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Estate Tax Marital Deduction: Eligibility of a Bequest in Trust Providing for Monthly Payments to Widow (Northeastern Pennsylvania National Bank & Trust Company v. United States, 87 S.Ct. 1573, 1967)

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search and seizure. The right of privacy must yield at some point to the right of search[30] and only intelligent rulings by detached magistrates, mindful of established limitations, will insure the privacy guaranteed by the Fourth Amendment.

The "mere evidence" distinction was in may ways a troublesome one. In dealing with it courts often found it necessary to confine or enlarge its definition in a particular case. The ruling in the instant case provides a logical end for the rule and is not surprising in the light of recent court decisions.[31]

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ESTATE TAX MARITAL DEDUCTION: ELIGIBILITY OF A BEQUEST IN TRUST PROVIDING FOR MONTHLY PAYMENTS TO WIDOW. Decedent's will created a trust which gave his wife $300[1] a month from the trust income and a testamentary power of appointment over the entire corpus. Decedent's executor included the interest in determining the estate's marital deduction. The Commissioner ruled the interest did not qualify and assessed a deficiency in the estate tax. The executor paid the deficiency and sued for a refund. The district court entered summary judgment for the executor,[2] which was reversed by the circuit court of appeals.[3] On writ of review the United States Supreme Court affirmed the district court. *Held,* a bequest in trust which provides decedent's spouse with a monthly stipend and power to appoint the entire corpus qualifies for the estate tax marital deduction. *Northeastern Pennsylvania National Bank & Trust Company v. United States,* 87 S. Ct. 1573 (1967).

Since an estate tax is assessed upon property which passes at death,[4] community property states initially enjoyed a distinct advantage over common law states. Each spouse in a community property state had a vested interest in half the community estate, so only the decedent's portion was taxable at his death. As a factual matter, in common law states the husband had legal title to a majority of the property. If he predeceased his spouse this property might be taxed not only upon his death, but also upon the death of his wife.

[30] *Johnson v. United States, supra* note 19, at 14.
[31] *See supra* note 15.

[1] Because the martial deduction is computed as of the date of the decedent's death, Jackson v. United States, 376 U.S. 503, 508 (1964), the parties agreed that although the trust provided for increasing the wife's interest to $350 a month when her youngest daughter reached 18, this had no bearing on the amount of the marital deduction.

[2] Northeastern Pennsylvania Nat'l Bank & Trust Co., 235 F. Supp. 941 (D.C.Pa. 1964).

[3] Northeastern Pennsylvania Nat'l Bank & Trust Co., 363 F.2d 476 (3d Cir. 1966).

[4] INT. REV. CODE of 1954, § 2001.

Congress first attempted to equalize the estate tax burden by treating community property as property held in joint tenancy or tenancy by the entirety for estate tax purposes.[5] This only shifted the burden to the community property states,[6] so in 1948 Congress enacted legislation which attempted to treat common law estates as community property estates.[7] The estate tax was deferred until death on half the adjusted gross estate[8] which the surviving spouse inherited.[9] Since equalization of the tax burden was to be achieved by two-stage taxation and not by allowing tax free transfer of property, only interests taxable at the second spouse's death qualified for the deduction.[10] These were interests which resembled a fee.[11] The 1948 law allowed the marital deduction if a surviving spouse received a life interest in the *entire* trust and a power to appoint the corpus either to herself or to her estate.[12] Consequently, partial interests in trusts did not qualify for the deduction.[13]

In 1954 the deduction was extended to partial interests in trusts by allowing the deduction ". . . if his [the settlor's] surviving spouse is en-

[5]INT. REV. CODE of 1939, § 811 (*e*)(2), added by § 402(*b*), 1942 Act.

[6]"In one respect the 1942 Act taxed community property even more severely than jointly held property. In the case of a joint tenancy or a tenancy by the entirety, nothing is taxed upon the death of the tenant, who has contributed nothing to the joint estate. However, in the case of community property, if the spouse who had not contributed to the acquisition of the property died, the 1942 Act required any part of the community property over which the decedent had a power of testamentary disposition to be included in the taxable estate. As a practical matter this meant that if the spouse responsible for the accumulation of community property died, all of the community property would be taxed to his estate; while if the other spouse died first half the property would be taxed." LOWNDES AND KRAMER, FEDERAL ESTATE AND GIFT TAXES 372 (1956).

[7]INT. REV. CODE of 1939, § 812(*e*).

[8]"The adjusted gross estate is a concept introduced by the 1948 Act whose sole function is to furnish a ceiling for the marital deduction. Where community property is not involved, the adjusted gross estate is the gross estate less the deductions for expenses,, indebtedness, and taxes and losses enumerated in sections 2053 and 2054." LOWNDES AND KRAMER, *supra* note 6, at 374.

