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What You Should Know About Estate and Gift Taxes, by J.K. Lasser

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WHAT YOU SHOULD KNOW ABOUT ESTATE AND GIFT TAXES. By J. K. Lasser.* New York: Henry Holt and Company, 1951. Pp. xi, 175. $2.95.

This distillate goes half circle in reconstructing the skeleton of the estate and gift tax law in readable non-technical language. The enthusiastic publisher puffs the offering as a "must" for lawyers wherein is "all the essential information required to understand every important aspect of the Federal Estate and Federal Gift Tax." The more modest Mr. Lasser states that he writes primarily for the layman—the taxpayer; he characterizes his effort as an attempt at the "perfect chip shot to the green." Mr. Lasser's statement is the more accurate. The author has neither evolved a universal panacea nor run the gamut of the full-blown omelet which is our estate and gift tax law. Certain inaccuracies and liberties are a by-product of this simplification. With the exception of stock valuation, this book is not addressed to the important issue of establishing values for the inventory of an estate. Concededly, the work is not a penetrating analysis. It is primarily a client's book to stimulate constructive thinking as to what the client should do with his property. But this little volume is not without interest to the lawyer.

The prolific Mr. Lasser is an accountant who has enjoyed wide circulation of his tax writing. His forte is simplification for the taxpayer of the complexities of contemporary tax law. In light of the friction in some jurisdictions between lawyers and accountants as to the professional qualifications for practice in tax matters, an observation seems appropriate on Mr. Lasser's conduct in the phase of the tax field most sacred to the lawyer. This is an area in which the lawyer, above all others, should be preeminently qualified. This reviewer, who has served in the camps of both professions, will not use

11. The converse of this suggestion that "simple location" may be a distorting feature of our traditional Western concepts, is developed by Professor Pool in his essay, where he suggests that current Soviet thinking has fallen into the "organismic fallacy," a fallacy of misplaced concreteness that is created when abstractions attend exclusively to "diffuse" as opposed to "simple" location. If the early Soviet conception of "capitalism" involved extreme over-emphasis on simple location, it is easy to see why in its antithesis an antithetic notion of place appears.

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this vehicle to labor the professional jurisdictional issue. Mr. Lasser readily concedes the role of the lawyer in achieving the objectives suggested in the estate planning chapters; however, the tools which aid the legal practitioner—sample clauses to assist the draftsman, Internal Revenue Code, Treasury Regulation and case citations, the effects of local law and probate practice—are all absent.

Financial transactions today do not escape the all inclusive effect of the swath cut by taxes. The lawyer engaging in general practice, of necessity, engages in tax practice. And tax practice is a game of constantly shifting ground rules; certainty is a relative thing. Because of the complexity and rapid changes of tax law, many consider the area to be one calling for specialization. But the problem may not be dismissed so readily. Every will draftsman must bear in mind that even death gives rise to a financial transaction which may leave the Federal Government as an unintended and substantial beneficiary. A lawyer in protecting the interest of his client is charged with the duty of minimizing taxes insofar as is consonant with the dispositive intent of the testator. For those who have been reluctant to undertake a study of the estate and gift tax law, the background acquired from this study will provide direction and quicker comprehension in a more detailed study of these laws and the tax saving possibilities thereunder; for the initiate, this volume will serve little purpose other than providing an outline to regain perspective of the over-all area.

Important changes have rewrought the estate tax since its inception on a permanent basis in 1916. The inflationary spiral of our economy and the increase in rates have added potency to the tax. In actuality, the estate tax is composed of the original "basic tax" plus the "additional tax" which was added in 1932. That year also ushered in the implementing gift tax. Purportedly to discourage states from offering the wealthy the inducement of spending their waning years under skies unclouded by state inheritance or estate taxes, Congress enacted, in 1926, an amendment which allowed a credit of up to 80 per cent of the basic tax for amounts paid as state inheritance or estate taxes. With this opportunity to offer a tax inducement gone, most of the states enacted inheritance and estate tax laws to take advantage of the federal credit.[1] Such is the means and power by which a federal estate tax policy can influence the estate and inheritance tax policies of the individual states. The relatively low rates of the basic tax when coupled with this background explain the minor federal fiscal, but major federal political, role of the basic tax. It is the additional tax which is the federal breadwinner. Apparently in the interest of simplification, the text and tables of the volume under review do not

1. Florida, along with a few other states, imposes an estate tax to the extent of the federal credit only.

refer to the component basic and additional taxes but only to the federal estate tax as a whole.

