

2010

Sticky Copyrights: Discriminatory Tax Restraints on the Transfer of Intellectual Property

Bridget J. Crawford

Mitchell M. Gans

Maurice A. Deane School of Law at Hofstra University

Follow this and additional works at: https://scholarlycommons.law.hofstra.edu/faculty_scholarship

Recommended Citation

Bridget J. Crawford and Mitchell M. Gans, *Sticky Copyrights: Discriminatory Tax Restraints on the Transfer of Intellectual Property*, 67 Wash. & Lee L. Rev. 25 (2010)
Available at: https://scholarlycommons.law.hofstra.edu/faculty_scholarship/93

This Article is brought to you for free and open access by Scholarly Commons at Hofstra Law. It has been accepted for inclusion in Hofstra Law Faculty Scholarship by an authorized administrator of Scholarly Commons at Hofstra Law. For more information, please contact lawcls@hofstra.edu.

Sticky Copyrights: Discriminatory Tax Restraints on the Transfer of Intellectual Property

Bridget J. Crawford*

Mitchell M. Gans**

Abstract

This Article focuses on the federal estate and gift tax treatment of copyright termination rights. The ability of a creative individual to terminate prior copyright transfers serves to protect against economic exploitation. Once a copyright's value has been established in the marketplace, the author (or the author's heirs) enjoys a "second look" at the gift, sale, license or other transfer of a copyright. But copyright termination rights—intended to enhance the economic well-being of authors and artists—undermine estate planning strategies available to owners of other types of property. There is no policy justification for such discrimination, and so this Article proposes legislative changes that would level the playing field for wealth transfer tax purposes.

Table of Contents

I. Introduction	26
II. Overview of Intellectual Property Termination Rights	29
III. Gift Taxation of Copyright Interests	34
A. The Hoarding Author: No Gift, No Tax	34
B. The Giving Author and the Repetitive Gift Syndrome	35

* Bridget J. Crawford is a Professor at Pace University School of Law.

** Mitchell M. Gans is the Steven A. Horowitz Distinguished Professor of Tax Law at Hofstra University School of Law and an Adjunct Professor at New York University School of Law.

For helpful conversations and comments, we thank Horace Anderson, Ann Bartow and Jonathan Blattmachr.

1. General Rules Applicable to Gifts.....	35
2. No Transfer, No Gift.....	37
3. Valuing Sticky Copyrights	39
4. Qualifying Sticky Copyrights for Beneficial Tax Treatment	41
a. The Annual Exclusion	41
b. The Marital Deduction	41
c. Consequences of Failing to Qualify for the Available Exclusions and Deductions	48
5. Planning with Sticky Copyrights.....	49
C. The Selling Author and the Derivative Gift Syndrome.....	50
IV. Estate Taxation of Copyright Interests.....	52
A. The Hoarding Author and the Estate Tax Marital Deduction	53
B. The Giving Author Stuck on Copyrights	55
1. If the Giving Author Dies Before Termination Window Opens.....	56
2. If the Giving Author Dies During Period of Termination.....	62
3. If the Giving Author Dies After Termination Window Closes.....	63
C. The Selling Author Confronts Estate Tax.....	65
1. If the Selling Author Dies Before Termination Window Opens.....	65
2. If the Selling Author Dies During Period of Termination.....	71
3. If the Selling Author Dies After Termination Window Closes.....	71
V. Policy Concerns with Sticky Copyrights	72
VI. Legislative Reform to Unstick Copyrights.....	74
VII. Conclusion.....	75

I. Introduction

Estate planning with copyrights presents special challenges. Copyrights are different—at least for estate planning purposes—from other property

interests in two notable ways. First, copyrights have a defined lifespan.¹ Second, the creator of the copyrightable work has an unwaivable statutory right of termination with respect to any grant of a transfer or license of a copyright made on or after January 1, 1978.² This termination right is exercisable only during a specified time period,³ and does not apply to derivative works⁴ or works made for hire.⁵ If the author dies before exercising her termination right but before the applicable time period expires, then certain of the author's heirs, as specified in the statute, may exercise the termination right.⁶ These termination rights make copyrights "sticky" for wealth transfer tax purposes. Consequently, copyrights are difficult to give away in a tax-effective matter.

Because of the highly specialized nature of their respective fields, copyright specialists tend to know little about estate planning and vice versa. Intellectual property literature explains the nature of termination rights, but it is virtually silent on tax planning for donative transfers of intellectual property.⁷ Conversely, estate planning literature occasionally discusses conflicts between the substantive law of copyrights,⁸ on the one hand, and donative transfers, on

1. See 17 U.S.C. § 302(a) (2006) ("Copyright in a work created on or after January 1, 1978, subsists from its creation and . . . endures for a term consisting of the life of the author and 70 years after the author's death.").

2. See *id.* § 203(a)(5) ("Termination of the grant may be effected notwithstanding any agreement to the contrary, including an agreement to make a will or to make any future grant."); H.R. REP. NO. 94-1476, at 124 (1976), *reprinted in* 1976 U.S.C.C.A.N. 5659, 5741 ("The provisions of section 203 are based on the premise that the reversionary provisions of the present section on copyright renewal (17 U.S.C. sec. 24) should be eliminated, and that the proposed law should substitute for them a provision safeguarding authors against unremunerative transfers."); see also BRUCE P. KELLER & JEFFREY P. CUNARD, *COPYRIGHT LAW: A PRACTITIONER'S GUIDE* § 7:5.2[A] (2005) (discussing the scope of transfers by authors of copyrights). Transfers or licenses prior to January 1, 1978, are beyond the scope of this discussion. In this Article, the term "author" refers to any author, artist, entertainer, performer or other person whose creative work gives rise to property subject to copyright protection.

3. See 17 U.S.C. § 203(a)(3) ("Termination of the grant may be effected at any time during a period of five years beginning at the end of thirty-five years from the date of execution of the grant . . .").

4. See *id.* § 203(b)(1) ("A derivative work prepared under authority of the grant before its termination may continue to be utilized under the terms of the grant after its termination, but this privilege does not extend to the preparation after the termination of other derivative works based upon the copyrighted work covered by the terminated grant.").

5. See *id.* § 203(a) ("In the case of any work other than a work made for hire . . .").

6. See *id.* § 203(a)(2) (dictating which of the author's heirs may exercise the termination interest).

7. See, e.g., KELLER & CUNARD, *supra* note 2; 3 MELVILLE B. NIMMER & DAVID NIMMER, *NIMMER ON COPYRIGHT* § 11 (1996).

8. See generally Cheryl E. Hader, *Making the Intangible Tangible: Planning for Intellectual Property*, 29 *EST. PLAN.* 574 (2002).

the other.⁹ Rarely does one find a thorough analysis of the wealth transfer tax consequences of copyright transfers and the particular tax concerns that arise with respect to copyright termination rights.¹⁰ This Article seeks to fill that void.

Part I provides an overview of an author's copyright termination rights. Part II explores gift tax considerations for three taxpayers: an author who hoards copyrights (or makes no transfers during lifetime), an author who gives copyrights (during lifetime or at death), and an author who sells an interest in a copyright. In the latter two cases, a gift tax may be imposed on the value of the termination rights that arise in an author's spouse and heirs. Part III considers the estate tax treatment of transfers by the same three taxpayers: the hoarder, the giver, and the seller of a copyright. The tax consequences depend in part on when an author dies in relation to the period for exercise of the termination right. Part IV attempts to reconcile the special property law treatment of copyrights with the wealth transfer tax consequences of hoarding, giving, or selling them. Contrary to federal copyright law's intended purpose of securing economic benefits for authors and their families, the law in fact disadvantages creative individuals. Termination rights cause creative individuals to be subject to more estate and gift taxation than similarly situated taxpayers who own noncopyright property. Copyrights are "sticky" insofar as they are difficult to transfer without attracting some wealth transfer tax liability—not just with respect to the copyright itself but also with respect to the termination rights that arise under federal copyright law in the author and the author's heirs. Part V proposes revisions to federal copyright law to eliminate the (seemingly unintended) negative estate and gift tax aspects of sticky intellectual property termination rights.

9. See, e.g., Bridget J. Crawford & John Sare, *Estate Planning for Authors and Artists*, 815-2d TAX MGMT. PORTFOLIOS A-1, A-31, A-36 (2004) (discussing some of the copyright transfer issues involved in estate planning); Ann Bartow, *Intellectual Property and Domestic Relations: Issues to Consider When There is an Artist, Author, Inventor, or Celebrity in the Family*, 35 FAM. L.Q. 383, 401-11 (2001) (explaining how a copyright author can terminate a license or transfer); Lee-ford Tritt, *Liberating Estates from the Constraints of Copyright*, 38 RUTGERS L.J. 109, 112 (2006) (discussing the problems the Copyright Act of 1976 created for authors attempting to transfer copyright rights at death).

10. The two minor exceptions appear to be Jeffrey K. Eisen & Allan E. Biblin, *Estate Planning for Clients in the Entertainment Business*, EST. PLAN., Feb. 2006, at 26, 29-32 (discussing estate tax consequences involving copyrights), and William M. Weintraub & Burton A. Mitchell, *Estate and Gift Tax Planning for Copyright Owners*, L.A. LAW., May 25, 2002, at 20, 20-27 (explaining the various tax issues involved with the transfer and termination of copyright rights).

As a general matter, taxpayers can make inter vivos gifts of their property and thereby "freeze out" of their estate all post-gift appreciation and income.¹¹ This advantage is forfeited, however, where the donor retains certain kinds of access to, or control over, the gifted asset.¹² In such a case, the date-of-death value of the asset is included in the donor's gross estate, thereby causing all post-gift appreciation to be subject to estate tax.¹³ Thus, well-advised taxpayers seeking to freeze the value of their estate through an inter vivos gift should make sure not to retain any prohibited access or control.¹⁴ In contrast, in the case of a copyright, this kind of planning does not work as effectively. Because of termination rights, the author—whether gifting or selling the copyright—may not be able to achieve the same kind of "freeze" that is enjoyed by taxpayers owning other kinds of property.¹⁵ From a copyright perspective, termination rights may protect the author from exploitation and, therefore, may be viewed as a salutary concept, but they produce discrimination on the tax front that cannot be justified.

II. Overview of Intellectual Property Termination Rights

Under the 1976 Copyright Act,¹⁶ a copyright typically lasts for the creator's lifetime plus seventy years in the case of a work (other than a work for hire) created on or after January 1, 1978.¹⁷ Until that expiration date, copyrights are as freely transferrable as other property interests,¹⁸ subject to one

11. See generally Mitchell M. Gans, *GRIT's, GRAT's and GRUT's: Planning and Policy*, 11 VA. TAX REV. 761, 763 (1992) (explaining how inter vivos gifts can be used to reduce transfer tax liability).

12. See *id.* at 878–911 (explaining the estate tax consequences of retaining an income interest for a term of years or life).

13. See Jonathan G. Blattmachr & Mitchell M. Gans, *Putting the Heat on Freezes*, 2 PROB. & PROP. 12, 13–14 (1988) ("Prior to OBRA, Section 2036(a) provided that pre-death transfers . . . were beyond the scope of estate tax inclusion under Section 2036 even if the transferor retained an income interest in . . . the property until death. But OBRA eliminates this bona fide transfer exception under the new rule . . .").

14. See *id.* (providing examples demonstrating the estate tax benefits of not retaining any access or control to an inter vivos gift).

15. *Infra* Part III.B–C.

16. Copyright Act of 1976, Pub. L. No. 94-553, 90 Stat. 2541 (codified as amended at 17 U.S.C. §§ 101–1332 (2006)).

17. 17 U.S.C. §302(a). The copyrights of the owner of a work for hire expire 120 years from the date of the work's creation or 95 years from the date of its first publication, whichever occurs first. *Id.* § 302(c). For purposes of this Article, all examples assume that the copyright relates to a work other than a work for hire and one created on or after January 1, 1978.

18. See *id.* § 201(d)(1) ("The ownership of a copyright may be transferred in whole or in

major caveat: "In the case of any work other than a work made for hire, the exclusive or nonexclusive grant of a transfer or license of copyright or of any right under a copyright, executed by the author on or after January 1, 1978, otherwise than by will, is subject to termination"¹⁹ The author may terminate a copyright if she is alive during the specified exercise period for giving notice and for termination of the interest.²⁰ If not, certain of the author's heirs specified by statute may exercise the termination right.²¹ Ordinarily, the heirs who may terminate an author's prior transfers are the author's surviving spouse (who owns a one-half interest in the termination right) and children (who, together with any children of a predeceased child of the author, own the remaining one-half interest in the termination right per stirpes).²² If grandchildren of the author become entitled to participate, they must exercise by majority vote the termination interest that otherwise would have passed to their parent, had their parent survived the author.²³ Termination requires the agreement of more than half of the beneficial owners of the termination right.²⁴

part by any means of conveyance or by operation of law, and may be bequeathed by will or pass as personal property by the applicable laws of intestate succession.").

19. *Id.* § 203(a). Some scholars have referred to this ability of the author or the author's heirs to disrupt prior transfers as "contract bumping." See, e.g., Francis M. Nevins, Jr., *The Magic Kingdom of Will-Bumping: Where Estates Law and Copyright Law Collide*, 35 J. COPYRIGHT SOC'Y 77, 77–114 (1988) (describing the history and process of bumping); Michael Rosenblum, *Give Me Liberty and Give Me Death: The Conflict Between Copyright Law and Estates Law*, 4 J. INTELL. PROP. L. 163, 166–67 (1997) ("In essence, if an author assigned his copyright during the first copyright term, the Statute of Anne mandated a return of the copyright interest to the author at the end of the term, thereby 'bumping' the assignment contract in favor of copyright law.").

20. See 17 U.S.C. § 203(a)(1) ("In the case of a grant executed by one author, termination of the grant may be effected by that author").

21. This discussion is limited to grants of a transfer or license of a copyright or of any right under a copyright executed by the author on or after January 1, 1978. *Id.* § 203(a). Specifically, if a spouse but no children or grandchildren survive the decedent, this termination right passes to the decedent's surviving spouse. *Id.* § 203(a)(2)(A). If the decedent is survived by a spouse and any children or grandchildren, the termination right passes one-half to the surviving spouse. *Id.* The other half passes to the decedent's children and grandchildren per stirpes. *Id.* § 203(a)(2)(B)–(C). The termination rights passing to the children of any predeceased child of the decedent may be exercised only by a majority of such predeceased child's surviving children. *Id.* § 203(a)(2)(C). If a decedent is not survived by a spouse, but is survived by any children or grandchildren, the termination right passes to such children and grandchildren, per stirpes. *Id.* § 203(a)(2)(B)–(C). If a spouse does not survive the decedent, children, or grandchildren, the termination right passes to the decedent's executor or administrator. *Id.* § 203(a)(2)(D).

22. *Supra* note 21 and accompanying text.

23. See 17 U.S.C. § 203(a)(2)(C) (2006) ("[T]he share of the children of a dead child in a termination interest can be exercised only by the action of a majority of them.").

24. See *id.* § 203(a)(1) ("In the case of a grant executed by one author, . . . if the author is

This means that if an author's widow or widower succeeds to a one-half interest in the termination right, at least one of the author's surviving children (or the children of any predeceased child, acting by majority) must join to effect the termination.

Whether held by the author or by the author's heirs, termination rights may be exercised only during a five-year time period.²⁵ The window for exercise "opens" thirty-five years after the author's grant of the copyright; if the initial grant also included the right of publication, the window opens at the earlier of thirty-five years after publication or forty years from the date of the grant.²⁶ The window then "closes" five years later.²⁷ Notice of termination, however, must be given at least two years in advance—and may be given up to ten years in advance—of the window's opening.²⁸ Practically speaking, this means that, at any time between twenty-five and thirty-eight years from the date of the initial grant, an author (or the author's heirs) may serve a notice of termination.²⁹ After the author or her heirs give notice, termination occurs automatically on the date during the five-year window that is specified in the notice.³⁰ If the author subsequently dies before the termination actually occurs, the copyright becomes part of the author's estate.³¹ So if an author gives notice in year twenty-five of her intent to terminate a copyright in year thirty-six, but dies in year twenty-nine, the copyright is delivered to her estate in year thirty-six.³²

dead, [the grant may be effected] by the person or persons who . . . own and are entitled to exercise a total of more than one-half of that author's termination interest.").

25. See *id.* § 203(a)(3) ("Termination of the grant may be effected at any time during a period of five years beginning at the end of thirty-five years from the date of execution of the grant . . .").

26. *Id.*

27. *Id.*

28. See *id.* § 203(a)(4)(A) ("[T]he notice shall be served not less than two or more than ten years before . . . [the] date [of termination].").