[9]The Act of 1948 did not absolutely disallow use of the marital deduction by spouses in community property states. What the Act did was bar any community property from being included in the decedent's adjusted gross estate.

[10]INT. REV. CODE of 1954, § 812 (*e*)(1)(*B*).

[11]In community property states the rule excluding one-half of the community property from taxation is based on the notion that the surviving spouse owns one-half of such property. Such one-half interest is generally an absolute fee simple interest. The statute allowing the marital deduction is based on the premise that the survivor ought to have something similar to a fee simple in order to maintain an estate tax equilibrium between states using the differing systems of property law. To permit a life interest to qualify for the deduction would result in a loss of taxation on the remainder since it is already vested and therefore would not pass through the surviving spouse's estate.

[12]INT. REV. CODE of 1939, § 812(1)(*F*). This power of appointment made the life interest taxable at the surviving spouse's death.

[13]Estate of Sweet v. Comm'r, 234 F.2d 401 (10th Cir. 1956) (power to appoint one-half of the value of the adjusted gross estate); Estate of Hoffenberg v. Comm'r, 22 T.C. 1185 (1954) (power to appoint two-thirds of the corpus and accumulated income); Estate of Shedd v. Comm'r, 23 T.C. 41 (1954) (right to two-thirds of the income and power to appoint one-half of the corpus); Estate of Bickers v. Comm'r, Tax Ct. Mem. 1958-68 (power to invade corpus to the extent of $15,000). To ease the burden of this provision, courts in isolated instances interpreted the decedent's will as creating separate trusts for each beneficiary instead of a common trust for all of them. Estate of Barry v. Comm'r, Tax Ct. Mem. 1956-97.

titled for life to all the income from the entire interest, or all the income from a *specific portion* thereof . . . with power in the surviving spouse to appoint the entire interest, or such *specific portion* . . ."[14] (emphasis added.)

Instead of settling the law, however, the 1954 amendment only created a new controversy, this time centering around the meaning of the words "specific portion."

The House and Senate reports concerning the 1954 amendment contained examples which described as a fraction the interest qualifying as a "specific portion."[15] The Treasury Department interpreted this to mean that a fractional description was necessary to create a "specific portion" and included this interpretation in a treasury regulation.[16] The theory of the regulation was two-fold. First, only a fractional description could absorb the appreciation in value of the corpus, thus avoiding any tax free transfer of capital appreciation.[17] Second, only a fractional description would place on the beneficiary the risk of depreciation in value, a risk which is shared by spouses in community property states.[18]

Three federal courts disagreed with the Treasury Department.[19] These courts allowed partial interests to qualify for the deduction even

[14]INT. REV. CODE of 1954, § 2056(*b*)(5). The Technical Amendments Act of 1958, 72 Stat. 1606 (1958), applied the 1954 amendment retroactively to estates of decedents dying after April 1, 1948, and before August 17, 1954. Concerning the Technical Amendments Act the Court said, "Plainly such a provision should not be construed so as to impose unwarranted restrictions upon the availability of the deduction." *Instant case* at 1578.

[15]H.R.Rep. No. 1337, 83d Cong. 2d Sess. (1954) as set out in U.S. CODE CONG. & ADMIN. NEWS 4461-4462 (1954); S.Rep. No. 1622 83d Cong. 2d Sess. (1954) as set out in U.S. CODE CONG. & ADMIN. NEWS 5118-5119 (1954).

[16]"A partial interest in property is not treated as a specific portion of the entire interest unless the rights of the surviving spouse in income and as to power [of appointment] constitute a fractional or percentile share of a property interest so that such interest or share in the surviving spouse reflects its proportionale share of the increment or decline in the whole of the property interest to which the income rights relate." Treas. Reg. § 20.2056(*b*)-5(*c*) (1954). Administrative regulations are either legislative or interpretative. Most of the Treasury Regulations are of the latter type and may or may not carry the force of law. "This Court has long given considerable and in some cases decisive weight to Treasury decisions and to interpretative regulations of the Treasury and other bodies that were not of adversary origin. We consider that the rulings, interpretations and opinions of the Administrator under this Act, while not controlling upon the courts by reason of their authority, do constitute a body of experience and informed judgment to which courts and litigants may properly resort for guidance. The weight of such a judgment in a particular case will depend upon the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors giving it power to persuade, if lacking power to control." Skidmore v. Swift, 323 U.S. 134 (1944); 1 DAVIS, ADMINISTRATIVE LAW TREATISE 298-306 (1958).

