Florida Law Review

Volume 3 | Issue 1 Article 4

March 1950

New Florida Apportionment of Estate Taxes

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NEW FLORIDA APPORTIONMENT OF ESTATE TAXES

Florida Laws 1949, c. 25435

Chapter 25435, enacted by the Florida Legislature in 1949, provides that, unless the decedent has specifically directed otherwise, the state and federal estate taxes are to be apportioned among all persons interested in the estate, in the same ratios that their respective interests bear to the total taxable estate.

I. General Background

This statute is drawn against a background in which death taxes are playing an increasingly greater part in raising revenue for state and federal purposes, as well as in effectuating the present federal policy of discouraging large accumulations of wealth by making it impossible to pass on substantial amounts when one dies.[1] There are two forms of death taxes: inheritance taxes and estate taxes. The former are levied against the privilege of receiving property, whereas the latter are exacted for the privilege of transmitting it.[2] Since New York has an estate tax, the incidence of which is the privilege of transmission, it has held its apportionment statute inapplicable to the estate of a deceased domiciled elsewhere; when he dies leaving property in New York, the law of his domicile governs the apportionment, if any, and in the absence of such law there is no apportionment.[3] Inasmuch as neither the Federal Government nor the State of Florida has an inheritance tax, the apportionment statute pertains to estate taxes only.

Prior to the enactment of our new act, Florida and the decided weight of American authority agreed that when the intent of the deceased, including a testator, was not clearly set out the residuary estate bore the entire estate tax,[4] although the testator could by suit-

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[1]*See, e.g.*, Bross v. Bross, 123 Fla. 758, 769, 167 So. 669, 673 (1936).

[2]Griswold, Cases and Materials on Federal Taxation 115 (2d ed. 1946).

[3]*In re* Bernie's Estate, 74 N. Y. S.2d 887 (Surr. Ct. 1947).

[4]Y. M. C. A. of Columbus v. Davis, 264 U. S. 47 (1924); *In re* Bernay's Estate, 150 Fla. 414, 7 So.2d 444 (1942).

able designation indicate which portion of his estate was to bear it.[5] Often this ruling caused the testator to leave the least to those he loved most, particularly in those instances in which he had miscalculated the probable size of his estate or of the taxes to be borne, or was not aware that the residuary estate would have to bear the entire tax. Obviously, if the maxim that every man is presumed to know the law is pursued to its blind ultimate, it follows that the testator lets the burden of the tax fall where he knows it will; but the disparity between this theoretical maxim and practical reality has caused several states to alter their law so as to place on each person receiving benefits from an estate his portion of the tax burden, unless the testator specifies otherwise.[6]

The federal courts have consistently exhibited a willingness to follow the law of the state in question as regards assignment of the burden of both state and federal estate taxes, so long as the Federal Government receives its revenue. The Florida Supreme Court accurately summarized the federal position, with ample citations,[7] in *Henderson v. Usher*:[8]

> "The federal government is not concerned with who shall ultimately bear the burden of paying the estate taxes, but is concerned only with collecting the tax, leaving it to the states to fix the time, and principle, or method of determining who shall assume the burden of paying the tax."

In 1924 the Florida Constitution was amended so as to forbid levy by this state of estate, inheritance, or income taxes against its residents.[9] Two years later Congress passed a statute allowing a credit of up to eighty percent of the basic federal estate tax for any state

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[5]Y. M. C. A. of Columbus v. Davis, 264 U. S. 47 (1924).

[6]*E.g.*, N. Y. DEC. EST. LAW §124 (1930); PA. STAT., tit. 20, §844 (1937); MD. ANN. CODE GEN. LAWS Art. 81, §126 (Cum. Supp. 1947); R. I. GEN. LAWS, c. 43, §33 (1938); ARK. ANN. STAT. §63-150 (1947); MASS. ANN. LAWS Art. 65A, §5 (Cum. Supp. 1948); N. H. Laws 1943, c. 175; CONN. GEN. STAT. §2076 (Supp. 1949).

[7]*E.g.*, Y. M. C. A. of Columbus v. Davis, 264 U. S. 47 (1924); Edwards v. Slocum, 287 Fed. 651 (C. C. A. 6th 1923), *aff'd.*, 264 U. S. 61 (1924); Hill v. Grissom, 299 Fed. 641 (D. D. C. 1924).

[8]125 Fla. 709, 731, 170 So. 846, 854 (1936).