29. *Id.*

30. See *id.* § 203(b) ("Upon the effective date of termination, all rights under this title that were covered by the terminated grants revert to the author, authors, and other persons owning termination interests . . .").

31. See *Bourne Co. v. MPL Commc'ns, Inc.*, 675 F. Supp. 859, 862 (S.D.N.Y. 1987) ("Because [the author] died after the notice of termination was served, her rights under the terminated grant had vested and thus passed to her estate."), *modified*, 678 F. Supp. 70 (S.D.N.Y. 1988); see also Bobby Rosenblum, *A Very Welcome Return: Copyright Reversion and Termination of Copyright Assignments in the Music Industry*, 17 ENT. & SPORTS L. 3, 7 (1989) (stating that, where an author dies after notice of termination is given but before the termination window opens, the copyright vests in the author's estate, not in her statutory heirs).

32. See *Bourne Co.*, 675 F. Supp. at 862 (finding that a copyright vests when notice of termination is given).

The law of donative transfers generally reflects a commitment to the principle of testamentary freedom³³—the ability of a testator to dispose of property at death as she chooses as long as the transfer does not contradict public policy.³⁴ In that sense, copyright law is consistent with the law of wills and trusts. An author may make *testamentary* transfers of copyrights or interests in copyrights free from any claim by statutory heirs to terminate the transfer.³⁵ Heirs may challenge death-time dispositions of copyrights only through a standard will contest (or possibly a separate claim of tortious interference).³⁶

With respect to lifetime transfers, copyright law takes a position that is inconsistent with a commitment to free transfer, or even vigorous property ownership. An author and the author's heirs may revisit grants of copyrights or interests in copyrights once the intellectual property's value has been established in the marketplace.³⁷ Practically speaking, termination rights over lifetime transfers thus operate as a right of revocation in the author's hands, or a veto right in the heirs' hands. Termination trumps (or "bumps")³⁸ any and all prior agreements or promises.³⁹ The property then re-vests in the author, if

33. According to the Restatement (Third) of Property, the purpose of the law of donative transfers is to "facilitate rather than regulate." See RESTATEMENT (THIRD) OF PROP.: WILLS AND OTHER DONATIVE TRANSFERS § 10.1 cmt. c (2003) ("American law curtails freedom of disposition only to the extent that the donor attempts to make a disposition or achieve a purpose that is prohibited or restricted by an overriding rule of law.").

34. A bequest conditioned on a beneficiary's divorce from a current spouse is an example of a transfer that offends public policy. See RESTATEMENT (SECOND) OF PROP.: DONATIVE TRANSFERS § 7.1 (1983) ("An otherwise effective restriction in a donative transfer . . . designed to permit the acquisition or retention of . . . property by the transferee only in the event of a separation or divorce . . . is invalid, unless the dominant motive of the transferor is to provide support in the event of separation or divorce . . .").

35. Termination rights apply to transfers executed by the grantor "otherwise than by will." 17 U.S.C. § 203(a) (2006). Indeed, if an author dies owning a copyright, without ever having assigned an interest in it to anyone, the author is free to dispose of that copyright as he or she chooses. *Id.*

36. See JESSE DUKEMINIER ET AL., WILLS, TRUSTS & ESTATES 141–94, 199–235 (7th ed. 2005) (noting common grounds for a will contest, such as defects in the execution, lack of mental capacity, undue influence, fraud, and duress).

37. See JAY DRATLER, JR. & STEPHEN M. MCJOHN, INTELLECTUAL PROPERTY LAW: COMMERCIAL CREATIVE AND INDUSTRIAL PROPERTY § 6.04(A)[1] (2008) ("By allowing copyright grants and licenses to be terminated after a number of years, . . . the statute lets authors and their statutory successors recoup more of the commercial value of works whose true value emerges in time.").

38. See Nevins, *supra* note 19, at 77 (defining the term "bumps").

39. See 17 U.S.C. § 203(a)(5) ("Termination of the grant may be effected notwithstanding any agreement to the contrary . . ."). The notice must comply in content and form with rules promulgated by the Register of Copyrights and a copy of the termination notice must be

living, or if not, the author's heirs—even those who did not join in the termination—in proportion to their ownership of the termination rights.⁴⁰

The copyright law might appear to offer *more* protection for testamentary transfers than for inter vivos transfers, insofar as heirs have limited grounds to challenge an author's death-time transfers. Heirs have an almost unconstrained ability to terminate lifetime transfers.⁴¹ This discrepancy is especially odd given that the law demands less, in terms of mental capacity, from one who executes a will than from one who enters into a contract (or makes a gift) during lifetime.⁴² But in fact, both the law of wills and trusts and the law of copyright share the goal of minimizing the likelihood of an economically disastrous *lifetime* transfer. The law of donative transfers does this by requiring that a person be capable of understanding the economic consequences of her actions.⁴³ Copyright law accomplishes this by theorizing copyright interests as unsusceptible to accurate valuation until exploited, usually commercially.⁴⁴ Thus all lifetime transfers of copyright interests are worthy of suspicion, if not inherently unstable.⁴⁵

Termination rights are the copyright law's protection against transactions that are grossly unfair to the author.⁴⁶ In the parts that follow, we examine

recorded in the Copyright Office in order to take effect later. *Id.* § 203(a)(4)(A).

40. *See id.* § 203(b) ("Upon the effective date of termination, all rights under this title that were covered by the terminated grants revert to the author, authors, and other persons owning termination interests . . .").

41. *See* Tritt, *supra* note 9, at 173 ("If an author makes lifetime gifts of copyright interests and dies before the termination rights vest in the author, the statutory heirs may potentially bump these lifetime gifts.").

42. *See* RESTATEMENT (THIRD) OF PROP.: WILLS AND OTHER DONATIVE TRANSFERS § 8.1(c) (2003) (stating that, to make a lifetime gift, a transferor must have testamentary capacity "plus"—the capacity for "understanding the effect that the gift may have on the future financial security of the donor and of anyone who may be dependent on the donor"); *see also* Lee v. Lee, 337 So. 2d 713, 715 (Miss. 1976) (holding that the testator had mental ability to execute a valid will, but not to make a valid lifetime conveyance of real property).

43. *See* DUKEMINIER ET AL., *supra* note 36, at 145–46 (finding that to make a donative transfer, an individual must "meet all of the elements for making a will" and understand the financial consequences of the transfer).

44. *See generally* DRATLER & MCJOHN, *supra* note 37.

45. *See* Jane B. Baron, *Gifts, Bargains, and Form*, 64 IND. L.J. 155, 157 (1989) ("Despite the benevolent motives and family settings usually associated with gifts, the accepted justification for formality assumes that, in giving, people are fundamentally unreliable and deceitful.").

46. Copyright law does not permit the author or the author's heirs to relinquish, transfer, or trade their termination rights. *See* 17 U.S.C. § 203(a)(5) (2006) ("Termination of the grant may be effected notwithstanding any agreement to the contrary, including an agreement to make a will or to make any future grant."); *see also* H.R. REP. NO. 94-1476, 124 (1976) ("A provision of this sort is needed because of the unequal bargaining position of authors, resulting in part

three scenarios of interest from a gift tax perspective and then from an estate tax perspective. An author with a copyright created by her may retain the property, making no lifetime transfers; she may gratuitously give the property away; or she may sell or license the copyright. We call these authors hoarders, givers, and sellers, respectively. Each faces wealth transfer tax rules with different—and often unpredictable—results.

III. Gift Taxation of Copyright Interests

A. The Hoarding Author: No Gift, No Tax

From a gift tax perspective, the simplest scenario involves an author who makes no transfers of copyrights during her lifetime. Generally speaking, I.R.C. § 2501 imposes a tax on all property transferred by gift during a calendar year by any individual.⁴⁷ A gift is any disposition of property "for a consideration to the extent that the value of the property transferred by the donor exceeds the value in money or money's worth of the consideration given therefor."⁴⁸ Gifts of property having a value less than or equal to the annual exclusion amount (\$13,000 in 2009 and 2010) are not subject to taxation.⁴⁹ Each citizen or resident of the United States has a cumulative credit of \$1,000,000 against the gift tax.⁵⁰ So a "hoarding" author, one who makes no property transfers during lifetime, should owe no gift tax. But in the hands of an author who gives or sells an interest in a copyright, the copyright is "sticky" and potentially can result in transfer-tax complications.

from the impossibility of determining a work's value until it has been exploited.").

47. See I.R.C. § 2501(a)(1) (2006) ("A tax . . . is hereby imposed for each calendar year on the transfer of property by gift during such calendar year by any individual resident or nonresident."). A donative transfer by an author of a copyright with respect to which no other grants or licenses have been made is fairly straightforward from a gift and estate tax perspective. Tax is imposed on the fair market value of the property transferred. See generally *id.* § 2501 (imposing gift tax); *id.* § 2512(b) (declaring the method for valuing gifts); *id.* § 2001 (imposing estate tax); *id.* § 2031 (defining the gross estate).

48. Treas. Reg. § 25.2512-8 (1992).

49. See I.R.C. § 2503(b)(1) (explaining that gifts up to the statutory limit shall not be considered "taxable gifts"). For the inflation adjustment, see Rev. Proc. 2009-50, 2009-45 I.R.B. 617 ("For calendar year 2010, the first \$13,000 of gifts to any person (other than gifts of future interests in property) are not included in the total amount of taxable gifts under § 2503 made during that year.").

50. See I.R.C. § 2505(a)(1) (allowing the \$1,000,000 cumulative credit).

B. The Giving Author and the Repetitive Gift Syndrome

Any lifetime transfer of a copyright—whether gratuitous or not—gives rise to termination rights in the grantor and certain statutorily designated heirs.⁵¹

In the vocabulary of wills and trusts, these termination rights operate as time-delayed and time-limited rights of revocation held first by the author and then by the author's heirs.⁵² So a lifetime gift of a copyright, then, gives rise to three distinct interests: the transferee's interest in the copyright, the author's termination rights, and the heirs' (contingent) termination rights.⁵³

1. General Rules Applicable to Gifts

Consider first a scenario in which an author transfers a copyright without consideration to a third-party donee:

Hypothetical 1. *Author* is married and has two adult children. *Author* already applied his maximum unified credit to prior lifetime transfers. On January 1, 2009, each of *Author* and his wife made a \$13,000 annual exclusion cash gift to *Person B*, an unrelated third party. *Author* is the creator and owner of a copyright having a fair market value of \$20,000. On February 1, 2009, *Author* gives the copyright to *Person B* and receives no consideration in return.

The cash gifts of \$13,000 are protected by the annual exclusion and are not subject to gift tax.⁵⁴ But when *Author* subsequently gives the copyright to *Person B*, even if *Author* and his spouse agree to split the gift,⁵⁵ the transfer is

51. *Supra* notes 18–24 and accompanying text.

52. *See supra* Part II (discussing termination rights as having the effect of revocation rights).

53. *Supra* notes 18–24 and accompanying text.

54. *See* I.R.C. § 2503(b)(1) (2006) ("[I]n the case of gifts . . . the first \$10,000 of such gifts to such person shall not, for purposes of subsection (a), be included in the total amount of gifts made during such year.").

55. *See id.* § 2513(a)(1) ("A gift made by one spouse to any person other than his spouse shall . . . be considered as made one-half by him and one-half by his spouse."). Gift splitting requires the nondonor spouse to indicate his or her consent on the donor's timely filed gift tax return. *Id.* § 2513(a)(2) ("[I.R.C. § 2513(a)(1)] shall apply only if both spouses have signified . . . their consent."); *see also* Treas. Reg. § 25.2513-2(a)(1) (as amended in 1983) (explaining that consent to the application of I.R.C. § 2513 is sufficient if the consent of the husband is signified on the wife's return (and vice-versa), each spouse signifies consent on their own return, or both signify it on one of the returns). Only when each spouse is either a citizen or resident of the United States at the time of the transfer may spouses gift-split. I.R.C. § 2513(a)(1).

taxable.⁵⁶ *Author* has no remaining unified credit to "shelter" the subsequent gift, thus causing the gift to produce a gift tax liability.⁵⁷ What is the value of the transfer for gift tax purposes? At initial glance, *Author* appears to make a gift of a copyright worth \$20,000. On closer examination, the situation is more complex.

When *Author* gives *Person B* the copyright on February 1, 2009, federal copyright law creates in *Author*⁵⁸ and *Author's* heirs⁵⁹ a right to terminate the transfer to *Person B*. Prior to the gift from *Author* to *Person B*, these termination rights did not exist.⁶⁰ In the case of Hypothetical 1, the rights may be exercised beginning on February 1, 2044, until February 1, 2049.⁶¹ Exercise may be effectuated by delivering to *Person B*—at any time after February 1, 2034 (ten years before the commencement of the exercise period), but no later than February 1, 2042 (two years prior to the expiration of the exercise period)⁶²—written notice of the intent to exercise the termination right. Termination then would occur automatically at the time specified in the notice of exercise.⁶³ If *Author* were to die without exercising his termination rights but before they have expired, then his surviving widow and adult children would own—and they could exercise—the termination interest.⁶⁴

56. *Supra* note 47 and accompanying text.

57. *Supra* note 50 and accompanying text.

58. See 17 U.S.C. § 203(a)(1) (2006) (granting author right to terminate grant).

59. See *id.* § 203(a)(2) (granting author's heirs right to terminate grant).

60. See *id.* § 203(a) (delineating termination rights that come into existence upon nonexclusive grant of a transfer or license of a copyright).

61. See *id.* § 203(a)(3) ("Termination of the grant may be effected at any time during a period of five years beginning at the end of thirty-five years from the date of execution of the grant.").

62. See *id.* § 203(a)(4) ("The termination shall be effected by serving an advance notice in writing . . . upon the grantee [T]he notice shall be served not less than two or more than ten years before [the effective date of termination].").

63. See *Bourne Co. v. MPL Commc'ns Inc.*, 675 F. Supp. 859, 861 (S.D.N.Y. 1987) ("When a termination is effected, all rights covered by the terminated grant revert, on the effective date of termination, to the author or his statutory successor."); *modified*, 678 F. Supp. 70 (S.D.N.Y. 1988); see also *supra* notes 30–32 and accompanying text.

64. See 17 U.S.C. § 203(a)(2) (2006) ("Where an author is dead, his or her termination interest is owned, and may be exercised [by his or her statutory successors, as defined in § 203(a)(2)(A) through § 203(a)(2)(D)]."). Hypothetical 1 and the related examples are distinguishable from *Stewart v. Abend* in several ways. *Stewart v. Abend*, 495 U.S. 207, 221 (1990) ("[I]f the author dies before the renewal period, then the assignee [of the renewal rights] may continue to use the original work only if the author's successor transfers the renewal rights to the assignee."). In *Stewart*, the Court ruled that a successor copyright holder could prevent production of derivative works, where right to produce derivative works arose under agreement with original copyright holder who died before renewal term. *Id.* Apart from the facts that the *Stewart* case arose under the Copyright Act of 1909, Pub. L. No. 60-349, 35 Stat. 1075, and

To be more concrete, when *Author* transfers a copyright to *Person B* on February 1, 2009, there are three property interests to track for gift tax purposes: (1) the copyright transferred to *Person B*;⁶⁵ (2) the termination rights that arise in *Author* himself;⁶⁶ and (3) the termination rights that arise (contingently) in *Author*'s spouse and children.⁶⁷ It is clear that *Author* transfers the copyright by gift to *Person B*. It is less clear whether *Author* transfers (or if, instead, *copyright law creates*) the termination rights to (or in) *Author* and his heirs. Without a transfer by *Author*, there cannot be a gift-taxable transaction.⁶⁸ The next subsection evaluates whether, for gift tax purposes, there is a *transfer* by *Author* of the termination rights, and if so, how the transfer should be treated for gift tax purposes.

2. No Transfer, No Gift

Absent statutory rules on what constitutes a *transfer* for gift tax purposes, we look to case law for the meaning of the term. Generally speaking, for gift tax purposes, one cannot make a "transfer" to oneself.⁶⁹ Therefore, even if the author, not federal copyright law, is the source of the termination right, the author cannot *transfer* that right to himself for gift tax purposes. No gift tax will be imposed on the creation (or "retention") of the author's termination right.⁷⁰

Consider next whether the author transfers termination rights to his heirs. Case law suggests that no gift-taxable transfer occurs without a sufficient

involved renewal rights, not termination rights, the holders of termination rights in the property transferred in Hypothetical 1 are in a position analogous to the successor copyright holder—not the licensee—in *Stewart*. *Id.* at 212. The rights of *Author* or *Author*'s heirs to terminate the prior transfer in Hypothetical 1 are superior to *Person B*'s rights in the property, just as the successor copyright holder's rights were superior to the licensee's in *Stewart*.

