and State Estate, Inheritance and Legacy Taxes.

82. Int. Rev. Code § 1004(a)(1); see 26 Code Fed. Regs. § 86.12 (Cum. Supp.).

83. Int. Rev. Code § 935(c); see 26 Code Fed. Regs. § 81.48 (Cum. Supp.).

the bulk of the cases, similarly exceed the amount of gifts and estates of persons of average means.[84] It is only where large amounts are involved that gift and estate and inheritance taxes are paid. In this situation registration in the owner-beneficiary rather than the coowner form may be more desirable because of the difference in the burden of proof where the owner is predeceased by the other party having an interest. The law provides that the entire amount of the coowner type bond is prima facie part of a decedent's gross estate;[85] thus, if the owner survives, the taxpayer has the burden of proving consideration contributed by the owner. It would seem that no such burden rests with the taxpayer where the beneficiary predeceases the owner of an owner-beneficiary type bond inasmuch as the tax regulations do not affirmatively provide for this situation. The fact that a gift tax has been paid does not eliminate liability for estate and inheritance taxes, merely being allowable as a credit against those taxes.[86]

Conclusions

Although the problem of ownership has not been authoritatively settled, ownership disputes have been resolved in accord with the purposes of the savings bond program of the Treasury Department since 1943. Taxation of savings bonds poses no particular difficulties. Effectuation of the fiscal and social policy behind the sale to the public of savings bonds continues to be hindered, however, by transferability and creditors' rights problems. The foregoing survey leads to the conclusion that these final barriers can be removed by (1) uniform decisions restricting transferability in accord with the plain meaning and purpose of Section 315.11 and (2) a revision of the regulations directed toward a clarification of Section 315.13.

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84. E.g., Minnesota allows gift and inheritance tax exemptions of $10,000 each if the donee is a wife or minor child, $5,000 each if the donee is a husband or adult child, etc. 1 Minn. Stat. 1945, §§ 292.05, 291.05.

85. 26 Code Fed. Regs. § 81.22 (Supp. 1945).

86. Int. Rev. Code § 813(a); 26 Code Fed. Regs. § 81.8 (Cum. Supp.).