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Taxation - Federal Income Tax - Right of Donee to Deduct Expense of Contesting Gift Tax Asserted Against Donor

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TAXATION—FEDERAL INCOME TAX—RIGHT OF DONEE TO DEDUCT EXPENSE OF CONTESTING GIFT TAX ASSERTED AGAINST DONOR—In 1948 taxpayer's mother gave him 410 shares of stock in the family enterprise. She filed a gift tax return, but the government, in auditing it, disagreed with her valuation of the stock. Donor had no desire to contest the government's valuation, but since his mother and father still held substantial stock in the business which would eventually go to him, donee desired a lower valuation for estate tax evidentiary purposes. Allegedly fearing personal liability for any deficiency assessed against his mother as well as a lien against the corpus of the gift for any unpaid tax, he decided to contest the government's determination. He hired a lawyer, but the contest was conducted in his mother's name in accordance with Treasury rules. The lawyer served from 1952 to 1954 when the case was settled and a compromise deficiency was assessed against and paid by donor. Taxpayer paid the lawyer's fee and took it as an income tax deduction in 1954. The government disallowed the deduction contending that (1) the fee was the legal liability of the mother and (2) no gift tax liability was ever asserted against taxpayer. *Held,* taxpayer may deduct the expenses of contest. He was liable for the attorney's fee and the fact that a lien attached to the gift and that he as donee would be personally liable for any deficiency up to the amount of the gift indicates that he was no mere volunteer in contesting the valuation. *Bonnyman v. United States,* (D.C. Tenn. 1957) 156 F. Supp. 625.

If the gift tax, initially asserted against donor,[1] remained unpaid at the time it was due, donee became personally liable for it.[2] Section 212(3) of the 1954 code, however, permits a deduction only for expenses incurred

[1] I.R.C. (1939), §1008.
[2] I.R.C. (1939), §1009.

"in connection with the determination, collection, or refund of any *tax*," (emphasis supplied) not for expenses incurred in connection with any *liability*. Moreover, the decisions indicate that the tax must have been asserted against the taxpayer, viz., the donee son, rather than against some other person, viz., the donor mother.[3] Whether the donee's liability was a tax[4] would therefore seem critical. Although courts have held that this liability was a separate tax on donee,[5] several factors indicate that these holdings may not be correct and that donee is merely an insurer, assuring that donor's tax will be paid.[6] The "tax" would appear to be assessed against donee at donor's, not donee's, rate on the graduated cumulative scale.[7] Moreover, donee is liable for all of donor's gift taxes for that year up to the value of the gift, not just the tax on his particular gift.[8] The legislative history of section 6901, similar in purpose to section 1009 of the 1939 code, would indicate that the gift assets constituted a trust fund to assure the government's collection of donor's tax.[9] Of course, the word tax in section 212(3) may not be limited to taxes in the ordinary sense and may encompass the personal liability in this case.[10] Although the court did not discuss this issue, it would seem necessary to decide it before any deduction is allowed.

The controversy in the principal case centered upon whether the donee's liability, prior to its actual assertion by the government, was

3 See Deputy v. DuPont, 308 U.S. 488 (1940); Jacob M. Kaplan, 21 T.C. 134 (1953), acq. 1954-1 Cum. Bul. 5. These cases indicate that the words "determination . . . of any tax" in I.R.C. (1954), §212(3) mean a tax imposed on the taxpayer claiming the deduction.

4 "An enforced contribution of money . . . assessed in accordance with some reasonable rule of apportionment by authority of a sovereign state on persons or property within its jurisdiction." BALLANTINE, LAW DICTIONARY, 2d ed., p. 1263 (1948).

5 Mississippi Valley Trust Co. v. Commissioner, (8th Cir. 1945) 147 F. (2d) 186; Fidelity Union Trust Co. v. Anthony, 13 N.J. Super. 596, 81 A. (2d) 191 (1951). In the latter case it was held that the donee, having paid the tax, could not recover back from the donor's estate. See also Moore v. Commissioner, (2d Cir. 1945) 146 F. (2d) 824. But see Fletcher Trust Co. v. Commissioner, (7th Cir. 1944) 141 F. (2d) 36.

6 E.g., Baur v. Commissioner, (3d Cir. 1944) 145 F. (2d) 338 at 339: "The words of the provision [§510 of the Revenue Act of 1932] [clearly] . . . render a donee personally liable (to the extent of the value of his gift) for the gift tax due by the donor regardless of the fact that the gift to the particular donee did not contribute to the imposition of any tax."

7 I.R.C. (1939), §1009; Baur v. Commissioner, note 6 supra.

8 I.R.C. (1939), §1009.

9 H. Rep. 356, 69th Cong., 1st sess., p. 43 (1926): "By reason of the trust fund doctrine and various state statutory provisions the transferee of assets of an insolvent transferor is ordinarily liable for the accrued and unpaid taxes of the transferor." The context indicates that the principle extended beyond cases of insolvency and the amendment in question purported not to change "the extent of such liability of the transferee. . . ."

10 See Treas. Reg. §1.212-1(*l*) (1957). "Expenses paid or incurred by an individual in connection with the determination, collection, or refund of any tax . . . are deductible." H. Rep. 1337, 83d Cong., 2d sess., p. 29 (1954). This contention would seem to be contra to the DuPont doctrine in construing "any tax" as covering both donee's and donor's tax.

sufficiently proximate to allow the donee to say he was contesting his tax liability rather than donor's. The court held that the donee was not a volunteer, basing its decision on the lien which attached as well as personal liability for donor's tax.[11] It is reasonably clear, however, that expenses incurred in determining the extent of or attempting to remove a lien are not deductible, though they could probably be capitalized into the cost of the property.[12] Absent the lien as a basis for the decision, it seems doubtful whether the mere unasserted personal liability, even if denominated a tax when and if finally asserted, would be sufficient to constitute a tax and allow the donee in this instance to be other than a volunteer, especially in light of his rights after its assertion by the government.[13] At most, then, it would seem that the expenses could be capitalized, and allowing the deduction is questionable.

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[11] I.R.C. (1939), §1009.

[12] Treas. Reg. §1.212-1(k) (1957); Garrett v. Crenshaw, (4th Cir. 1952) 196 F. (2d) 185.

[13] Since he filed no return, taxpayer could pay the tax, claim a refund and then contest the assessment within two years of the date of payment. I.R.C. (1939), §1027(b)(1). He, alternatively, might have filed a petition with the Tax Court for redetermination of the deficiency within 90 days of receipt of the notice of deficiency. I.R.C. (1939), §1012(a). With these rights available when the tax was finally asserted against himself, it is arguable that taxpayer was a volunteer by prematurely contesting the tax when asserted against the donor.