The Revenue Act of 1948, introducing the "marital deduction," shook the skeleton of the estate and gift tax law. In the case of inter vivos gifts made from spouse to spouse, a gift tax deduction is allowed to the extent of one half of the gift—that is, the deduction has the effect of cutting the gift in half. In the case of property passing from a decedent spouse to the surviving spouse, an estate tax deduction is allowed for the amount of property, terminable interests excluded, so passing to the extent of one half of the "adjusted gross estate." The marital deduction amendment was a far-reaching innovation. In its light, well drafted wills suddenly appeared as poorly drafted wills; it taxed the ingenuity of lawyers to achieve the full advantage of the marital deduction for the testator; it negated the hitherto tax advantage of the community property state at which the equalizing legislation of 1942 was directed. Further important amendments were added by the Revenue Act of 1950. Previously all inter vivos gifts made "in contemplation of death" were includable in the decedent's estate for estate tax purposes even though a gift tax, of a lesser amount, had been paid. "In contemplation of death" was, and is, a very nebulous test with the burden of proof being all important. Cases under the old section constitute a good share of all federal estate tax litigation. The language of the section prior to amendment provided: "Any transfer made by the decedent within two years prior to his death without consideration shall, unless shown to the contrary, be deemed to have been made in contemplation of death." The Commissioner did not content himself with merely those transfers within the two year presumption. From the broader language of Internal Revenue Code Section 811(c), the Commissioner acknowledged a mandate to challenge transfers made many years prior to death.[2] This would no longer be possible following the amendment of the section. Now, a conclusive presumption provides that transfers were not made in contemplation of death if made more than three years prior to death. But if the transfers were made within three years of death, the burden of proof is still on the taxpayer to establish life, as opposed to death, motives. Thus, since death's blow cannot be predicted, a farsighted lawyer or client who builds an affirmative record of motive at the time of a gift may save, if death follows within three years, an otherwise lost tax cause. Evidence of the transferor's good health might be included; the motive underlying the gift might be recited—for example, setting up children in business, rearranging financial affairs for security before embarking on a new business venture, etc. Further, gifts might advisedly be timed to coincide with birthdays, marriages, or anniver-

2. See *In re* Kroger's Estate, 145 F.2d 901 (6th cir. 1944) where the attack was on a prenuptial transaction made ten years prior to death.

saries. All these factors would be favorable evidence in establishing a life rather than a death motive.

The outer fringes of the estate tax constitute a pioneer area for the ingenious tax practitioner. On many issues in the estate tax field conclusive authority is not available. Legwork and a factual record may often be of more comfort than any authority found in the Code, Regulations, cases or standard authorities—especially when the question presented is one of valuation of the assets includable in the gross estate. Valuation of the stock of a closed corporation is a problem in point. Although the Commissioner sets forth a general guide[3] to which Mr. Lasser refers, the factors justifying variation or complete negation of this formula are many, *e.g.*, loss of the decedent to the business. Many cases involving valuation poignantly illustrate the cleavage between the value ascribed by the taxpayer and that contended for by the Commissioner.[4] In *Estate of Heppenstall,*[5] the taxpayer valued at $275 per share; the Commissioner contended for $1250 per share; the Tax Court ascribed $750 per share. Of course, many problems of valuation require the assistance of an expert appraiser. The valuation of property with underlying minerals may be a difficult matter. Case authority for the valuation of producing oil properties looks to the runs and to geological surveys of reserves. But in valuing an Indiana limestone quarry, the practitioner will find that there is no deep-rooted procedure or authority.

Even deductions for expenses of and claims against the estate, which will usually be crystallized by the local probate practice, present tax questions. For example, suppose a decedent died in November and left all his property to his wife who had a substantial independent income for the year. The estate and the wife file a joint return for the portion of the taxable year prior to death.[6] The tax due under the return is a joint and several liability.[7] All claims to which the estate is liable are allowable as deductions in computing the estate tax.[8] As there are no other beneficiaries under the will, there is no resistance in the probate court in deducting all of the joint income tax from the decedent's gross estate. The joint income tax is $40,000; the net estate is $1,000,000. By filing a joint, rather than a separate, return the federal estate tax "saving" is $13,000. But the Commissioner would probably resist such a deduction by the estate and seek to stem the tax saving. Would his stand be justified under the law? This appears to be an open question at this writing.