65. *Supra* note 47 and accompanying text.

66. See 17 U.S.C. § 203(a)(1) (granting termination right to *Author*); see also *infra* Part III.B.2.

67. See 17 U.S.C. § 203(a)(2) (granting termination rights to *Author*'s heirs); see also *infra* Part III.B.2 (discussing the transfer of termination rights to an author's heir).

68. See I.R.C. § 2501(a)(1) (2006) (imposing a gift tax on any "transfer of property by gift"). A transfer is a condition precedent to the imposition of a gift tax. *Id.*

69. See Treas. Reg. § 25.2511-1(e) (as amended in 1997); *Comm'r v. Hogle*, 165 F.2d 352, 353 (10th Cir. 1947) ("[T]he tax cannot be sustained unless there was a transferor, a transferee, and an effective transfer . . .").

70. *But see infra* notes 83–88 and accompanying text (discussing application of I.R.C. § 2702).

degree of voluntariness.⁷¹ In *Estate of DiMarco v. Commissioner*,⁷² the decedent worked for a company that provided a benefit plan to all regular employees.⁷³ The decedent's spouse thus was entitled to a death benefit.⁷⁴ The United States Tax Court found that the decedent had not made a taxable transfer to his spouse of the value of the death benefit simply by going to work.⁷⁵ The court noted several factors: "the decedent's participation in the pension plan inaugurated by his employer was not voluntary," the decedent had no role in selecting the beneficiaries, and, except by resigning from his employment, the decedent could not defeat the beneficiaries' rights to the death benefit.⁷⁶ The court explained: "[W]e do not believe that a taxable event can occur for gift tax purposes unless there is first and in fact an act of transfer by the donor; and there can be no act of transfer unless the act is voluntary . . . that is, he must intend to do so."⁷⁷ In other words, accepting employment is not a "transfer" for gift tax purposes, absent any action directed toward the creation of the survivorship benefit.⁷⁸

Applying *DiMarco* to the creation of the heirs' termination rights in Hypothetical 1, the voluntariness required for the imposition of a gift tax appears to be present. When *Author* in Hypothetical 1 makes a gift of the copyright to *Person B*, *Author* takes specific and directed action with respect to the property in which the heirs' termination rights arise. Unlike the decedent in *DiMarco*, however, *Author* in Hypothetical 1 undertakes a "voluntary" action for the sole purpose of making a donative transfer. *Author* intentionally

71. See, e.g., *Estate of DiMarco v. Comm'r*, 87 T.C. 653, 663 (1986) ("[T]here can be no act of transfer unless the act is voluntary and the transferor has some awareness that he is in fact making a transfer of property, that is, he must intend to do so.").

72. See *id.* (holding that decedent did not make a taxable gift of the survivor's income benefit to his spouse, and the present value of the survivor's income benefit is not, therefore, an adjusted taxable gift).

73. *Id.* at 655. Under the benefit plan, if an employee died, an amount equal to three times the employee's annual compensation became payable to his or her surviving spouse and dependents. *Id.* The individual employee had no power to change the benefit, designate different beneficiaries or terminate the benefit (except by resigning from employment). *Id.* The Service sought to impose a gift tax. *Id.* at 657–58. The court, however, concluded that because the transfer to the surviving spouse was not sufficiently voluntary, it could not be subject to gift tax. *Id.* at 663.

74. See *id.* at 655 (explaining survivors benefit plan).

75. See *id.* at 622–63 ("Respondent argues, however, that decedent's simple act of going to work for IBM on January 9, 1950, constituted an act of transfer by decedent for gift tax purposes. We disagree.").

76. *Id.* at 662.

77. *Id.* at 663.

78. *Id.* at 662–63 (summarizing court's position that decedent's working at IBM did not constitute an act of transfer for gift tax purposes).

disposes of property that otherwise would be includible in his gross estate at death, thereby creating rights in his heirs.⁷⁹ For gift tax to function as a meaningful "back-stop" for estate tax, a donative transfer of a copyright should be precisely the type of voluntary action that gives rise to a taxable gift of the termination rights.⁸⁰

Admittedly, in both *DiMarco* and Hypothetical 1, the decedent lacks the ability to designate the recipients of the termination rights.⁸¹ But *Author* in Hypothetical 1 is fully aware that he is making a donative transfer (to *Person B*). *Author's* actions are sufficiently voluntary and connected to the creation of the termination rights so that a court likely would find that *Author's* creation of the termination rights is a transfer for gift tax purposes to the holders of the contingent termination rights.⁸² If so, the next question is what value the transfers have for gift tax purposes.

3. Valuing Sticky Copyrights

In order to determine the value of any taxable gift by *Author* in Hypothetical 1, we must determine not only the value of the interest transferred to *Person B* but also the value of the termination right (whether retained by *Author* or transferred to his heirs). Under I.R.C. § 2702, for purposes of valuing a donative transfer in trust to or for a member of the transferor's family,⁸³ an interest in trust retained by the transferor or certain members of the

79. *Supra* Part II.

80. *See* Estate of Sanford v. Comm'r, 308 U.S. 39, 44 (1939) (describing purpose of gift tax as "to prevent or compensate for avoidance of death taxes"). Again, this assumes that the author is treated as having made a transfer of the termination rights. *Supra* notes 71–73 and accompanying text.

81. *See* Estate of DiMarco v. Comm'r, 87 T.C. 653, 655 (1986) (describing decedent's inability to alter, amend, revoke, or terminate the Group Life Insurance and Survivors Income Benefit Plan).

82. For a discussion of the gift tax consequences of the characterization of the expiration of the termination right as a taxable lapse, see *infra* Part III.B.4. Note that if the author is alive at the time the termination window opens, the author may defeat the heirs' termination rights by revesting the property in himself. In a conventional analysis, this power should partially defeat the gift. *See* Treas. Reg. 25.2511-2 (as amended in 1999) (indicating that the donor's power to revoke or extinguish the gift negates it); *see also* Smith v. Shaughnessy, 318 U.S. 176, 181 (1943) ("The essence of a gift by trust is the abandonment of control over the property put in trust."). This analysis, however, must be subject to two qualifications. First, because the giver's ability to defeat the termination right is contingent upon surviving until the window opens, the value of the giver's retained right must reflect this contingency. Second, I.R.C. § 2702 (discussed in Part II.B.3, *infra*), somewhat supplants the conventional analysis, permitting the retention of such a contingent right to be disregarded in determining the value of the gift.

83. For purposes of I.R.C. § 2702, a transfer resulting in one or more term interests is

transferor's family is valued at zero, unless it is a "qualified interest."⁸⁴ A qualified interest is the right to receive fixed payments, at least annually; the right to receive a fixed percentage of the fair market value of property held in trust, payable at least annually; or a noncontingent remainder interest in certain trusts.⁸⁵ A copyright termination right does not meet the definition of a "qualified interest" for purposes of I.R.C. § 2702,⁸⁶ and so the rights of *Author* should have zero value for gift tax purposes.⁸⁷ Thus, the interest transferred to *Person B*, as well as the value of any retained or transferred termination right, would be taxable.⁸⁸

The next section considers what exclusions or deductions, if any, might be available in connection with a gift of a copyright or a copyright termination interest.

treated as a transfer in trust. *See* Treas. Reg. § 25.2702-4(a) (1992) ("For purposes of section 2702, a transfer of an interest in property with respect to which there are one or more term interests is treated as a transfer in trust. A term interest is one of a series of successive (as contrasted with concurrent) interests.").

84. *See* I.R.C. § 2702(a)(2)(A) (2006) ("The value of any retained interest which is not a qualified interest shall be treated as being zero."). A "qualified interest" means:

- (1) any interest which consists of the right to receive fixed amounts payable not less frequently than annually,
- (2) any interest which consists of the right to receive amounts which are payable not less frequently than annually and are a fixed percentage of the fair market value of the property in the trust (determined annually), and
- (3) any noncontingent remainder interest if all of the other interests in the trust consist of interests described in paragraph (1) or (2).

Id. § 2702(b).

85. *See id.* § 2702(b) (defining a "qualified interest").

86. *See id.* (giving three separate criteria, at least one of which must be met before interest can be considered "qualified"); *see also supra* note 85 and accompanying text (same). We assume throughout the remainder of this Article that the *author* is deemed to make a *transfer* of the termination rights that arise in his heirs. If this were not the case, the analysis would differ.

87. Prior to the enactment of I.R.C. § 2702, the author would not be deemed to have made a gift of the retained interest. *See* *Smith v. Shaughnessy*, 318 U.S. 176, 181 (1943) (reflecting the government's concession that the taxpayer did not make a gift of a retained reversion).

88. Presumably, the value of any copyright itself takes into account the likelihood that the termination rights will be exercised at some point in the future, among other factors. *See* GORDON V. SMITH & RUSSELL L. PARR, VALUATION OF INTELLECTUAL PROPERTY AND INTANGIBLE ASSETS 300-01 (2d ed. 1994) (explaining that the value of copyrights to an individual owner is solely represented by the present value of future royalty income). Beyond that, if one assumes that *Author* has made a taxable transfer of the termination rights, and that *Author's* interest has zero value for gift tax purposes, then all of the value—the fair market value of \$20,000—must be allocated between the interest transferred to *Person B* and the interests that arise in the giving author's spouse and heirs. It is not clear how that value should be allocated between the copyright transferee and the holders of the termination rights.

4. *Qualifying Sticky Copyrights for Beneficial Tax Treatment*

a. The Annual Exclusion

With any gift, one looks to see whether the transfer might qualify for the annual exclusion. Under I.R.C. § 2503(b)(1), gifts (other than gifts of future interests in property) are not included in the total amount of taxable gifts.⁸⁹ To the extent that the value of the copyright is less than the annual exclusion amount, some portion of the value of the transfer to *Person B* will escape taxation.⁹⁰ But the heirs' termination rights, exercisable no sooner than thirty-five years after the transfer of the copyright,⁹¹ are future interests that will not qualify for the annual exclusion.⁹²

b. The Marital Deduction

As a technical matter, it is possible that a lifetime gift of a copyright to a spouse might not qualify for the marital deduction.⁹³ The regulations explicitly provide that copyrights are terminable interests.⁹⁴ They further deny the marital deduction for a terminable interest when the transferor retains an interest in the transferred property and may "possess or enjoy any part of the property after the termination or failure of the interest therein transferred to the donee spouse."⁹⁵ To the extent that a copyright transferor is deemed to "retain" the termination right, even though the right arises by operation of law,⁹⁶ no marital deduction would appear to be available. As a matter of policy, such a result would be problematic. In effect, copyright holders would be unable to make tax-free transfers to their spouse of their intellectual property. Contrast this with the ability of owners of virtually every other type of property to make tax-free lifetime gifts. There is no justification for such inequity.

89. I.R.C. § 2503(b)(1).

90. *See id.* (explaining that gifts up to the annual exclusion amount are not counted as taxable gifts); *see also supra* note 49 and accompanying text (same).

91. *See* 17 U.S.C. § 203(a)(3) (2006) (setting timetable for exercise of termination rights); *see also supra* note 26 and accompanying text (same).

92. *See* I.R.C. § 2503(b)(1) (excluding future interests in property from qualifying as tax-exempt gifts); *see also supra* notes 80–88 and accompanying text (discussing the creation and valuation of heirs' contingent termination of rights).

93. I.R.C. § 2523(b) (2006); Treas. Reg. § 25.2523(b)-1(c) (1994).

94. Treas. Reg. § 25.2523(b)-1(a)(3).

95. Treas. Reg. § 25.2523(b)-1(c)(1).

96. *Infra* Part IV.B.1.

When an author makes a gratuitous transfer of an interest in copyright, consider the possibility that the termination rights arising in the author's spouse have value and that they qualify for the gift tax marital deduction.⁹⁷ Generally speaking, gifts to a spouse who is a United States citizen will qualify for the marital deduction under I.R.C. § 2523 unless the transferred property is a nondeductible terminable interest.⁹⁸ A terminable interest is one which "will terminate or fail on the lapse of time or on the occurrence or failure to occur of some contingency."⁹⁹ Examples of terminable interests include life estates, terms of years, patents, and copyrights.¹⁰⁰ Like a term of years, a copyright interest lasts for a fixed period of time.¹⁰¹ But not all terminable interests are nondeductible.¹⁰² For gift tax purposes, nondeductible terminable interests arise:

(1) if the donor retains in himself, or transfers or has transferred (for less than adequate and full consideration in money or money's worth) to any person other than such donee spouse (or the estate of such spouse), an interest in such property, and if by reason of such retention or transfer the donor (or his heirs or assigns) or such person (or his heirs or assigns) may possess or enjoy any part of such property after such termination or failure of the interest transferred to the donee spouse; or

(2) if the donor immediately after the transfer to the donee spouse has a power to appoint an interest in such property which he can exercise (either alone or in conjunction with any person) in such manner that the appointee may possess or enjoy any part of such property after such termination or failure of the interest transferred to the donee spouse.¹⁰³

97. See *id.* § 2523(a) (establishing the gift tax marital deduction).

98. See *id.* § 2523 (allowing for the marital deduction except where the gift is a life estate or a terminable interest and other enumerated conditions apply).

99. Treas. Reg. § 25.2523(b)-1(a)(3) (1994); see also I.R.C. § 2056(b)(1) ("Where, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail, no deduction shall be allowed.").

100. Treas. Reg. § 25.2523(b)-1(a)(3) (1994) ("Life estates, terms for years, annuities, patents, and copyrights are therefore terminable interests.").

101. Except in the case of works made for hire, copyrights in works created after January 1, 1978, last for the life of the author plus seventy years. See 17 U.S.C. § 302(a) (2006) ("Copyright in a work created on or after January 1, 1978, subsists from its creation and, [subject to certain exceptions], endures for a term consisting of the life of the author and 70 years after the author's death.").

102. See I.R.C. § 2523(b) (2006) (giving conditions whereby a transfer of a terminable interest is nondeductible).

103. *Id.*

To take the classic example, assume that a transferor creates a lifetime income interest in her transferee-spouse. Upon the death of the transferee-spouse, the remainder in the property passes to the children of the transferor.¹⁰⁴ In this example, the transferee-spouse's life estate is a terminable interest because it will terminate upon the death of the transferee-spouse.¹⁰⁵ It does not qualify for the marital deduction (i.e., it is nondeductible) because the remainder will pass to the transferor's children without consideration.¹⁰⁶ If, however, the transferor's children obtained the remainder interest by purchasing it from the transferor—instead of by gift from the transferor—then the spouse's income interest would qualify for the marital deduction, even though it is a terminable interest.¹⁰⁷

In the case of lifetime transfers of a copyright, a surviving spouse's termination rights become vested only if (1) the author does not exercise the termination right before her death; (2) the spouse survives the author; and (3) the spouse exercises the termination right while the window is still open.¹⁰⁸ If any one of these conditions is not met, then the termination right in the author's spouse evaporates. In Hypothetical 1, at the time of the gift by *Author* to *Person B*, the interest of *Author's* spouse (the termination right) would appear to be a terminable interest. It will cease to exist if, for example, *Author* exercises his termination right, or if the spouse predeceases *Author*, or if the other heirs refuse to join with the spouse in exercising the right.¹⁰⁹

104. See, e.g., JESSE DUKEMINIER ET AL., PROPERTY 226 (6th ed. 2006) (explaining that a life estate with no remainder reverts back to the grantor or, if the grantor predeceases the life tenant, to the grantor's heirs through the grantor's will).

105. See Treas. Reg. § 25.2523(b)-1(a)(3) (1994) ("*Life estates*, terms for years, annuities, patents, and copyrights are therefore terminable interests." (emphasis added)).

106. See I.R.C. § 2056(b)(1) ("Where, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail, no deduction shall be allowed.").

107. It has been suggested that, in permitting a deduction for the value of the life estate in an example like this, the Internal Revenue Code inadvertently creates gaming opportunities for taxpayers. See David A. Handler & Deborah V. Dunn, *RPM Trusts: Turning the Table on Chapter 14*, TR. & EST., July 2000, at 31, 39 ("In an RPM Trust, the grantor will not hold an interest in the property both before and after the transfer, and thus Sec. 2702(a) would not apply.").

108. See 17 U.S.C. § 203(b)(2) (2006) ("The future rights that will revert upon termination of the grant become vested on the date the notice of termination has been served The rights vest in the author, authors, and other persons named in, and in the proportionate shares provided [by the statute].").