[9]FLA. CONST. Art. 9, §11.

estate tax paid.[10] As a result of this enactment, Florida in 1930 further amended its Constitution so as to take advantage of this deduction by permitting the levy of an estate tax up to eighty percent of the basic federal tax.[11] At this time, lacking an apportionment statute, Florida by court decisions followed the weight of American authority and placed the entire burden of estate taxes on the residuary estate whenever the testator had expressed no contrary instructions.

In 1949, however, our Legislature recognized the problem previously faced by other states and enacted its apportionment statute.[12] The gist of this, which appears in the first two sections, follows the corresponding statute of New York,[13] although Sections 3, 4 and 5 are not taken therefrom. Nevertheless, this near-duplication renders the New York cases construing that statute of great value in interpreting the Florida enactment.

It might be added parenthetically, as regards the widow, that, since Florida has held dower subject to estate and inheritance taxes whenever she elects against the will, the apportionment statute should lessen her taxes somewhat by virtue of the allocation to the legatees of shares of the total burden formerly borne in its entirety by her dower and the residuary estate.[14]

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[10]44 STAT. 70 (1926), as amended, 26 U. S. C. §813(b) (1946). There are today two federal estate taxes: the basic tax and the larger additional tax. The credit is allowed against the basic tax only and applies to the tax itself rather than merely to the taxable base.

[11]FLA. CONST. Art. 9, §11; FLA. STAT., c. 198 (1949).

[12]Fla. Laws 1949, c. 25435, FLA. STAT. §734.041 (1949). Sec. 1 of c. 25435 provides that state and federal death taxes shall be proportionally prorated by the county judge among those persons interested in the taxable estate unless the testator directs otherwise. Sec. 2 directs him to order any person in possession of some part of the gross estate to pay a pro rata share of the tax. Sec. 3 bars recovery of taxes from insurance companies on policies issued either on the life of the decedent or in which he owned any interest at his death. Sec. 4 applies the statute to estates of all persons dying after Jan. 1, 1948, as well as to all payment of estate or death taxes made or required to be made after June 13, 1949. Sec. 5 directs severability of the statute as regards any portions invalidated. Sec. 6 sets the effective date at the time the act becomes a law. It became a law without approval of the governor on June 13, 1949.

[13]N. Y. DEC. EST. LAW §124.

[14]FLA. STAT. §731.34 (1949); *In re* McMillan's Estate, 158 Fla. 898, 30 So. 2d 354 (1947); Horney v. Rhea, 152 Fla. 817, 12 So.2d 302 (1943); Murphy v. Murphy, 125 Fla. 855, 170 So. 856 (1936); Henderson v. Usher, 125 Fla. 709, 170 So. 846 (1936); as regards dower generally see Legis., 2 U. OF FLA. L. REV. 118 (1949).

II. Sections 1 and 2: Apportionment and Collection

1. Equitable Proration

Both the New York and Florida statutes direct that the taxes be "equitably prorated." At first glance this may appear to be an anomaly or even a contradiction in terms, but closer examination reveals that such is not the case. By the coupling of these terms the Legislature has taken cognizance of the multitude of varying situations that will be presented by future wills, and has attempted to lay down a somewhat elastic standard for meeting these situations.

The legislative mandate now prescribes proration of the taxes, that is, apportionment among the beneficiaries on the basis of their respective mathematically calculated shares of the taxable estate. But what is to enter into each type of estate, on the one hand, in determining the total from which the actual dollar amount of each share is reckoned; and, on the other hand, what deductions, directly related to taxes, are to be credited against the whole estate? At this point the legislative body has ceased definite formulation; instead it has left this function to the judiciary, with the solitary guide-post that the results must be "equitable." Case law must follow; it has already appeared in New York and other states, and undoubtedly it will develop in Florida also. For example, who should receive the benefit of discount for early payment; who should be saddled with the difference between estate and gift taxes when an attempted inter vivos transfer later fails taxwise as a gift; or who should meet the penalty for late payment, and under what circumstances?