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3. 1919-21: A.R.M. 34, 2 CUM. BULL. 31 (1920).
4. See this reviewer's article, *SEC v. Commissioner,* 29 TAXES 828 (1951) wherein the commissioner's market value contentions are questioned in cases where the SEC holds that to deal in such markets is illegal.
5. 8 TC MEM. DEC. 136 (1949).
6. INT. REV. CODE § 51(b)(4).
7. INT. REV. CODE § 51(b)(1).
8. INT. REV. CODE § 812(b)(3).

In an earlier paragraph, reference was made to the will draftsman's problem in light of the marital deduction. The question is: What language should be employed to achieve the fullest tax benefit of the marital deduction—how does the testator leave one half of his "adjusted gross estate" to the surviving spouse? Myriad are the answers. If maximum life income plus the greatest possible tax free transfer of principal for the surviving spouse W is desired, the will would probably set up two trusts. Trust No. 1 would be for half the adjusted gross estate. Trust No. 2 would be for the other half, less all estate and inheritance taxes payable by reason of the decedent's death. W would have a life income from both trusts. As to Trust No. 1, W would have a testamentary general power of appointment so as not to disqualify the marital deduction because of terminable interest.[9] The corpus of Trust No. 2 would be payable over to named beneficiaries at the death of W.

In establishing trusts which would take full advantage of the marital deduction, the draftsman might look to the clause set out by Professor Casner:

> If my wife survives me, I give to my trustees hereinafter named and their successor or successors the following: An amount equal to the maximum estate tax marital deduction (allowable in determining the federal estate tax on my gross estate) diminished by the value for federal estate tax purposes of all other items in my said gross estate which qualify for said deduction and which pass or have passed to my wife under other provisions of this will or otherwise. In making the computations necessary to determine the amount of this gift, the final determinations in the federal estate tax proceedings shall control.[10]

Professor Leach, in the monumental *Perpetuities in a Nutshell*,[11] sets forth the "administrative contingency" cases in which the Rule against Perpetuities had been applied. Cases are cited where the rule (a strict one—not one of construction) had been invoked to negative will language which turned on the closing of the estate. If there is any possibility, regardless of how improbable, that the estate would not be closed within 21 years, it could not be said that a beneficiary's interest would vest within the time limit of the rule and hence it failed.

In the proffered example there are trusts the corpus of which is dependent upon a final tax determination; of course, claims and expenses allowable under the local law enter into the determination of the adjusted gross estate.[12] Without a definite corpus can we have a valid trust? Can it be certain that a final tax determination will be made within 21 years (there is no statute of limitations if fraud is found)? The possibilities are remote—but then, does the application of the rule require more? It is conjectural whether the courts would extend the rule to such marital deduction trusts. But thoughts of the

9. INT. REV. CODE § 812(e)(1)(b).

10. Casner, *Estate Planning—Marital Deduction Provisions of Trusts*, 64 HARV. L. REV. 582, 584 (1951).

11. 51 HARV. L. REV. 638 (1938).

12. INT. REV. CODE § 812 (b).

rule as ammunition in the hands of the wily will contestant should serve as a caveat to the draftsman. Tax objectives cannot be divorced from other legal sanctions.

Moving on from problems predominantly in the estate tax field, this reviewer feels that a few words might be in order on problems of estate planning. Mr. Lasser states that his is a tax book and not a book on estate planning. But of necessity there must be an overlap. A chapter is devoted to buy-sell agreements and their utilization as a means of insuring the continuation of the small business. In essence, these agreements provide for a prearranged sale of the business to associates, key employees, or family members. The sale is effective at death and serves the double purpose of placing the control in the desired successors and providing the estate of the decedent businessman with the funds necessary to meet taxes and other death expenses. Very often these buy-sell agreements are funded by partners or stockholders buying insurance policies on the lives of each other. These agreements have a further tax advantage in that they may peg the value of the stock of the business interest at the value set in the agreement, since the amount at which the estate is obligated to sell is the value to the estate. Mr. Lasser mentions this possibility of pegging the value; however, he does not mention the pitfall. In order for the pegged value to succeed for tax purposes, the provisions of the agreement must be such that the decedent did not have it within his power to make an inter vivos disposition of the stock free of the agreement.[13]