109. See I.R.C. § 2056(b)(1) (2006) ("Where, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail, no deduction shall be allowed."); see also Rev. Rul. 82-184, 1982-2 C.B. 215 (indicating that, where the spouse must make an election in order to

Furthermore, in Hypothetical 1, *Author* receives no consideration for the transfer, and so the marital deduction would not be allowed.¹¹⁰ For that reason, the transfer of the termination rights to *Author's* spouse should not qualify for the gift tax marital deduction.¹¹¹

Note that the Internal Revenue Service (the Service) has embraced a case-law exception to the terminable interest rule where the transferee spouse is given an elective right to take the donor's (or decedent's) property.¹¹² The Service permits a deduction even though the property would pass to a third party without consideration if the spouse allowed a lapse to occur.¹¹³ While this exception probably would not be available in the copyright context, the contours of the authorities are illuminating.

In *Estate of Mackie v. Commissioner*,¹¹⁴ the United States Tax Court addressed the question of whether a bequest to a surviving spouse at the

receive the interest, it must be unconditionally exercisable by the spouse—nonterminable—in order to qualify for the marital deduction).

110. See I.R.C. § 2523(b)(1) (stating that a nondeductible interest arises when the author "retains in himself, or transfers or has transferred *for less than adequate and full consideration in money or money's worth* to any person other than such donee spouse" (emphasis added)).

111. Cases decided under the estate tax rules suggest that where a spouse's interest is subject to a condition precedent other than an election by the spouse, no marital deduction is allowed. Absent any direct gift tax authority on point, however, the estate tax law supplies guidance because courts must interpret estate and gift tax laws *in pari materia*. See, e.g., *Merrill v. Fahs*, 324 U.S. 308, 311 (1945) ("[T]he gift tax was supplementary to the estate tax. The two are in *pari materia* [sic] and must be construed together." (quoting *Estate of Sanford v. Comm'r*, 308 U.S. 39, 44 (1939))); *Comm'r v. Weymyss*, 324 U.S. 303, 306 (1945) (noting that "Congress directed [the estate and gift tax laws] to the same purpose, and they should not be separated in application"); cf. *Natchez v. United States*, 705 F.2d 671, 676 (2d Cir. 1983) (applying a gift tax rule to an estate tax question in part because of "the Supreme Court's consistent rulings that the estate tax and gift tax are to be construed *in pari materia*" (citations omitted)). On conditions precedent, see Rev. Rul. 82-184, 1982-2 C.B. 215 ("A cash bequest in lieu of a life estate, payable unconditionally at the election of a surviving spouse within a reasonable time after the decedent's death qualifies for the estate tax marital deduction under section 2056 of the Code.").

112. See Rev. Rul. 82-184, 1982-2 C.B. 215 (incorporating *Mackie* and *Neugass* into the decision to allow a deduction despite the existence of a *terminable* interest). Both of these cases are discussed at length *infra*.

113. See *Estate of Mackie v. Comm'r*, 545 F.2d 883, 884 (4th Cir. 1976) (allowing the deduction despite the fact that "a person other than the surviving spouse could, under the terms of the bequest, if Mrs. Mackie did not elect to take under item nine, come into the possession or enjoyment of the property" without consideration).

114. See *Estate of Mackie v. Comm'r*, 64 T.C. 308, 310 (1975) (declining to accept the Commissioner's argument that "the possibility of [Petitioner's] failure or refusal to accept, coupled with the gift over in such an eventuality," meant the bequest was not entitled to the deduction), *aff'd*, 545 F.2d 883 (4th Cir. 1976).

spouse's election qualified for the marital deduction.¹¹⁵ In *Mackie*, the decedent bequeathed certain property to his wife and gave her the right to select from the estate other property, so that the total value of the property she received equaled the full estate tax marital deduction.¹¹⁶ The only restraint on Mrs. Mackie's interest was that her election must occur within four months of the decedent's date of death.¹¹⁷ If Mrs. Mackie failed to make the election, she would be deemed to have rejected the bequest.¹¹⁸

The Service asserted a deficiency against the estate on the grounds that the bequest to Mrs. Mackie did not qualify for the marital deduction.¹¹⁹ The taxpayer argued that Mrs. Mackie acquired a "vested indefeasible interest" in the bequest as of the moment of her husband's death, and that the election was a mere formality for "perfection" of that interest.¹²⁰ In finding for the taxpayer, the court reasoned that Mrs. Mackie's interest was not subject to a condition precedent, and as such, it qualified for the marital deduction.¹²¹ The court explained that Mrs. Mackie was in the same position as a surviving spouse who is disinherited and subsequently elects against the will.¹²² If amounts passing pursuant to an election *against* a will qualified for the marital deduction, amounts passing pursuant to an election *under* a will should, too, the court reasoned.¹²³ Because Mrs. Mackie's right, like a statutory right of election, was

115. See *id.* (ruling in favor of petitioner despite the Commissioner's characterization of the will as a "conditional bequest" that was terminable and "non-deductible").

116. See *id.* at 309 (describing the will's instruction that the wife should have "properties to be selected by her . . . equal in total value to the remainder of the said maximum deduction or exemption so computed").

117. See *id.* (repeating the will's provision that the "election she shall make by a statement in writing to that effect delivered to [the testator's] executrix within four months from the date of [the testator's] death").

118. See *id.* (quoting that "failure of [testator's] said wife to deliver such statement to [testator's] executrix within such time shall be deemed an election by her to reject this devise, bequest and appointment in full").

119. See *id.* at 310 (repeating the Commissioner's argument that "the possibility of [petitioner's] failure or refusal to accept, coupled with the gift over in such an eventuality," meant the bequest was not entitled to the deduction).

120. *Id.*

121. See *id.* at 313 (distinguishing bequests held nondeductible "because conditioned on the beneficiary's performance of acts *in addition to* merely accepting the bequest" that "had independent legal significance and constituted substantive limitations both on the power of acceptance and on the interest transferred").

122. See *id.* at 312 ("Mrs. Mackie was put in the same position as a disinherited surviving spouse who is given a statutory right of election . . . [Here] her right of election is encompassed by the will rather than by statute, but we perceive this to be a difference without a distinction." (citations omitted)).

123. See *id.* (noting the "difference without a distinction" between statutory election and

unqualified, the property passing to her was eligible for the marital deduction.¹²⁴

Like *Mackie*, the decedent in *Estate of Neugass v. Commissioner*¹²⁵ bequeathed property to his surviving spouse at the survivor's election.¹²⁶ In *Neugass*, the decedent owned a substantial art collection.¹²⁷ In his will, he bequeathed to his wife a life estate in the artwork and gave her the right, exercisable within six months of his death, to "elect to take absolute ownership of any item, whereupon said item shall become the absolute property of my wife."¹²⁸ Upon the death of the wife, a life estate in the art would pass to the decedent's daughter, if living, or if not, to a named charity.¹²⁹ Mrs. Neugass did in fact elect to take absolute ownership of certain of the artwork, and the executors of the estate claimed a marital deduction under I.R.C. § 2056(b) for the value of the artwork passing outright to Mrs. Neugass.¹³⁰ The taxpayer appealed from the Tax Court's disallowance of the estate tax marital deduction.¹³¹

In finding for the taxpayer, the United States Court of Appeals for the Second Circuit reasoned that Mrs. Neugass received an alternative bequest (i.e., either a life estate or outright ownership).¹³² The court rejected the Service's

right of election conferred in a will).

124. See *id.* at 314 ("Mrs. Mackie was given the absolute right to take outright a specified portion of decedent's estate . . . the property which she received passed to her within the meaning of section 2056(a) and (e) and did not constitute a terminable interest within the meaning of section 2056(b).").

125. See *Estate of Neugass v. Comm'r*, 555 F.2d 322, 328 (2d Cir. 1977) (deciding that "[t]he statutory policy governing the disposition of the 'elective share' cases is applicable to the testamentary election situation as presented here" and ordering judgment for the taxpayer).

126. See *id.* at 327 ("The decedent's will . . . gave Mrs. Neugass the choice between a life use of the 'collection' . . . or the vested indefeasible interests of absolute ownership of any or all of the items she selected . . .").

127. See *id.* at 323 (recognizing the claimed value of the part of the art collection chosen by spouse as \$383,495.00).

128. *Id.* at 323 n.2.

129. See *id.* at 323 n.1 (quoting the will as directing "life use of said collection" to the daughter upon death of the wife and to the charity should the daughter not survive the wife).

130. See *id.* at 323 ("Ludwig Neugass' executors claimed a marital deduction in the amount of \$682,605.12 including \$383,495.00 for the value of the works of art of which decedent's widow elected to take absolute ownership.").

131. See *id.* at 325 ("[A]ppellants seek a determination by this court that the interest acquired by Mrs. Neugass pursuant to Article FIFTH was an alternative or elective bequest and, as such was a non-terminable interest which qualified for the marital deduction.").

132. See *id.* at 327 ("[W]e are of the opinion that Mrs. Neugass had, under the provisions of the decedent's will, a mere election between alternatives.").

plea to disregard *Mackie* as "contrary to controlling legal principles."¹³³ Instead, the court likened the *Neugass* case to *Mackie*, explaining that Mrs. Neugass, like Mrs. Mackie, faced a choice, and alternate bequests, on their face, did not preclude eligibility for the estate tax marital deduction.¹³⁴ The court drew on evidence that the testator intended to provide his wife with "maximum flexibility,"¹³⁵ that he intended the bequest to qualify for "as full a marital deduction as the law allowed,"¹³⁶ and that Mrs. Neugass became entitled to absolute ownership of property from the decedent's estate.¹³⁷

The Service has embraced these cases.¹³⁸ In doing so, the Service emphasizes that the transferee spouse must be given an absolute right to take the property, and that the election must in fact be made within a reasonable time after the transfer giving rise to the right of election.¹³⁹ In Hypothetical 1, the spouse's termination rights cannot be exercised for a period of years and so any election is deferred until the window opens. Moreover, the transferee-spouse's termination rights are contingent upon survivorship of *Author* and *Author's* nonexercise of the right.¹⁴⁰ Thus the *Neugass-Mackie* exception to the terminable interest rule likely would not apply to copyright termination rights.

133. See *id.* ("Commissioner . . . contends that *Mackie* and this case are contrary to our opinion in [*Allen*], and the 'controlling federal legal principles.' *Allen*, however, is distinguishable from both.").

134. See *id.* at 326 ("The indication is then clear that Article FIFTH did not contain, explicitly or impliedly, a power of appointment, but instead an alternative bequest.").

135. *Id.*

136. *Id.*

137. *Id.* at 327.

138. See Rev. Rul. 82-184, 1982-2 C.B. 215 (using *Mackie* and *Neugass* as support for the adoption of this exception to the terminable interest rule).

139. See *id.* ("A cash bequest in lieu of a life estate, payable *unconditionally* at the election of the surviving spouse *within a reasonable time* after the decedent's death qualifies for the estate tax marital deduction under section 2056 of the Code." (emphasis added)).

140. See I.R.C. § 2056(b)(1) (2006) ("[O]n the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail . . ."). Because the transferee-spouse's termination rights depend upon (a) *Author* having a right of survivorship from the transfer to *Person B* and (b) *Author* failing to exercise the termination right for himself, the transferee-spouse cannot be said to have a "nonterminable" interest. See *supra* Part III.B.1 (describing the general rules applicable to gifts).

*c. Consequences of Failing to Qualify for the Available
Exclusions and Deductions*

Because copyright termination interests likely will not qualify for the annual exclusion or the gift tax marital deduction,¹⁴¹ any deemed transfer of termination rights by the author will be fully taxable.¹⁴² So in Hypothetical I, when *Author* makes a lifetime gift of a copyright to *Person B*, assuming that he is the deemed transferor of the termination rights,¹⁴³ he makes a taxable gift of the interest transferred to *Person B*,¹⁴⁴ and that transfer is eligible for the annual exclusion.¹⁴⁵ In contrast, any gift of the termination right—a future interest—will not qualify for the annual exclusion.¹⁴⁶ The failure to qualify the termination rights for the annual exclusion is another example of how copyright

141. How might a giving or selling author overcome the problem that a spouse's copyright termination interest is terminable? Consider this hypothetical:

Hypothetical 1.5. *Author* is married and has two adult children. *Author* already applied his maximum unified credit to prior lifetime transfers. On January 1, 2009, each of *Author* and his wife made a \$13,000 annual exclusion cash gift to their child, *Adult Daughter A*. Taxpayer is the creator and owner of a copyright having a fair market value of \$20,000. *Author* wants to make a gift of the copyright to *Adult Daughter A*, but he is concerned that the termination rights that arise in the spouse (*Adult Daughter A*'s mother) would not qualify for the marital deduction. *Author* sells the copyright to *Adult Daughter A* for \$20,000 minus *x*. *Adult Daughter A* pays her mother *x* for the mother's copyright termination interest that will arise on account of the sale.

Assume (however unrealistically for discussion purposes) that \$20,000 represents adequate and full consideration for all interests in the copyright. Although a sale ordinarily might take a transaction outside the scope of the nondeductible terminable interest rule, federal copyright law prevents the mother from divesting herself from her copyright termination rights. 17 U.S.C. § 203(a)(1)–(2) (2006). Thus, the same problem would arise if *Author* sold the copyright to his spouse, and the spouse paid *Adult Daughter A* for the daughter's termination interest.

142. See I.R.C. § 2056(a) (setting the value of the taxable estate after deducting certain property passing to the surviving spouse). The statute provides:

[T]he value of the taxable estate shall . . . be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

Id. Because no deductions apply to the transfer of termination rights, they will be taxable in full. *Id.*

143. *Supra* note 71 and accompanying text.

144. See Treas. Reg. § 25.2512-1 (as amended 1992) ("[I]f a gift is made in property, its value at the date of the gift shall be considered the amount of the gift. The value of the property is the price at which such property would change hands between a willing buyer and a willing seller . . .").

145. I.R.C. § 2503(b).

146. *Supra* Part III.B.4.a.

owners are treated more harshly for tax purposes than are other property owners. The law should not support this discrimination. Furthermore, given how difficult it is to allocate value between the copyright transferee and the holders of the termination rights,¹⁴⁷ administration of a gift tax on the transfer of termination rights would be extremely complex. The next section considers the possibility that a disclaimer could be used to avoid these difficulties.

5. Planning with Sticky Copyrights

Because of the unique nature of copyrights, many standard tax planning techniques will be unavailable. Consider, for example, the use of disclaimers. Disclaimers are a standard feature of any post-mortem tax plan.¹⁴⁸ Used correctly, disclaimers can prevent a gift from occurring in order to avoid an adverse tax result.¹⁴⁹ Generally speaking, a disclaimer causes property to pass as if the disclaimant had predeceased the transferor.¹⁵⁰ But disclaimers have no application to termination rights.¹⁵¹ By law, termination rights are not alienable,¹⁵² and therefore statutory heirs may not disclaim them.¹⁵³ A gift of

147. *Supra* note 88 and accompanying text.

148. *See generally* Mitchell M. Gans, *Disclaimers*, 46 INST. ON FED. TAX'N § 52.01 (1988); Steve R. Akers, *Postmortem Planning Considerations: A Review of Income, Gift, and Estate Tax Planning Issues*, SN0 ALI-ABA 1211 (2007) (explaining the many uses of disclaimers in postmortem planning).

149. *See* DUKEMINIER ET AL., *supra* note 36, at 132 ("The most common motivations for disclaimer are to reduce taxes or to keep property from creditors."); *see also* *Jewett v. Comm'r*, 455 U.S. 305, 310 (1982) ("[T]he practical effect of petitioner's disclaimers was to reduce the expected size of his taxable estate and to confer a gratuitous benefit upon the natural objects of his bounty.").

150. *See* DUKEMINIER ET AL., *supra* note 36, at 133 ("[A]lmost all states have enacted disclaimer legislation that provides that the disclaimant is treated as having predeceased the decedent."); *see also* UNIF. PROBATE CODE § 2-1106(b)(3)(B) (2006) ("If the disclaimant is an individual, except as otherwise provided in subparagraphs (C) and (D), the disclaimed interest passes as if the disclaimant had died immediately before the time of distribution.").

151. *See* 17 U.S.C. § 203(a)(1)–(2) (2006) (naming all the procedures for postmortem transfer of termination rights without allowing for disclaimers).

152. *See id.* § 203(a)(5) ("Termination of the grant may be effected notwithstanding any agreement to the contrary, including an agreement to make a will or to make any future grant."). *But see* Allison M. Scott, *Oh Bother: Milne, Steibeck, and an Emerging Circuit Split over the Alienability of Copyright Termination Rights*, 14 J. INTELL. PROP. L. 357, 368 (2007) ("The Ninth Circuit's interpretation of the termination provisions of the Copyright Act and their interaction with state contract law has created tension between Ninth Circuit courts and Second Circuit courts with respect to the question of the alienability or inalienability of termination rights.").