[17]A simple example is the instance where the testator creates a trust of 400 shares of stock, his wife to receive the income from and power of appointment over 200 of such shares. In the event of a stock split the trust corpus would consist of 800 shares. The resulting 200 share increase in her interest would become part of the corpus which had already been taxed, thus freeing the capital appreciation from taxation at her death.

[18]If the surviving spouse receives the right to $300 a month from a trust's income she is guaranteed this income though it might take the entire corpus to produce it if the capital should depreciate.

[19]Gelb v. Comm'r, 298 F.2d 544 (2d Cir. 1962); Allen v. United States, 250 F. Supp.

though the ratio of the partial interest to the total corpus was not expressed in a fractional form. They reasoned that the treasury regulation was an overly strict interpretation which would frustrate the purpose of the 1954 amendment which was to broaden the application of the marital deduction allowance.[20]

In the first of these cases, *Gelb v. Commissioner*,[21] a widow was provided with all the trust income and power to appoint the corpus, except a portion sufficient to supply her minor daughter with $5,000 a year. The Second Circuit Court refused to apply the treasury regulation and allowed the deduction although the non-fractional description of the power of appointment would permit her to appoint any capital appreciation of her daughter's portion. The court said:

> Congress spoke of a "specific portion," not a fractonal or percentile share, and nowhere indicated any policy that deductibility of a "specific portion" should be governed by the possibility that the spouse's portion will change in value relatively more or less than the clearly nonqualifying part. . . . A basic purpose of the marital deduction was to reduce the discrimination against taxpayers not in community property states. The liberalization in the provision as to trusts, made in the 1954 Code and applied to earlier years by the Technical Amendments Act, was evidently designed to permit certain normal testamentary dispositions without the total forfeiture of the deduction that the 1939 Code had occasioned in some instances.[22]

In the second case, *Allen v. United States*,[23] the widow was given a right to all the income and the power to withdraw $5,000 a year from the corpus. Though depreciation or appreciation in value of the corpus would vary the portion the widow could invade in relation to the total corpus, the court still permitted the deduction. The court did not feel it was "necessary to examine further the legislative history where the statute itself is not ambiguous."[24]

In *Citizens National Bank of Evansville v. United States*[25] an interest composed of income of $200 a month and a general testamentary power of appointment over the entire corpus qualified for the deduction. The deduction was allowed although the widow's income interest would be insulated from depreciation. The court relied upon *Gelb* and *Allen*.[26]

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155 (E.D.Mo. 1965); Citizens Nat'l Bank of Evansville v. United States, 359 F.2d 817 (7th Cir. 1966).

[20] *Gelb v. Comm'r*, *supra* note 21, at 551.

[21] *Gelb v. Comm'r*, *supra* note 21.

[22] *Gelb v. Comm'r*, *supra* note 21, at 551.

[23] *Allen v. United States*, *supra* note 21.

[24] *Id* at 157.

[25] *Citizens Nat'l Bank of Evansville v. United States*, *supra* note 21.

[26] *Id.* at 820, 821. The seventh circuit court also relied upon the reasoning of the district court in the instant case, which had not yet been reversed by the third circuit court. *Id.* at 821. One of the reasons the Supreme Court granted certiorari was the discrepancy between the third circuit court's disallowance of the deduction and the *Citizens Nat'l Bank of Evansville* case in which the seventh circuit court allowed the deduction. *Instant case* at 1575-1576.

Allen and *Citizens National Bank of Evansville* did not expand the reasoning of *Gelb*. They simply applied the *Gelb* rationale to different facts. All three cases involved a non-fractional description of the "specific portion" the spouse was to receive. In *Gelb* the description related to the portion of the trust which the widow could not appoint, while in *Allen* it concerned the amount the widow could appoint. *Citizens National Bank of Evansville* concerned a stipulated income provision. Thus, the three cases established the rule that a "specific portion" of the income or power of appointment could be described in non-fractional form although such a description would permit any capital appreciation to escape taxation, or insulate the beneficiary from any depreciation in the value of the principal.