The estate planner might also consider the legal form by which husband and wife hold property. Mr. Lasser does not orient the reader in this area. In brief, if the decedent and another own property jointly, *i.e.,* either by joint tenancy or by tenancy by entireties, such property is includable in the estate of the decendent for tax purposes at the full value of the property with a reduction only to the extent to which the estate establishes that the surviving tenant contributed to the acquisition of the property. In Indiana a conveyance to husband and wife, unless stipulated to the contrary, creates a tenancy by entireties with the wife taking by right of survivorship upon the death of the husband. Assuming, as is probably the case, the husband paid the purchase price, the total value of the property would be includable in the decedent husband's taxable estate. But if the husband and wife hold the property as tenants in common, only one half of the value of the property would be includable in the husband's estate upon his death. As a tenancy by entireties has little to recommend it over a tenancy in common, estate planning with an eye to tax savings should explore this possibility. The tenancy by entireties might be dissolved by having the husband and wife convey to a strawman who would reconvey to husband and wife as tenants in common. But consider the ingenious approach to the problem revealed by *Estate of Sullivan v. Commis-*

13. Estate of Matthews v. Commissioner, 3 T.C. 525 (1944).

sioner.[14] There, a 77 year old husband shortly before death entered into a transaction whereby he released his right of survivorship in consideration for a reciprocal release by his wife; a tenancy in common resulted. The Commissioner assailed the transaction and sought to include the full value of the property in the decedent husband's estate. The court sustained the taxpayer and held that, as it was a valid tenancy in common under state law, only one half of the value of the property was includable in the husband's estate. The court went further and pointed out that there was good consideration for the reciprocal releases, that is, one for the other; in fact, the husband got the better of the bargain in that actuarially his right of survivorship was worth less than that of his younger wife. The Commissioner's contention that it was a gift in contemplation of death under Internal Revenue Code Section 811(c) failed in light of this theory of consideration which the court spelled out.

This reviewer injects a caveat on the use of Mr. Lasser's simplified and undocumented "chip shot." Local law might cast doubt upon the procedures suggested. For example, in writing of the type of gifts which would qualify for the marital deduction, a suggestion is made for an inter vivos trust with the wife having all the income for life and the unrestricted right to subsequently appoint the principal. The Texas widow of General Hinds[15] might feel that there was a better way of doing it. In that case the General had established an irrevocable inter vivos New York trust for his wife, such as Mr. Lasser recommends, and on the General's death the Commissioner said that the corpus of the trust should be included in the taxable estate of the decedent husband. The Commissioner's contention was that the trust income, which the wife received during the General's lifetime, was community income under the community property laws of Texas and hence the husband had not parted with all his interest in the property. Internal Revenue Code Section 811(c) was utilized in holding that the husband retained an interest. This was contended notwithstanding the express provision of the trust that the income was payable to the wife. The Commissioner prevailed; one half of the property was included in the husband's estate. Upon the petition of the Commissioner seeking the other half, the 5th Circuit affirmed, not because it approved the decision, but because the Commissioner had already received more than he was entitled to. And thus, though the holding is questionable, it is law on the books and its full implication remains conjectural. The tax adviser, who feels that the better view would reject such a holding, must consider the uncertainty and expense of litigation which his client would incur in establishing the better view. It is questionable whether a counsel should burden his client with such an imposition.

14. 175 F.2d 657 (9th Cir. 1949).

15. Commissioner v. Estate of Hinds, 11 T.C. 314 (1948), *aff'd,* 180 F.2d 930 (5th Cir. 1950).

This reviewer has not intended to deal harshly with Mr. Lasser. The purpose of extending the scope of this review beyond the coverage of the book is twofold: first, to inject a caution as to the interplay of local law; and second, to indicate that the many problems of estate and gift taxes cannot be adequately covered in an introductory work. In keeping with his avowed purpose, the author has handled the subject admirably. His contribution will aid the reader in more readily appreciating the problem and the background.

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