153. *See* I.R.C. § 2518 (2006) (defining a disclaimer as a method by which a transferee rejects an interest given by a transferor, thus disqualifying the inalienable termination interest

copyright termination interest, then, is a gift that one must accept. Thus a taxable gift of termination rights may not be defeated by disclaimer. In addition, as Part IV discusses, the value of the termination right may be included in the giving author's gross estate at the giving author's later death.¹⁵⁴ This is to be contrasted with the inter vivos gift of an ordinary (i.e., noncopyright) asset, where the donor can prevent post-gift appreciation from being included in the gross estate. In this sense, copyrights are particularly sticky from a transfer-tax perspective.

C. The Selling Author and the Derivative Gift Syndrome

Moving away from a scenario in which an author makes a wholly donative transfer of a copyright, consider next an author who sells to a third party a copyright or an interest in a copyright. Somewhat counterintuitively, such a sale is partially sticky for gift tax purposes. The author makes a taxable gift of the heirs' termination rights. To illustrate, consider this variation on Hypothetical 1:

Hypothetical 2. *Author* is the creator and owner of a copyright having a fair market value of \$20,000. On February 1, 2009, in an arm's-length transaction with a third party (*Buyer*), *Author* sells the copyright in return for a payment of \$19,000 cash. The price is discounted to account for the termination rights, which are worth \$1,000.

Hypothetical 2 involves three separate property interests: the copyright itself, *Author's* termination rights, and the heirs' termination rights.¹⁵⁵ As in the case of the wholly donative transfer in Hypothetical 1, when *Author* sells the copyright to *Buyer* on February 1, 2009, *Author* may be deemed to retain a termination right for himself¹⁵⁶ and transfer a termination right to his heirs.¹⁵⁷ Those rights allow *Author* or his heirs to terminate the prior transfer to *Buyer*.¹⁵⁸ If *Author* dies before the exercise period without terminating the sale,

from the category). A qualified disclaimer causes the disclaimed property to pass directly from the initial transferor, not the disclaimant. *Id.* § 2518(a).

154. See *infra* Part IV (analyzing estate tax treatment of copyright interests).

155. See *supra* Part II (discussing termination rights of authors and their heirs).

156. See 17 U.S.C. § 203 (2006) (establishing an author's right to terminate the transfer of a copyright interest).

157. See *supra* Part III.B.1 (explaining that federal copyright law creates a termination right in the author and his heirs upon the author's transfer of the copyright).

158. See 17 U.S.C. § 203(a)(2) ("Where an author is dead, his or her termination is owned, and may be exercised, as follows . . ."). They may be exercised beginning on February 1, 2044, until February 1, 2049. At any time after February 1, 2034 (ten years before the

and his widow and adult children survive him, then *Author's* surviving spouse and children own—and may exercise—the termination rights.¹⁵⁹

We turn now to the question of whether an author makes a gift-taxable transfer of the termination right when the author sells a copyright to a third party. Recall that in *DiMarco*, the court held that a gift requires an element of voluntariness.¹⁶⁰ In that case, employment alone was an insufficient basis for finding that the decedent had made a gift of a survivor's benefit under an employee pension plan.¹⁶¹ In Hypothetical 2, *Author* sells a copyright to a third party, giving rise to termination interests, presumably worth \$1,000. Arguably the facts of Hypothetical 2 are distinguishable from the wholly donative transfer in Hypothetical 1, insofar as *Author* receives payment for the copyright. *Author* either will consume the amount realized from *Buyer* or own it at the time of his death (causing inclusion in *Author's* gross estate).¹⁶²

In Hypothetical 1, it seems fairly clear that *Author* engages in voluntary transfer of wealth to *Person B* sufficient to make the termination rights conferred on the heirs subject to the gift tax. The transfer in Hypothetical 2 is entirely different. In Hypothetical 2, *Author* does not set out to make a gift. To the contrary, *Author* sells the asset for its value and only indirectly confers rights on his or her heirs. *Author's* primary motivation appears to be the economic benefit from the copyright, not a gift to his heirs. In this sense, Hypothetical 2 is closer to *DiMarco* (although it is not clear). If this analysis is correct and Hypothetical 2 is analogous to *DiMarco*, then no gift should be deemed to occur in connection with the sale to *Buyer*.¹⁶³ Table A summarizes

commencement of the exercise period), but no later than February 1, 2042 (two years prior to the expiration of the exercise period), *Person B* must receive written notice of the intent to exercise the termination right. *See id.* § 203(a)(4) ("[T]ermination shall be effected by serving an advance notice in writing . . .").

159. *See id.* § 203(a)(2) (listing all the possible heirs of the termination right upon author's death).

160. *See Estate of DiMarco v. Comm'r*, 87 T.C. 653, 663 (1986) (noting that a taxable gift can only occur when there is "an act of transfer by the donor; and there can be no act of transfer unless the act is voluntary and the transferor has some awareness that he is in fact making a transfer of property").

161. *See id.* (rejecting the idea that "the simple act of going to work for an employer that has an automatic, non-elective, company-wide survivors income benefit plan . . . constitutes a 'transfer' of an interest in the benefit for either estate or gift tax purposes").

162. *See I.R.C.* § 2031(a) (2006) ("The value of the gross estate of the decedent shall be determined by including . . . the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated."). If *Author* consumes the full amount realized by the sale of the copyright to *Buyer* prior to death, it will not be included in this time-of-death valuation.

163. *See DiMarco*, 87 T.C. at 663 (holding that no gift took place).

the tax consequences of the lifetime transfers of copyrights discussed in this Part.

Table A: Gift Tax Consequences of Copyright Transfers			
Will gift tax be imposed on...	Type of Author		
	<u>Hoarder</u>	<u>Giver</u>	<u>Seller</u>
...value of copyright transferred?	n/a	Yes	No
...value of termination interest created in author?	n/a	No	No
...value of termination interest created in author's spouse?	n/a	Yes	Maybe
...value of termination interest created in author's heirs (other than spouse)?	n/a	Yes	Maybe

The next Part considers the estate tax consequences of transfers of copyrights.

IV. Estate Taxation of Copyright Interests

Copyrights are freely transferable by will.¹⁶⁴ Although heirs may have the right to terminate any of the decedent's lifetime transfers, if certain conditions are met,¹⁶⁵ they have no ability to terminate any testamentary transfers made by an author.¹⁶⁶ When an author dies, the value of all copyrights or interests in copyrights owned by the author will be included in her gross estate for federal estate tax purposes.¹⁶⁷ Generally, copyrights have an estate tax value equal to

164. See 17 U.S.C. § 203(a) (2006) (excluding transfer by will from the provisions of the statute).

165. *Supra* note 108 and accompanying text.

166. *Supra* Part III.B.5.

167. See I.R.C. § 2033 ("The value of the gross estate shall include the value of all property to the extent of the interest therein of the decedent at the time of his death."); see also Treas. Reg. § 20.2031-1(b) (as amended in 1965) ("The value of every item includible in a decedent's gross estate . . . is its fair market value at the time of decedent's death, except . . . if the executor elects the alternate valuation method . . ."). Fair market value is "the price at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of the relevant facts." *Id.* The valuation necessarily will take into account the time-limited nature of the copyright; between otherwise identical time-limited rights and rights unlimited in duration, the time-limited rights will be less valuable. See *Newark Morning Ledger Co. v. United States*, 507 U.S. 546, 556 (1993) ("Intangible assets such as patents and copyrights are depreciable over their 'legal lives,' which are specified by statute."). Therefore, the wealth transfer tax value of a copyright should reflect its limited duration.

their fair market value as of the decedent's date of death or as of the alternate valuation date, if the executor so elects.¹⁶⁸ This Part considers what amount, if any, will be included in the estate of a hoarding author, a giving author, and a selling author. The estate tax consequences are different in each case and may depend on the time of the author's death in relation to the termination period.

A. The Hoarding Author and the Estate Tax Marital Deduction

In the case of an author who dies without having made any lifetime transfers of copyrights, tax-free treatment of an author's sizeable estate will depend largely on the qualification of property in the estate for the marital deduction.¹⁶⁹ In order to qualify for the estate tax marital deduction, a property transfer must satisfy four requirements, which are somewhat similar to the gift tax marital deduction requirements:¹⁷⁰

168. See Treas. Reg. § 20.2031-1(b) (as amended in 1965) (explaining the fair market value/alternate valuation method scheme). The alternate valuation date is six months after the decedent's date of death. See Treas. Reg. § 20.2032-1(a) (as amended in 2005) (noting that alternatively valued property is valued either at the date it is sold "within six months" or at its fair market value "six months" after decedent's death). For an example of the valuation of copyright in an estate, see *Estate of Andrews v. United States*, 850 F. Supp. 1279, 1295 (E.D. Va. 1994). In that case, the district court approved the estate valuation of an author's copyrights as the amount of revenue they were expected to produce, discounted for marketing and other expenses, as well as the possibility that the copyrights would not be exploited. *Id.* at 1287. For a discussion of the challenges of valuing copyrights for estate tax purposes, see Bartow, *supra* note 9, at 401. Professor Bartow explains: "The long term value of a previously unexploited copyrighted work is exceptionally difficult to predict." *Id.* Previously exploited works are more susceptible to valuation, but challenges remain:

A copyright that is the subject of an exclusive license may generate easily calculable royalties during the term of the license, but the license may expire or can be terminated well before the end of the copyright term, posing valuation complexities for the unlicensed interval. Copyrights that are nonexclusively licensed provide some clues to their pecuniary merit based on past royalty-generating performances, but valuing them is still fraught with uncertainties because of the likelihood of changing societal tastes and desires throughout the lengthy duration of a typical copyright. A copyrighted song, for example, may sell many records, fade to obscurity, and then re-emerge more popular than ever decades later on a trajectory impossible to accurately predict or easily plan for.

Id.

169. See Jeffrey N. Pennell, *Tax Payment Provisions and Equitable Apportionment*, SH092 ALI-ABA 593, 613 (2003) ("With an 'optimum' or unlimited marital deduction, any normal estate tax imposed on the estate would be generated by property that did not qualify for the deduction.").

170. *Supra* Part III.B.4.b.

- (1) The property must be included in the gross estate of the decedent.
- (2) The property must "pass" from the decedent.
- (3) The property must pass to the decedent's surviving spouse.
- (4) The property interest must not be a non-deductible terminable interest.¹⁷¹

Generally speaking, a terminable interest is one "which will terminate or fail on the lapse of time or on the occurrence or the failure to occur of some contingency."¹⁷² Examples of terminable interests include life estates and terms of years.¹⁷³ Copyrights, too, are terminable interests.¹⁷⁴ Like a term of years, a copyright interest lasts for a fixed period of time.¹⁷⁵ But not all terminable interests are nondeductible.¹⁷⁶ Nondeductible terminable interests are those in which:

- (i) Another interest in the same property passed from the decedent to some other person for less than adequate and full consideration in money or money's worth, and

171. The Internal Revenue Code explains the restrictions as follows:

[T]he value of the taxable estate shall . . . be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

I.R.C. § 2056(a) (2006); *see also* Treas. Reg. § 20.2056(a)-1 (1958) ("A deduction is allowed . . . from the gross estate of decedent for the value of any property interest which passes from the decedent to the decedent's surviving spouse if the interest is a *deductible* interest" (emphasis added)).

172. Treas. Reg. § 20.2056(b)-1(b) (as amended in 1994); *see also* I.R.C. § 2056(b)(1) ("Where, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail, no deduction shall be allowed."); *supra* notes 99–102 (discussing terminable interests).

173. *See* Treas. Reg. § 20.2056(b)-1(b) (as amended in 1994) ("Life estates, terms for years, annuities, patents, and copyrights are therefore terminable interests.").

174. *Id.*

175. *See* 17 U.S.C. § 302 (2006) (explaining that except in cases of works made for hire, anonymous works, and pseudonymous works, copyrights in works created after January 1, 1978, last for the life of the author plus seventy years).

176. *See* Treas. Reg. § 20.2056(b)-1(a) (as amended in 1994) ("[T]he fact that an interest in property passing to a decedent's surviving spouse is a 'terminable interest' makes it nondeductible only . . . under the circumstances described in paragraph (c) of this section, and . . . if it does not come within one of the exceptions referred to in paragraph (d) of this section.").

- (ii) By reason of its passing, the other person or his heirs or assigns may possess or enjoy any part of the property after the termination or failure of the spouse's interest.¹⁷⁷

Evaluating these criteria, the value of a copyright interest is included in a hoarding author's gross estate.¹⁷⁸ If a hoarding author bequeaths a copyright to her surviving spouse, then the interest will pass from the decedent¹⁷⁹ and no person other than the surviving spouse may possess or enjoy any part of the copyright—by reason of the bequest—after the termination of the spouse's interest.¹⁸⁰ A bequest of a copyright to a surviving spouse, therefore, should qualify for the marital deduction.

One might think that an author's lifetime gift of a copyright is subject to gift tax, but not estate tax. But copyrights are "sticky" for both gift¹⁸¹ and estate tax purposes.¹⁸² The Internal Revenue Code (the Code) provides no specific rule for the estate taxation of copyright termination rights. The next section considers statutory grounds for an argument by the Service that some value associated with a copyright could be included in a deceased author's gross estate. We consider three different scenarios: the author's death before, during, and after the termination window.

B. The Giving Author Stuck on Copyrights

An author who gives an interest in a copyright simultaneously acquires a termination right that is exercisable during a specified time-period after the transfer.¹⁸³ Recall Hypothetical 1, in which *Author* gives *Person B* a copyright

177. Treas. Reg. § 20.2056(b)-1(c) (as amended in 1994).

178. See I.R.C. § 2033 (2006) ("The value of the gross estate shall include the value of all property to the extent of the interest therein of the decedent at the time of his death.").

179. See *id.* § 2056(a) ("[T]he value of the taxable estate shall . . . be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse . . ."); Treas. Reg. § 20.2056(a)-1 (as amended in 1994) ("A deduction is allowed under section 2056 from the gross estate of a decedent for the value of any property interest which passes from the decedent to the decedent's surviving spouse if the interest is a deductible interest as defined in § 20.2056(a)-2.").

180. See I.R.C. § 2056(a)(5) ("In the case of an interest in property passing from the decedent . . . no part of the interest so passing shall, for purposes of paragraph (1)(A), be considered as passing to any person other than the surviving spouse.").

181. See *supra* Part III.B (discussing the relevant provisions that yield the conclusion that an author's lifetime gift of a copyright is subject to a gift tax).

182. See *supra* notes 167–68 and accompanying text (discussing the implications of estate tax statutes on copyrights).

183. See 17 U.S.C. § 203(a)(3) (2006) ("Termination of the grant may be effected . . . at the

on February 1, 2009. In that case, *Author* may exercise his termination rights beginning on February 1, 2044, until February 1, 2049.¹⁸⁴ *Author* must do so by delivering a written notice of the intent to exercise the termination right any time after February 1, 2034 (ten years before the commencement of the exercise period), but no later than February 1, 2047 (two years prior to the expiration of the exercise period).¹⁸⁵ This Part considers the estate tax consequences of the giving author's death at three different points in time: before February 1, 2044; between February 1, 2044, and February 1, 2049 (assuming all notice requirements are met); and after February 1, 2049.

1. If the Giving Author Dies Before Termination Window Opens

If the giving author dies before the termination period, a portion of the copyright's value may be included in his gross estate under I.R.C. § 2036 and/or I.R.C. § 2037.¹⁸⁶ There should be no estate tax inclusion under I.R.C. §§ 2033, 2038, or 2041.¹⁸⁷ To begin the analysis, consider this noncopyright example:

Hypothetical 3. On February 1, 2009, *X* transfers property to *Y* for a period of thirty-five years. On February 1, 2044, the property will revert to *X*, if *X* is then living, or if not, to *X*'s estate.

In Hypothetical 3, if *X* dies before February 1, 2044, then the value of the property, less *Y*'s term interest, would be included in *X*'s gross estate under I.R.C. § 2036(a)(1).¹⁸⁸ Under that section, "except in case of a bona fide sale

end of thirty-five years from the date of publication of the work under the grant or at the end of forty years from the date of execution of the grant, whichever term ends earlier.").

184. *Id.*

185. *See id.* § 203(a)(4)(A) ("The notice shall state the effective date of the termination, which shall fall within the five-year period specified by clause (3) of this subsection, and the notice shall be served not less than two or more than ten years before that date.").

186. *See* I.R.C. § 2036(a) (2006) ("The value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer . . ."); *id.* § 2037(a) ("The value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time after September 7, 1916, made a transfer . . .").

187. *See infra* Part IV.C.3 (discussing the reasons that I.R.C. § 2033 does not apply); *infra* notes 214–18 and accompanying text (discussing I.R.C. § 2038); *infra* notes 219–28 and accompanying text (discussing I.R.C. § 2041).