Although the Third Circuit Court in the instant case disallowed the deduction, it recognized that the fractional form requirement of the treasury regulation had not been accepted in prior decisions.[27] The circuit court distinguished the instant case on the basis that actuarial computation was not feasible.[28] There were no constant investment factors from which the maximum income of the corpus could be determined.[29]

The Supreme Court, in reversing the Third Circuit Court, held that actuarial computation was feasible and developed a theory of "feasibility of computation" which would allow deduction of interests that do not contain a constant investment factor. After discussing the history of the deduction the Court determined that Congress intended a "liberal 'estate-splitting' possibility to married couples."[30] They then concluded that the Third Circuit's decision was an overly strict interpretation of the marital deduction:

> To be sure, perfect prediction of realistic future rates of return is not possible. However, the use of projected rates of return in the administration of the federal tax laws is hardly an innovation. It should not be a difficult matter to settle on a rate of return available to a trustee under reasonable investment conditions, which could be used to compute the "specific portion" of the corpus whose income is equal to the monthly stipend provided for in the trust. As the Court of Appeals for the Second Circuit observed in Gelb, "The use of actuarial tables for dealing with estate tax problems has been so widespread and of such long standing that we cannot assume Congress would have balked at it here; the United States is in business with enough different taxpayers so that the law of averages has ample opportunity to work."[31]

[27] "Suffice it to say, even assuming its [the treasury regulation] invalidity we have been unable to conceive of a method to compute the 'specific portion' of the trust corpus to which the surviving spouse is entitled to all the income for her life." *Northeastern Pennsylvania Nat'l Bank, supra* note 3, at 484.

[28] "Feasible computation of a specific portion is the key to martial deduction statutes." *Id.* at 483.

[29] "Thus, in this case, the factual constants do not exist upon which the maximum income can be theoretically computed, as it was possible to theoretically compute the maximum of corpus in *Gelb*. In short, the ratio between the maximum monthly income and the monthly stipend — the fraction of the entire corpus which could be the specific portion for martial deduction purposes — may not acceptably be computed." *Id.* at 484.

[30] *Instant case* at 1578.

[31] *Instant case* at 1579.

The basic policy of the marital deduction will be fulfilled by allowing the deduction in these instances. Otherwise, an interest may be taxed twice although it seems to be "fairly within the language and underlying policy" of the statute.[32] The liberality of the Court in construing "specific portion" offends the traditional policy of construing tax deduction statutes against the taxpayer,[33] but this rule of construction is not absolute.[34] The Supreme Court's ruling should have obviated the necessity for further legislation to interpret the present Act. Ironically, the dissent in *Citizens National Bank of Evansville* may best have described the ambit of "specific portion"—" . . . something judicially rationalized as approximately equivalent . . ."[35]

THOMAS A. HARNEY.

HUSBAND AND WIFE: HUSBAND'S CONTRIBUTORY NEGLIGENCE AS A BAR TO WIFE'S ACTION FOR LOSS OF CONSORTIUM. Gene Hall was seriously injured by reason of the negligence of the United States, but was denied recovery because of his own contributory negligence. His wife, Josephine Hall, was denied recovery for loss of consortium. Josephine Hall then moved for a new trial or in the alternative to amend the findings and conclusions entered to permit her to recover for loss of consortium. *Held,* that under Montana law, a husband's contributory negligence bars a wife's recovery from a negligent third party for loss of consortium. *Hall v. United States,* 266 F. Supp. 671 (D. Mont. 1967).

The term "consortium" has been variously defined by different courts and not one definition would be acceptable in all jurisdictions.[1] Under

[32]*Gelb v. Comm'r, supra* note 21, at 551.

[33]The dissent in the instant case lamented the interpretation of a tightly worded tax statute as if it were a workmens compensation act. *Instant case* at 1682. Traditionally, courts have construed tax deduction statutes against taxpayers. Empire *Trust Co. v. United States,* 226 F. Supp. 623, 626 (S.D.N.Y. 1960); Stapf *v. United States,* 189 F. Supp. 830 (N.D. Tex. 1960); Empire *Trust Co. v. Comm'r,* 94 F.2d 307 4th Cir. 1938); *Jackson v. United States, supra* note 1, at 510.

[34]"'And in denying the deduction, the courts have been less concerned with the underlying philosophy of the martial deduction than they have been with maintaining the so-called legislative principle that 'deductions should be strictly construed against the taxpayer and in favor of the sovereign.' This attitude, too, has played its part in subverting the original purpose of Congress of equalization between the different property systems . . . . If we consider these cases and the judicial attitude they reflect from the viewpoint of equalization, we see that the represent a frustration of that objective.'' Paul E. Anderson, *Marital Deduction and Equalization Under the Federal Estate and Gift Taxes Between Common Law and Community Property States.* 54 MICH. L. REV. 1087, 1111 (1956).

[35]*Citizens Nat'l Bank of Evansville v. United States, supra* note 21, at 822.

[1]Technically, ''consortium'' is an element of damage rather than an action. The expression has long been used by the courts, however, to denote those actions in which injury to consortium is the major element of damage. The following definition is typical of most: ''Conjugal fellowship of husband and wife, and the right of each to the company, cooperation, affection, and aid of the other in every conjugal relation.'' BLACK'S LAW DICTIONARY (4th ed. 1951).