188. *See* I.R.C. § 2036(a)(1) ("The value of the gross estate shall include the value of all property . . . if . . . possession or enjoyment of the property can, through ownership of such interest, be obtained only by surviving the decedent . . ."); *id.* § 2036(a)(2) (providing the weaker claim that the gross estate shall include the value of all property to the extent that the

for an adequate and full consideration in money or money's worth," the gross estate includes the value of all property,

to the extent of any interest therein of which the decedent has made a transfer . . . under which he has retained for his life or for any period not ascertainable without reference to his death or for any period that does not end before his death the possession, enjoyment, or right to income from, the property.¹⁸⁹

An author's termination interest is like a reversionary interest insofar as the author can repossess the copyright by delivering the requisite notice and surviving until the termination period.¹⁹⁰ If the author delivers the notice during lifetime but dies before the window opened, the copyright would become payable to the author's estate.¹⁹¹ Thus, just as with a reversionary interest, the value of the giving author's copyright, less the value of the donee's interest in the property, likely will be included in the author's estate under I.R.C. § 2036.¹⁹²

Observe that the Code does not specify whether rights that arise by operation of law (as opposed to the terms of a property transfer) are "retained" interests for purposes of I.R.C. § 2036(a)(1) or I.R.C. § 2036(a)(2).¹⁹³ Administrative rulings and case law provide some illumination. In Revenue Ruling 2004-64,¹⁹⁴ the Service addressed the impact of an express trust term or a local law that requires the trust grantor to be reimbursed for any income tax

decedent has retained "the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom").

189. *Id.* § 2036(a)(1).

190. *See id.* § 2038(b) ("For purposes of this section, the power to alter, amend, revoke, or terminate shall be considered to exist on the date of the decedent's death . . . whether or not on or before the date of the decedent's death notice has been given or the power has been exercised.").

191. *See id.* ("[I]f . . . notice has not been given or the power has not been exercised on or before the date of his death, such notice shall be considered to have been given, or the power exercised, on the date of his death."). For that reason, survival until actual delivery of written notice has the same legal effect as survival until actual termination.

192. Although Part IV.B.1 primarily discusses the application of I.R.C. § 2036(a)(1), I.R.C. § 2036(a)(2) should apply as well.

193. *See* I.R.C. § 2036 (2006) (stopping short of discussing retained interests beyond possession, the right to designate possession to others, and the right to vote). Note that the meaning of retention for purposes of I.R.C. § 2036(a)(1) is not necessarily applicable to other estate tax sections. *Supra* Part III.B.4.

194. Rev. Rul. 2004-64, 2004-2 C.B. 7 ("When the grantor of a trust, who is treated as the owner of the trust under subpart E, pays the income tax attributable to the inclusion of the trust's income in the grantor's taxable income, the grantor is not treated as making a gift of the amount of the tax to the trust beneficiaries.").

attributable to the trust.¹⁹⁵ In either case, the Service ruled, the full value of the trust's assets is includable in the grantor's estate for purposes of I.R.C. § 2036(a)(1).¹⁹⁶ Thus the Service considered irrelevant the issue of whether "retention" was accomplished by an affirmative provision in the instrument of transfer or by reason of a state statute.¹⁹⁷

In contrast to the position taken by the Service, there is case law that suggests that rights conferred on a taxpayer solely by operation of state law do not satisfy the retention requirement. In *Wyly v. Commissioner*,¹⁹⁸ the decedent transferred community property to an irrevocable trust that paid income to his wife for life, remainder to be held in further trust for the couple's grandchildren.¹⁹⁹ Under applicable Texas law, the decedent had a community property interest in the income from the trust.²⁰⁰ The Fifth Circuit ruled that rights bestowed on the decedent by state law did not constitute the retention of a "right to income" for purposes of I.R.C. § 2036(a)(1).²⁰¹ In the Fifth Circuit at least, then, explicit retention of a right—not a right arising by operation of state law—is a condition precedent to estate tax inclusion under I.R.C. § 2036(a)(1).²⁰² But because the position taken by the Service in Revenue

195. See *id.* ("[W]hat are the gift tax consequences when the grantor pays the income tax attributable to the inclusion of the trust's income in the grantor's taxable income, and . . . if, pursuant to the governing instrument or applicable local law, the grantor may or must be reimbursed by the trust . . . ?").

196. See *id.* ("If . . . the grantor must be reimbursed by the trust for the income tax payable by the grantor that is attributable to the trust's income, the full value of the trust's assets is includible in the grantor's gross estate under § 2036(a)(1).").

197. See *id.* ("If . . . the trust's governing instrument or applicable local law gives the trustee the discretion to reimburse the grantor for that portion of the grantor's income tax liability, the existence of that discretion . . . will not cause the value of the trust's assets to be includible in the grantor's gross estate.").

198. *Wyly v. Comm'r*, 610 F.2d 1282, 1294 (5th Cir. 1980) ("It is our conclusion that § 2036(a)(1) does not sweep the value of these transfers into the donor's gross estate.").

199. *Id.* at 1285.

200. See *id.* ("The crucial portions of that body of Texas law are those which cause the income from the separate property of a spouse to be the community property of both spouses.").

201. See *id.* at 1294 ("To summarize our review of federal and state law, we have held that the donor's community property interest in the income produced by these transferred properties is so limited, contingent, and expectant that it does not amount to a 'right to the income,' within the Act . . .").

202. See *id.* ("We do not believe that an interest, created solely by operation of law as the unavoidable result of what was in form and within the intent of the parties the most complete conveyance possible, is a retention within the Act."); *Comm'r v. Hinds*, 180 F.2d 930, 932 (5th Cir. 1950) ("[W]hether the income be regarded as separate property of the wife or as community income from the wife's separate property, the taxpayer retained neither 'the possession or enjoyment of, or the right to the income from,' the property so as to make applicable Sec. 811(c)(1)(B) . . .").

Ruling 2004-64 points in the other direction, it is difficult to predict the tax results with certainty.²⁰³ Note also that the estate might argue that the decedent never made the requisite transfer, in that rights were not volitionally conferred on the heirs.²⁰⁴ Also, even assuming that the section can be triggered where the decedent's rights are conferred solely by operation of law, I.R.C. § 2036 might be inapplicable because it can apply only when a decedent makes a transfer.²⁰⁵

Consider the application of I.R.C. § 2037 in the case of a giving seller who dies before the termination window opens. Under I.R.C. § 2037, the value of a decedent's gross estate includes the value of all property:

to the extent of any interest therein of which the decedent has . . . made a transfer (except in the case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, if—

(1) possession or enjoyment of the property can, through ownership of such interest, be obtained only by surviving the decedent, and

(2) the decedent has retained a reversionary interest in the property . . . and the value of such reversionary interest immediately before death of the decedent exceeds 5 percent of the value of such property.²⁰⁶

In effect, I.R.C. § 2037 includes in the decedent's gross estate transfers that are essentially testamentary in nature.²⁰⁷ For I.R.C. § 2037 to apply, four tests must be satisfied. First, there must be a transfer by the decedent.²⁰⁸ Second, the heirs' "possession or enjoyment of the property" must be conditioned on surviving the decedent.²⁰⁹ Third, the decedent must have "retained an interest

203. It is possible to reconcile Rev. Rul. 2004-264 with these cases. Compare Rev. Rul. 2004-64, 2004-2 C.B. 7 (positing the affirmative retention of the right to receive distributions from the trust), with *Hinds*, 180 F.2d at 932 ("[T]he taxpayer retained neither 'the possession or enjoyment of, or the right to the income from,' the property . . ."), and *Wyly*, 610 F.2d at 1294 ("We have further held that the interest arises only by operation of a mandatory definition contained in the Texas constitution which spouses may not circumvent, and that thus it is neither 'retained' within the meaning of the Act, nor arisen 'under' the transfers concerned.").

204. See I.R.C. § 2036(a) (2006) ("The value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time *made a transfer . . .*" (emphasis added)).

205. See *Estate of Skifter v. Comm'r*, 468 F.2d 699, 703 (2d Cir. 1972) ("[I.R.C. § 2036] is clearly not triggered in this case because it only applies to a power retained by the grantor over the income from property when he transferred it to another.").

206. I.R.C. § 2037(a).

207. Revenue Act of 1916, Pub. L. No. 64-271, § 202(b), 39 Stat. 756, 777-78 (1916).

208. I.R.C. § 2037(a).

209. *Id.* § 2037(a)(1); RICHARD B. STEPHENS ET AL., FEDERAL ESTATE & GIFT TAXATION

in the property that may bring the property back to the decedent."²¹⁰ Fourth, the value of the decedent's interest immediately before death must exceed five percent of the value of the property.²¹¹

Unlike I.R.C. § 2036, I.R.C. § 2037 clearly contemplates that it may apply even when the decedent's retained right arises by operation of law.²¹² Thus, the decedent's termination right can result in inclusion under this section in that, as the section requires, the decedent's spouse and heirs can only enjoy their rights by surviving the decedent. Nonetheless, the section will not apply if the value of the decedent's interest immediately before death is less than five percent of the value of the copyright (inclusive of the value of the termination right). Nor will it apply if the decedent is found not to have made a transfer because the creation of the termination rights is nonvolitional in nature.²¹³

Under I.R.C. § 2038, the value of a decedent's gross estate includes any interest in property of which the decedent has at any time made a transfer (except, as under I.R.C. § 2036, "in the case of a bona fide sale for an adequate and full consideration in money or money's worth") where enjoyment of the property was subject to the decedent's power to revoke, alter, amend, or terminate.²¹⁴ Note that unlike I.R.C. §§ 2036 and 2037, I.R.C. § 2038 has no retention requirement. A giving author in effect possesses a right to revoke the interests of the transferee (with respect to the copyright) and the interests of his or her heirs (with respect to the termination rights) at certain times.²¹⁵ Should this author die before the period for exercise of the termination right, however, no amount should be included in the author's estate under I.R.C. § 2038,²¹⁶ for, unlike I.R.C. § 2036, I.R.C. § 2038 does not apply where the decedent's power had been subject to an outstanding contingency at the time of death.²¹⁷ The

¶ 4.09[1] (8th ed. 2002).

210. I.R.C. § 2037(a)(2) (2006).

211. *Id.*

212. Treas. Reg. § 20.2037-1(f) (1958).

213. See *supra* Part III.B.2 (discussing the nonvolitional nature of termination rights).

214. I.R.C. § 2038(a)(1).

215. *Supra* Part II.

216. See I.R.C. § 2038(a)(1) (2006) ("The value of the gross estate shall include the value of all property . . . where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power . . . to alter, amend, revoke, or terminate . . ."). The statute also includes property in the gross estate "where any such power is relinquished during the 3-year period ending on the date of the decedent's death." *Id.* As discussed earlier, the imposition of gift tax requires some showing of voluntariness. *Supra* Part III.B.2. This assumes all relevant notice requirements have been met. *Supra* Part II.

217. See Treas. Reg. § 20.2038-1(b) (as amended in 1962) ("[S]ection 2038 is not applicable to a power the exercise of which was subject to a contingency beyond the decedent's control which did not occur before his death . . .").

requirement that the author be alive at the time the termination window opens—a contingency that did not occur—precludes application of I.R.C. § 2038.²¹⁸

Consider whether I.R.C. § 2041 might apply to the giving author who dies before the termination period. Under I.R.C. § 2041, the value of a decedent's gross estate includes "any property with respect to which the decedent has at the time of his death a general power of appointment."²¹⁹ A general power of appointment is any "power which is exercisable in favor of the decedent, his estate, his creditors or the creditors of his estate."²²⁰ When a giving or selling author transfers an interest in a copyright, federal copyright law creates in the author the right to reappoint the property to himself or herself.²²¹ But is a copyright termination right a general power of appointment?

The Treasury Regulations define as outside the scope of I.R.C. § 2041 any power existing as of a decedent's date of death that is subject to conditions precedent.²²² If a giving author dies before a copyright termination right is exercisable, then the condition precedent has not been satisfied and no amount should be included in the author's gross estate.²²³ To illustrate, consider this example:

Hypothetical 4. X transfers property in trust, payable to Y upon request, "when and if the Washington Nationals win a World Series during Y's lifetime." Y dies without the Washington Nationals ever having won a World Series.

In Hypothetical 4, Y's power is exercisable only if and when the Washington Nationals win the World Series. Such a win did not occur during Y's lifetime and, therefore, Y does not have a general power of appointment for purposes of I.R.C. § 2041.²²⁴ By analogy, where a giving author transfers a copyright to

218. See *id.* ("[S]ection 2038 is not applicable to a power the exercise of which was subject to a contingency beyond the decedent's control which did not occur before his death . . .").

219. I.R.C. § 2041(a)(2).

220. *Id.* § 2041(b)(1).

221. See *supra* Part II (discussing the conditions under which an author may exercise his right to terminate a transfer of the copyright).

222. Treas. Reg. § 20.2041-3(b) (1997) ("[A] power which by its terms is exercisable only upon the occurrence during the decedent's lifetime of an event or a contingency which did not in fact take place or occur during such time is not a power in existence on the date of the decedent's death."). For example, if a decedent was given a general power of appointment exercisable only after he reached a certain age, only if he survived another person, or only if he died without descendants, the power would not be in existence on the date of the decedent's death if the condition precedent to its exercise had not occurred. *Id.*

223. *Id.*

224. *Id.*

another, that transfer is revocable if the author lives to deliver the requisite termination notice.²²⁵ If the giving author dies before the termination window opens, the author could not have a general power of appointment.²²⁶ The results under I.R.C. § 2041 may be different, however, if the author dies during or after the period of termination.²²⁷ In addition, an argument also might be made by the author's estate that I.R.C. § 2041 does not apply to a self-created power.²²⁸

Finally, I.R.C. § 2033 cannot apply given that the decedent could not control by will the disposition of the termination right or any other interest in the copyright at her death.²²⁹

2. *If the Giving Author Dies During Period of Termination*

Consider next the tax consequences of a giving author's death during the period in which she may exercise the termination right. In such a case, inclusion in the author's gross estate may occur under these sections: I.R.C. §§ 2036(a)(1), 2036(a)(2), 2037, and 2038.²³⁰ To begin, consider these facts:

225. See *supra* note 31 and accompanying text (explaining that as long as notice is given, the author can die before termination actually occurs and the copyright still becomes part of his or her estate).

226. See Treas. Reg. § 20.2041-3(b) (1997) (explaining that only if the condition precedent to the power of appointment has occurred can the decedent exercise that power).

227. See I.R.C. § 2041(a)(2) (2006) ("[T]he power of appointment shall be considered to exist on the date of the decedent's death . . . whether or not on or before the date of the decedent's death notice has been given or the power has been exercised.").

228. See Treas. Reg. § 20.2041-1(b)(2) (1997) ("For purposes of §§ 20.2041-1 to 20.2041-3, the term 'power of appointment' does not include powers reserved by the decedent to himself within the concept of sections 2036 through 2038."); see also I.R.S. Priv. Ltr. Rul. 89-16-032 (Jan. 19, 1989) ("Section 20.2041-1(b)(2) of the Estate Tax Regulations provides that, for purposes of sections 20.2041-1 to 20.2041-3, the term 'power of appointment' does not include powers reserved by the decedent to himself within the concept of sections 2036 to 2038.").

229. *Infra* Part IV.C.1; see also Mitchell M. Gans et al., *Postmortem Rights of Publicity: The Federal Estate Tax Consequences of New State-Law Property Rights*, 117 YALE L.J. POCKET PART 203, 203, 206-09 (2008), available at <http://www.yalelawjournal.org/images/pdfs/658.pdf> (discussing the disadvantages of a California state law that permits descendible rights of publicity without limiting the decedent's ability to control the disposition of any postmortem rights of publicity); Mitchell M. Gans et al., *The Estate Tax Fundamentals of Celebrity and Control*, 118 YALE L.J. POCKET PART 50, 51 (2007), available at <http://www.yalelawjournal.org/images/pdfs/709.pdf> (stating that I.R.C. § 2033 "applies only where the decedent has the ability to exercise post-death control").

230. See *Helvering v. Safe Deposit & Trust Co. of Balt.*, 316 U.S. 56, 60 (1942) (noting that the power to appoint trust property to oneself does not require estate tax inclusion under the predecessor statute to I.R.C. § 2033); see also *infra* Part III.B.3 (noting that a copyright termination right does not require inclusion under I.R.C. § 2702).

Hypothetical 5. *Author* is the creator and owner of a copyright having a fair market value of \$20,000. On February 1, 2009, *Author* gives the copyright to *Person B* and receives no consideration in return. *Author* dies on February 2, 2044, when the termination window is open.

In Hypothetical 5, *Author* dies during the period in which the copyright transfer could be revoked. Thus, if the estate is unable to sustain an argument based on the elements of retention and transfer, inclusion in the gross estate should occur under I.R.C. § 2036.²³¹ In addition, without regard to the question of retention, I.R.C. §§ 2037 and 2038 may apply.²³²

Consider next the potential application of I.R.C. § 2041 in the case of an author who dies during the termination period. If, in Hypothetical 5, *Author* (as opposed to copyright law) is deemed for estate tax purposes to have created the termination right in herself, I.R.C. § 2041 likely does not apply.²³³

3. *If the Giving Author Dies After Termination Window Closes*

Consider next the tax consequences of a giving author's death after the termination window closes. In such a case, different rules might trigger inclusion in the author's gross estate.

Hypothetical 6. *Author* is the creator and owner of a copyright. On February 1, 2009, *Author* gives the copyright to *Person B* and receives no consideration in return. *Author* dies on February 1, 2054 (five years after the termination window closed), without having delivered any notice of termination.

231. Note, however, that Treas. Reg. § 20.2036-1 does not contain a rule similar to that found in Treas. Reg. §§ 20.2038-1(b) and 20.2041-3(b), which makes irrelevant any conditions precedent to the exercise. Compare Treas. Reg. § 20.2036-1 (as amended in 2008) (referring to retention, but not conditions precedent), with Treas. Reg. § 20.2038-1(b) (as amended in 1962) (making I.R.C. § 2038 inapplicable to "a power the exercise of which was subject to a contingency beyond the decedent's control which did not occur before his death"), and Treas. Reg. § 20.2041-3(b) (1997) (stating that a power "which by its terms is exercisable only upon the occurrence during the decedent's lifetime of an event or a contingency which did not in fact take place or occur during such time is not a power in existence on the date of the decedent's death").

232. See *Estate of Skifter v. Comm'r*, 468 F.2d 699, 703 (2d Cir. 1972) (indicating there is no retention requirement under I.R.C. § 2038); Treas. Reg. § 20.2037-1(f) (indicating that I.R.C. § 2037 applies even if retained right arises by operation of law).

233. See Treas. Reg. § 20.2041-1(b)(2) (as amended in 1961); I.R.C. § 2041(a)(1) (2006) (stating that the value of the gross estate includes "property with respect to which a general power of appointment created on or before October 21, 1942, is exercised by the decedent"); see also Treas. Reg. § 20.2041-3(a)(2) (1997) ("If the power is a general power of appointment, the value of an interest in property subject to such a power is includable in a decedent's gross estate.").

In Hypothetical 6, *Author* dies after the expiration of the period for exercise of the termination right. In that case, the passage of time has extinguished both *Author's* termination right and any termination rights to which his heirs might have succeeded. It is not likely that any amount will be included in *Author's* gross estate under I.R.C. §§ 2033,²³⁴ 2036,²³⁵ 2037,²³⁶ or 2038.²³⁷ But consider the potential gift tax consequences under I.R.C. § 2514.²³⁸

Under I.R.C. § 2514, a general power of appointment is any power which is exercisable in favor of the powerholder, her estate, her creditors, or the creditors of her estate.²³⁹ A lapse of a power is considered a release of the power.²⁴⁰ To the extent that the value of the property subject to the lapse (in Hypothetical 6, the value of the copyright) exceeds \$5,000, the lapse triggers gift tax liability under I.R.C. § 2514.²⁴¹ In Hypothetical 6, if the termination right is a power of appointment, then the giving author's failure to exercise it would be treated as a taxable lapse (or release) of a power of appointment, if the lapse is a completed gift.²⁴² Upon the

234. See *supra* note 230 (discussing how the power to appoint property to oneself does not require estate tax inclusion under the predecessor statute to I.R.C. § 2033).

235. See I.R.C. § 2036(a) (stating that the value of the gross estate includes any interest of which the decedent has made a transfer under which he has retained "for any period which does not in fact end before his death" possession, income or enjoyment of transferred property or the right to designate possession, income from, or enjoyment of the property).

236. See *id.* § 2037 (providing for estate tax inclusion of transfers that, among other things, become possessory only by surviving decedent).

237. If *Author* dies within three years of the expiration of the termination window, then the full value of the copyright may be included in *Author's* gross estate. See *id.* § 2035(a) (providing for the inclusion of certain property in gross estate if the decedent "relinquished a power with respect to any property, during the three-year period ending on the date of the decedent's death").

238. See *id.* § 2514 (describing tax treatment of property subject to powers of appointment and defining term).

239. See *id.* § 2514(c) ("[T]he term 'general power of appointment' means a power which is exercisable in favor of the individual possessing the power . . . his estate, his creditors, or the creditors of his estate.").

240. See *id.* § 2041(b)(2) ("The lapse of a power of appointment created after October 21, 1942, during the life of the individual possessing the power shall be considered a release of such power.").

241. *Id.* § 2514(e). The statute says the following:

The lapse of power of appointment . . . during the life of the individual possessing the power shall be considered a release of such power . . . only to the extent that the property which could have been appointed by the exercise of such lapsed power exceeds in value the greater of [\$5,000 or 5% of the property subject to the power].

Id.

242. See *id.* § 2511 (providing that gift tax is imposed on all direct and indirect gifts). Because it is a completed gift, there is a potential double taxation issue, given that I.R.C. § 2702 sets the value of any retained interest at zero. See *id.* § 2702 ("The value of any retained interest which is not a qualified interest shall be treated as being zero."); see also Treas. Reg. § 25.2702-

giving author's subsequent death on February 1, 2054 (five years after the termination window closed), the author would no longer possess a power of appointment, so for estate tax purposes, there would be no estate tax inclusion under I.R.C. § 2041.²⁴³

C. *The Selling Author Confronts Estate Tax*

An author who sells or licenses an interest in a copyright faces many of the estate tax challenges that a giving author does. The author's termination right is exercisable during a specified period after the transfer.²⁴⁴ This section explores the estate tax consequences of a selling author's death before, during, and after the termination period.

1. *If the Selling Author Dies Before Termination Window Opens*

If an author licenses a copyright to a third party and then dies before the time at which she could exercise her termination rights, then I.R.C. § 2033 will include in the author's estate the value of the author's anticipated royalties under the license.²⁴⁵ If, for example, the author sold a copyright in return for a right to receive \$1,000 per year for twenty years, and the author died after the first year of the transfer, then the

6(a) (1992) (providing additional adjustments to mitigate double taxation where the amount of the transferor's property was previously determined under I.R.C. § 2702). It might also be noted that if the author received consideration in exchange for allowing the termination interest to lapse, then the ordinary-course-of-business exception might be applicable. *See* Treas. Reg. § 25.2512-8 (the bona fide exception). So, for example, where an author licenses a copyright and then decides to allow the termination interest to lapse because she wishes to retain the valuable licensing fee, the ordinary-course-of-business exception should preclude a taxable gift from occurring.

243. *See* I.R.C. § 2041(a) (2006) ("The value of the gross estate shall include . . . any property with respect to which a general power of appointment . . . is exercised by the decedent . . . but the failure to exercise such a power or the complete release of such a power shall not be deemed an exercise thereof."). Note that if the lapse occurs less than three years before the decedent's death, then the gift tax paid on the taxable lapse is included in the decedent's gross estate. *See id.* § 2035(b) ("The amount of the gross estate . . . shall be increased by the amount of any tax paid . . . by the decedent or his estate on any gift made by the decedent . . . during the 3-year period ending on the date of the decedent's death.").

244. *Compare supra* Part IV.B (describing the estate tax consequences when a giving author dies before, during, or after the termination period), *with supra* Part IV.C (describing the estate tax consequences when a selling author dies before, during, or after the termination period).

245. *See* I.R.C. § 2033 ("The value of the gross estate shall include the value of all property to the extent of the interest therein of the decedent at the time of his death.").

author's estate would include the present value (as of the author's date of death) of the right to receive \$19,000, the remaining payments due under the license agreement.²⁴⁶

Consider whether I.R.C. § 2033 requires inclusion of any value attributable to the termination rights that could be exercised in the future by the author's heirs.²⁴⁷ Regardless of when a giving or selling author dies in relation to a prior copyright transfer, the value of these termination rights should escape inclusion in the decedent's gross estate under I.R.C. § 2033 by analogy to wrongful death benefits.²⁴⁸ Recall that termination rights arise in heirs only if the author is not alive when they become exercisable.²⁴⁹ The Service has ruled that state law wrongful death benefits are not included in a decedent's gross estate when the applicable statute creates in the decedent's heirs—as opposed to the decedent's estate—a cause of action that did not otherwise exist during the decedent's lifetime.²⁵⁰

In *Maxwell Trust v. Commissioner*,²⁵¹ the United States Tax Court addressed the question of whether the estates of two American citizens, killed in a plane crash in Japan, should include the value of settlement proceeds received by their heirs in a wrongful death action.²⁵² In that case, the court noted that under applicable local

246. See *id.* § 2039(a) ("The gross estate shall include the value of an annuity or other payment receivable by any beneficiary by reason of surviving the decedent under any form of contract or agreement . . . if, under such contract or agreement, an annuity or other payment was payable to the decedent."). Upon receipt, these royalties become income of a decedent under I.R.C. § 691(a) and are subject to unfavorable taxation. See *id.* § 691(a) (treating, for tax inclusion purposes, "the right . . . to receive an amount . . . as if it had been acquired by the estate or such person in the transaction in which the right to receive the income was originally derived").

247. See *id.* § 2033 ("The value of the gross estate shall include the value of all property to the extent of the interest therein of the decedent at the time of his death.").

248. See Gans et al., *The Estate Tax Fundamentals of Celebrity and Control*, *supra* note 229, at 51 (stating that a decedent's ability to control an interest post-death is necessary for estate tax inclusion under § 2033, and that, because a living person has no wrongful death claim during life, damages received under such a claim are not included in that person's gross estate).

249. See *supra* Part II (describing the termination rights of an author); see also I.R.C. § 2036(a) (2006) (stating that the value of the estate includes any interest of which the decedent has made a transfer under which he has retained "for any period which does not in fact end before his death . . . the possession or enjoyment of, or the right to income from, the property").

250. Rev. Rul. 69-8, 1969-1 C.B. 219 ("The decedent in his lifetime never had an interest in either the right of action or the proceeds. Therefore, with respect to damages recoverable under the Act, nothing passed from the decedent to the beneficiaries which would be includible in his gross estate for Federal estate tax purposes.").

251. See *Maxwell Trust v. Comm'r*, 58 T.C. 444, 451 (1972), *acq. in result*, 1973-2 C.B. 2 (holding that because local law vested the rights to the wrongful death proceeds in the dependents of the decedents and not in the decedents themselves, decedents' gross estates did not include the value of the proceeds under I.R.C. § 2033).

252. See *id.* at 448 ("The dispute in this case under section 2033 turns upon whether the

law, the decedents themselves had no such wrongful death claim against the airline or the airplane manufacturer.²⁵³ Because the local law "vested the rights to [wrongful death claims] in the dependents of the decedents and not in the decedents themselves or their estates," the court ruled that "section 2033 does not require inclusion of the settlement proceeds in the gross estates of the decedents."²⁵⁴ Concededly, copyright termination rights are different. Unlike wrongful death damages, the author is entitled to the termination right during life (though subject to the contingency that the author must survive until the rights are exercisable). This difference, however, is not one of consequence. For whenever a right is extinguished or otherwise disappears at the decedent's death, I.R.C. § 2033 cannot apply.²⁵⁵

In terms of I.R.C. § 2036, the Service likely would argue that the elements of transfer and retention are present and the estate therefore should include not only the present value of the royalty stream but also the present value of the termination right.²⁵⁶ Because the author received valuable consideration, the estate likely would

decedents had at the time of their deaths a claim against BOAC and Boeing on account of the airplane crash which passed to their estates.").

253. *Id.* at 451–52.

254. *Id.* at 451.

255. *Helvering v. Safe Deposit*, 316 U.S. 56, 60 (1942); *Wadewicz v. Comm'r*, 39 T.C. 925, 934–35 (1963).

256. *Eisen & Biblin*, *supra* note 10, at 7. Eisen and Biblin illustrate the effects of applying I.R.C. § 2036, though they argue against its application on the ground that the element of retention is absent. They use an example of an author (referred to as an "Entertainer") who dies with a \$21 million estate, comprised of \$1 million in cash and a copyright catalogue "worth" \$20 million in copyrights. The Entertainer makes a prior transfer of some of the copyrights, retaining a royalty interest valued, for illustration purposes, at \$12 million at the time of the Entertainer's death. *Id.* The Entertainer dies prior to the period in which he may exercise his termination rights. *Id.* Eight million dollars is the assumed date-of-death value of the proceeds from a fictive future sale of the post-termination interest. Eisen and Biblin believe that

the only amount that should be subject to estate tax upon the Entertainer's death is the \$12 million. Under the willing buyer/willing seller test for measuring value, all that a willing buyer would pay for the rights that the Entertainer had was \$12 million. At the instant of the Entertainer's death, if his estate attempted to sell its entire interest in the copyrights to a third-party purchaser, all that purchaser could acquire would be the right to receive royalties until a termination took place. No additional rights could be acquired from the Entertainer's estate. * * *

The IRS might not agree with the above result. In the above example, \$8 million of value was excluded from the Entertainer's estate. The half of this amount that will be enjoyed by the surviving spouse would have been sheltered by the marital deduction in any event, but the \$4 million of value that went to descendants effectively "escaped the system." The IRS might argue that estate tax inclusion should result under Section 2036 on the theory that the situation is analogous to a taxpayer transferring assets but retaining the income for himself. The problem with this argument is that the Entertainer never made a "transfer" of assets to his

invoke the bona fide sale exception. If the estate could establish that the decedent had received full and adequate consideration, the exception would apply and I.R.C. § 2036, as well as I.R.C. §§ 2037 and 2038, would be rendered inapplicable (enabling the estate to sidestep the retention and transfer issues). Although the scope of the exception is unclear, and there is no authority applying the exception in this context, it would seem to be unavailable on the rationale that the author did not receive full consideration.

The courts disagree on the precise meaning of the phrase "adequate and full consideration." One approach, adopted by courts in *United States v. Allen* in the Tenth Circuit,²⁵⁷ *Estate of Gregory v. Commissioner* in the United States Tax Court,²⁵⁸ and *Gradow v. United States* in the Federal Circuit,²⁵⁹ requires a decedent

descendants. The descendants' rights were granted to them by Congress by virtue of the copyright law, and not by a transfer from the Entertainer.

Id. (citations omitted).

257. See *United States v. Allen*, 293 F.2d 916, 917 (10th Cir. 1961) (finding that payment of fair market value for the life estate constitutes adequate and full consideration). In *Allen*, the decedent created a trust from which she was to receive three-fifths of trust income and her children were to receive two-fifths of trust income. *Id.* at 916. Upon her death, the trust assets would pass to her children. *Id.* At the age of 78, Mrs. Allen sold her income interest (having a stipulated value of \$135,000) to her son in a bona fide sale for \$140,000. *Id.* at 916–17. The decedent died shortly thereafter. *Id.* at 917. The Service argued that three-fifths of the trust corpus, less the \$140,000, should be included in Mrs. Allen's gross estate. *Id.* The United States Court of Appeals for the Tenth Circuit held that three-fifths of the value of the trust corpus should be included in her estate, on the grounds that, "[i]t seems certain in a situation like this, Congress meant the estate to include the corpus of the trust or, in its stead, an amount equal in value." *Id.* at 918. Practically speaking, *Allen*'s effect is to require a grantor of a trust who wishes to minimize estate tax to sell that life estate for more than its fair market value. This in turn raises the possibility that the purchaser would be deemed to make a gift to the grantor. For a discussion of *Allen*, see Mitchell M. Gans & Jonathan G. Blattmachr, Strangi: *A Critical Analysis & Planning Suggestions*, 100 TAX NOTES, Sept. 1, 2003, at 1153, 1166 (2003) ("[T]he court held that the grantor does not receive full consideration within the meaning of the exception unless she receives an amount equal to what would have been included in the gross estate had the sale not occurred.").

258. See *Estate of Gregory v. Comm'r*, 39 T.C. 1012, 1016 (1963) (finding that "adequate and full consideration" requires "a comparable value which would be includable in the transferor's gross estate"). In *Gregory*, the decedent's husband predeceased her, leaving a will that allowed the widow to either take under her share of the couple's community property or take under the will. *Id.* at 1013. Mrs. Gregory elected to take under the will, receiving personal effects, a probate homestead and family allowance, and an income interest in a trust funded by her husband's share of the community property and her share of the couple's community property, which she was required as a condition of the will to transfer to the testamentary trust. *Id.* at 1014–15. The parties stipulated that Mrs. Gregory's income interest in the community property of her husband was worth \$11,926.96; the value of her share of the community property, which she transferred to the testamentary trust, was \$65,925.08. *Id.* at 1017. The Tax Court ruled that the amount Mrs. Gregory was deemed to receive (\$11,926.96) was far less than what she transferred (\$65,925.08), and that therefore, her estate should include the value of the property she transferred to the trust, measured as of Mrs. Gregory's date of death, less the consideration she received. *Id.* at 1021–22.

259. See *Estate of Gradow v. United States*, 11 Cl. Ct. 808, 816 (1987), *aff'd*, 897 F.2d 516

who sold a partial interest in property to receive a consideration equal to the fair market value of the fee interest, not just the partial interest that is the subject of the sale, in order for the bona fide exception to apply. The other approach, adopted by courts in *United States v. Wheeler* in the Fifth Circuit,²⁶⁰ *Estate of Magnin v. Commissioner* in the Ninth Circuit,²⁶¹ and *D'Ambrosio v. Commissioner* in the Third Circuit,²⁶² requires a taxpayer to receive a consideration equal to the fair

(Fed. Cir. 1990) (finding "adequate and full consideration" in "the property which would otherwise have been included in her gross estate by virtue of her retention of a life estate"). In *Gradow*, the decedent's husband predeceased her, leaving a will that allowed the widow to either take under her share of the couple's community property or take under the will. *Id.* Mrs. Gradow elected to take under the will, receiving an income interest in a trust funded by her husband's share of the community property and her share of the couple's community property, which she was required as a condition of the will to transfer to the testamentary trust. *Id.* The parties stipulated that Mrs. Gradow's income interest in the community property of her husband was worth \$234,767; the value of her share of the community property, which she transferred to the testamentary trust, was \$444,641. *Id.* The Claims Court held, and the United States Court of Appeals for the Federal Circuit affirmed, that Mrs. Gradow's gross estate included the value of her community property which she transferred to the trust under her husband's will. *Id.* at 816. The Claims Court reasoned that any other rule would contradict "Congress' judgment that transfers with retained life estates are generally testamentary transactions and should be treated as such for estate tax purposes," and permit an otherwise abusive transfer to escape taxation. *Id.*

260. See *Wheeler v. United States*, 116 F.3d 749, 767 (5th Cir. 1997) ("[W]e hold that the sale of a remainder interest for its actuarial value as calculated by the appropriate factor set forth in the Treasury Regulations constitutes an adequate and full consideration under section 2036(a)."). In *Wheeler*, the decedent sold to his sons a remainder interest in a ranch in which the decedent retained a life estate. *Id.* at 751. The purchase price was determined by reference to the fair market value of the entire property and accepted actuarial principles for determining the value of the decedent's life estate. *Id.* at 752. The sons paid the purchase price with an interest-bearing note secured by the borrowers' personal guarantees. *Id.* The decedent's executor did not include in his gross estate any value with respect to the ranch, on the theory that the bona fide sale exception under I.R.C. § 2036(a)(1) applied to the sale of the remainder. *Id.* at 753. The Fifth Circuit embraced the interpretation of "adequate and full consideration" in the gift tax context, and pronounced the estate tax rule as follows: "[U]nless a transfer that depletes the transferor's estate is joined with a transfer that augments the estate by a commensurate (monetary) amount there is no 'adequate and full consideration' for the purpose of either the estate or gift tax." *Id.* at 762.

261. See *Estate of Magnin v. Comm'r*, 184 F.3d 1074 (9th Cir. 1998) ("[W]e hold that 'adequate and full consideration' is measured against the actuarial value of the remainder interest rather than the fee-simple value of the property transferred to the trust."). In *Magnin*, the decedent and his father agreed that decedent would bequeath his remainder interest in certain stock the family business to the decedent's children in return for the father's agreement to fund a trust for the decedent's benefit, essentially giving the decedent a life estate in the family business. *Id.* at 1075. The Ninth Circuit reversed the Tax Court's finding in favor of the Service and remanded the case for a determination of whether the value of the decedent's remainder interest was equal to the value of the life estate—in other words, did the decedent receive adequate and full consideration for the transfer. *Id.* at 1082.

262. See *Estate of D'Ambrosio v. Comm'r*, 101 F.3d 309, 318 (3d Cir. 1996) (finding that sale of remainder interest for its fair market value constitutes "adequate and full consideration"). In

market value of the partial interest that is the subject of the sale. Under this approach, the focus is on whether the transfer effects depletion in the transferor's estate. The exception becomes available because the consideration received for the partial interest, together with the value of the retained interest, prevents depletion from occurring.

Even under this more taxpayer-friendly line of cases, the exception will in all likelihood not be available.²⁶³ For the transfer consists not only of the copyright but also of the termination right to the spouse and children. The person acquiring the copyright does not pay any consideration for the value of the termination rights conferred on the spouse and children. Thus, an author who sells a copyright does in fact deplete her estate, rendering the exception unavailable. To illustrate, assume the author conveys a copyright and receives \$18 in an arm's-length transaction. Assume further that the value of the termination right, measured at the time of the conveyance, is \$2, one half of which is attributable to the author's termination right and the other half of which is attributable to the termination rights conferred on the author's spouse and children. Put differently, if under the copyright law the author could convey the termination rights and the copyright, the author would have received \$20. In these circumstances, the transaction results in depletion in that the author transfers an asset having a value of \$20 but has only \$19 in assets after the conveyance (the purchase price of \$18 plus the \$1 value of the author's termination right). Thus, even under the taxpayer-friendly approach, the author's estate could not qualify for the exception. Interestingly, however, with proper planning, the transaction could be made to qualify for the exception. If the author's children and spouse had paid the author \$1 for their termination rights, the transaction would have resulted in no depletion, thus permitting the estate to argue for the exception under the taxpayer-friendly line of cases.

D'Ambrosio, the decedent sold a remainder interest in stock for an annuity interest. *Id.* at 311. The parties stipulated that the remainder and the annuity had identical fair market values. *Id.* The Third Circuit addressed the question of whether the decedent must receive the fair market value of the interest she sold (in *D'Ambrosio*, a remainder interest) or the value of the fee simple interest in the underlying property, for the bona fide exception under I.R.C. § 2036(a)(1) to apply. *Id.* at 312. The court found that the decedent must receive full and adequate consideration for the property interest that she sold, not the underlying property. *Id.* at 315. The Third Circuit agreed with the *Gregory* court's statement that eligibility for the bona fide exception under I.R.C. § 2036 requires the transferor to receive "comparable value which would have been includable in the transferor's gross estate." *Id.* at 313 (quoting *Estate of Gregory*, 39 T.C. at 1016). The Third Circuit rejected *Gregory*'s application of that rule, however, insofar as the *Gregory* court took a snapshot of value at the time of the transferor's death, instead of at the time of the transfer. *Id.*

263. See *Magnin*, 184 F.3d at 1080 (defining "adequate and full consideration" in reference to the value of the remainder interest transferred); *Wheeler*, 116 F.3d at 767 (same); *D'Ambrosio*, 1010 F.3d at 318 (same).

It is unlikely that I.R.C. § 2038 would apply to a selling author who dies prior to the termination window. The author's rights are contingent upon surviving to the point at which the termination right may be exercised. This contingency precludes the application of I.R.C. § 2038. If the contingency were disregarded, this section may not apply because of the bona fide exception.²⁶⁴

As is true with the giving author who dies prior to the termination period, I.R.C. § 2041 should not apply to the selling author who dies before the termination period.²⁶⁵ The copyright termination right is not a general power of appointment because the condition precedent (i.e., survival) has not been satisfied.²⁶⁶

2. If the Selling Author Dies During Period of Termination

A selling author who dies during the period for exercise of the copyright termination interests should experience the same estate tax consequences as one who dies before the period of termination, with one qualification. Because there is no longer any outstanding contingency (the author survived to the point at which she could exercise the termination right), I.R.C. §§ 2038 and 2041 can now apply.

3. If the Selling Author Dies After Termination Window Closes

If the selling author survives the termination period without exercising her rights—the third scenario under consideration—then the termination rights evaporate.²⁶⁷ No value attributable to these rights should be includable in her gross estate under I.R.C. § 2033.²⁶⁸ Furthermore, there should be no inclusion under I.R.C. §§ 2036, 2037, or 2038.²⁶⁹ As in the case of the giving author who dies after the termination period, I.R.C. § 2041, standing alone, should not be sufficient to trigger estate tax inclusion either.²⁷⁰

264. *Supra* notes 256–62 and accompanying text.

265. *Supra* Part IV.B.1.

266. *Supra* Part IV.B.1.

267. *See* 17 U.S.C. § 304(c) (2006) (defining the extent of termination rights).

268. The remainder of Part IV.B considers alternate theories for estate tax inclusion.

269. As discussed earlier, the imposition of gift tax requires some showing of voluntariness. *See supra* Part III.B–C (discussing the gift taxation of transfers of copyright termination rights). Allowing the termination right to lapse should not cause I.R.C. § 2035 to apply, even if death occurs within three years of the lapse, inasmuch as the lapse occurs without any volitional act of transfer or relinquishment by the decedent at the time of the lapse. *See* I.R.S. Tech. Adv. Mem. 199935003 (May 18, 1999) (intimating that I.R.C. § 2035 cannot apply in the absence of a volitional act).

270. The lapse of the power might be a taxable gift under I.R.C. § 2514. *See* I.R.C.

Table B summarizes the estate tax consequences of the copyright transfers discussed in this Part.

Table B: Estate Tax Consequences of Copyright Transfers²⁷¹

<i>Will estate tax be imposed on . . .</i>	<u>Time of Author's Death</u> (in relation to period when notice of termination may be delivered)		
	<u>Before</u>	<u>During</u>	<u>After</u>
Hoarding Author	✕	✕	✕
Giving Author			
... under IRC § 2033?	★	★	★
... under IRC § 2036?	⊗	⊗	★
... under IRC § 2037?	⊗	⊗	★
... under IRC § 2038?	★	⊗	★
... under IRC § 2041?	★	★	★
Selling Author			
... under IRC § 2033?	✕	✕	★
... under IRC § 2036?	⊗	⊗	★
... under IRC § 2037?	⊗	⊗	★
... under IRC § 2038?	★	⊗	★
... under IRC § 2041?	★	⊗	★

Key:

- ✕ Estate tax imposed on some or entire value associated with copyright
- ⊗ Under some circumstances and if certain assumptions are correct, estate tax may be imposed on some or entire value associated with copyright. See analysis *infra*.
- ★ No estate tax consequences

§ 2514(e) (2006) (discussing the lapse of a power of appointment). Note that if the lapse occurs less than three years before the decedent's death, then the gift tax paid on the taxable lapse would be includable in the decedent's gross estate. *Id.* § 2035(b). On the other hand, a selling author, unlike a gifting author, may be able to argue that a lapse of termination does not create a taxable gift by reason of the ordinary-course-of-business exception in Treas. Reg. 25.2512-8.

271. Assuming all relevant notice requirements satisfied.

V. Policy Concerns with Sticky Copyrights

Because federal copyright law uniquely grants an author the ability to terminate a prior transfer, authors do not have the ability to fix the transfer tax value of the donated property.²⁷² Ordinarily, when a person makes a gift, the transfer tax value of the gifted property is its fair market value as of the date of the transfer.²⁷³ Because of the likelihood of the estate tax inclusion, however, the author has no ability to fix the value of a copyright for wealth transfer tax purposes at the time of the initial transfer.²⁷⁴ Although federal copyright law aims to protect the author and her family members,²⁷⁵ it actually limits an author's ability to engage in tax-effective giving. There is seemingly little rationale for this discrimination against copyrights relative to other types of property.

The underlying policy goal of copyright termination rights is protection for the author. Supporters of the revised federal copyright law explained that termination rights were necessary "because of the unequal bargaining position of authors, resulting in part from the impossibility of determining a work's value until it has been exploited. Section 203 reflects a practical compromise that will further the objectives of the copyright law while recognizing the problems and legitimate needs of all interests involved."²⁷⁶ Motivated by the desire to protect authors, Congress appears to have made it difficult, if not impossible, for authors to engage in effective estate planning. The solicitude of the legislature for creative individuals is salutary, but the unintended tax consequences are not.²⁷⁷

Most authors and their advisors already understand the ability to "bump" or disturb prior transfers with copyright termination rights,²⁷⁸ but the

272. On the benefits of fixation of value generally, see Gans, *supra* note 11, at 765–87 (discussing rate, appreciation, and leverage benefits).

273. See I.R.C. § 2512(a) ("[T]he value thereof at the date of the gift shall be considered the amount of the gift.").

274. See *supra* Part IV (discussing estate taxation of copyright interests).

275. See RESTATEMENT (THIRD) OF PROP.: WILLS AND OTHER DONATIVE TRANSFERS § 10.1 cmt. a (2003) (claiming the purpose of the law of donative transfers is to "facilitate rather than regulate").

276. H.R. REP. NO. 94-1476, at 124 (1976).

277. For a critique of the unintended consequences of state legislation that creates retroactive descendible rights of publicity, see Gans et al., *Postmortem Rights of Publicity: The Federal Estate Tax Consequences of New State-Law Property Rights*, *supra* note 229, and Gans et al., *The Estate Tax Fundamentals of Celebrity and Control*, *supra* note 229.

278. See, e.g., Nevins, *supra* note 19 (discussing the intersection of estates and copyright law in "will-bumping").

professional and scholarly literature is almost entirely silent on the wealth transfer tax consequences of these rights. To date, the Service has not sought to enforce any of the gift or estate tax consequences of sticky copyrights. This may be for a variety of reasons including, perhaps, the failure of the Service and taxpayers to appreciate all of the tax consequences.

If the wealth transfer tax consequences of copyright termination rights were better understood, vigorous markets in copyright transfers would be hindered by the tax system. For example, an author who apprehends that her estate will include some residual value of any copyright sale may be discouraged from making lifetime transfers. Enforcement of the wealth transfer tax system would lead to an inefficient hoarding of intellectual property, as creative individuals would seek to minimize their tax exposure. To the extent that an author makes a decision to exploit (or not to exploit) a copyright based on tax considerations, the law hinders rather than protects creative individuals. Freedom of testation and economic efficiency are then impeded by overly complex tax rules.

VI. Legislative Reform to Unstick Copyrights

Copyrights are not like other property, admittedly. But if termination rights created by statute—a statute meant to protect authors and their heirs—attract harsher transfer tax treatment than other assets, then the tax law should be changed. Authors, like owners of other kinds of property, should be able to gift or sell their assets without concern that termination rights will cause adverse tax consequences. Equally important, authors should be able to make lifetime gifts of their copyrights to their spouses without incurring gift tax, just as other property owners are permitted to do.

To remedy this inequality, Congress might consider the following possibilities: First, Congress should provide that a transfer of a copyright qualifies for the marital deduction, thereby eliminating the potential for gift tax on transfers to spouses. Second, Congress should provide that an author who gifts or sells a copyright is not subject to gift tax on the value of the termination right and that no inclusion in the gross estate occurs by reason of these rights. Third, Congress should adopt an early completion rule, under which the full value of the copyright (including the value of the termination rights) is subject to gift tax at the time of the initial gift, and no amount would be includable in the donor's estate on account of the termination rights.²⁷⁹ Fourth, the author

279. See, e.g., Mitchell M. Gans & Jay A. Soled, *Reforming the Gift Tax and Making it Enforceable*, 87 B.U. L. REV. 759, 789 n.117 (2007) (discussing the application of an early

should be given an election: either (1) treat the termination right conferred at the time of gift or sale as having been gifted, or (2) include the value of the right in the gross estate at the time of death. Any of these alternatives would bring welcome clarity to this area of the law. But to continue treating such authors as if termination rights were a valuable "string" requiring estate tax inclusion makes no sense.

VII. Conclusion

Federal copyright law shapes an artist's legacy, in both senses of the word. Through the ability to terminate prior transfers, an author and the author's heirs can revisit contracts that turn out to be unwise or imbalanced. Copyright termination rights, which are tantamount to a property law right of revocation, allow a creative individual a high degree of control over how others use her work. But with that right of revocation comes unintended tax consequences. Transfers during the author's lifetime, whether by gift or by sale, may have negative gift and estate tax consequences. This Article takes the position that federal copyright termination rights both protect authors and prevent them from engaging in effective estate planning. To harmonize the law of copyright and the law of donative transfers, the tax law should be revised to provide that termination rights do not provide adverse transfer tax outcomes. Only when the tax law is changed will the interests of copyright owners truly be served.

completion rule to transfers to grantor retained annuity trusts or qualified personal residence trusts).