The New York courts have held that, instead of being prorated among the general legatees subject to the tax, the entire discount for early payment accrues to the benefit of the residuary legatee on the theory that the residuary estate would have been entitled to income earned during the administration period on the sum prepaid if the payment had been delayed until the tax became due.[15] Similarly, when an inter vivos transfer is included in the gross estate, because made in contemplation of death, and a gift tax has previously been

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[15] *E.g., In re* Murdoch's Estate, 142 Misc. 186, 254 N. Y. Supp. 154 (Surr. Ct. 1931). There is as yet no discount for early payment of Florida estate taxes.

paid on the transfer, the estate tax is charged on a pro rata basis against all beneficiaries of the estate rather than solely against the donees of the inter vivos gift, and the gift tax already paid is ratably credited in the same manner as an offset.[16] Although several cases state that penalties and interest for late payment of taxes are considered part of the tax and are apportionable among the various beneficiaries,[17] an exception is made when the person causing the delay can be determined; in such event the penalties and interest are allocated entirely to him.[18]

All this is not to say, of course, that rules do not actually come into existence. Bases of proration, once judicially established, bind the courts in future factual situations falling into the determined categories. If these bases prove unsatisfactory, then legislative action is in order; but by such time the problem involved can be clearly recognized, and accordingly the appropriate legislative change can intelligently be made by statute. Meanwhile stare decisis applies, and rules of law are gradually built up by the judiciary. As the highest court of New York delineated this process in the traditional manner In re *Del Drago's Estate*:[19]

> "Whether it is just and equitable in all cases to impose the tax upon the estate as a whole and not upon the specific legatees on the benefits they derive from the estate is a matter admitting of wide diversity of opinion. It is not the province of the courts to resolve that conflict. 'The Congress has spoken and it is our function to interpret, not to legislate'."[20]

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[16]*In re* Blumenthal's Estate, 182 Misc. 137, 46 N. Y. S.2d 688 (Surr. Ct. 1943), *aff'd*, 293 N. Y. 707, 56 N. E.2d 588 (1944).

[17]Chase Nat. Bank v. Mackenzie, 192 Misc. 172, 76 N. Y. S.2d 19 (Sup. Ct. 1947); *In re* Clark's Estate, 169 Misc. 202, 7 N. Y. S.2d 176 (Surr. Ct. 1938).

[18]*In re* Ryle's Estate, 170 Misc. 450, 10 N. Y. S.2d 597 (Surr. Ct. 1939).

[19]287 N. Y. 61, 78, 79, 38 N. E.2d 131, 139, 140 (1941), *rev'd on other grounds*, 317 U. S. 95 (1942).

[20]The quotation within the quotation is from Matter of Hamlin, 226 N. Y. 407, 420, 124 N. E. 4, 8 (1919). See also *In re* Mollenhauer's Will, 257 App. Div. 296, 13 N. Y. S.2d 619, 622 (2d Dep't 1939): "The determination of the tax apportionment by a definite formula has been made by the Legislature and its action in this respect is final . . . and amelioration thereof is a legislative and not a judicial matter."

2. *Intent of Testator*

The Florida statute is not applicable when the testator has clearly indicated his wish as to where the burden of the tax is to fall;[21] but it is well to observe that the New York courts, in construing their similar statute, have consistently placed the onus of establishing non-apportionment on those seeking it.[22] They have insisted that the statute applies unless the language of the testator is clear and unambiguous, and have even gone so far as to refuse the legatee a preference in the apportionment of estate taxes when this is claimd solely on the basis of testamentary directions that certain benefits under the will be granted a priority in payment.[23] Indeed, inter vivos transfers later included in the gross estate as made in contemplation of death have been ratably taxed along with the residuary estate, notwithstanding specific directions in the will that the estate taxes be paid out of the latter.[24]

Perhaps the overall effect of the New York statute can be most clearly expressed by saying that a strong presumption in favor of apportionment now obtains, and that this presumption can be rebutted by nothing short of clear and unambiguous proof of an intent on the part of the testator to prescribe non-apportionment. Even then, the principle of non-apportionment will be extended no further than the words of the testator render its application mandatory.

III. Section 3: Exemption of Insurance Companies from Liability

The Florida Legislature, apparently having taken cognizance of the New York decisions exempting insurance companies from liability

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[21]Fla. Laws 1949, c. 25435, §1, Fla. Stat. §734.041(1) (1949).

[22]*E.g., In re* Dettmer's Will, 179 Misc. 844, 40 N. Y. S.2d 99 (Surr. Ct. 1943); *In re* Klein's Estate, 175 Misc. 961, 25 N. Y. S.2d 869 (Surr. Ct. 1941); *In re* Meynen's Estate, 173 Misc. 19, 18 N. Y. S.2d 62 (Surr. Ct. 1939); *In re* Kaufman's Estate, 170 Misc. 436, 10 N. Y. S.2d 616 (Surr. Ct. 1939).

[23]*E.g., In re* Kelly's Will, 86 N. Y. S.2d 441 (Surr. Ct. 1949); *In re* Burr's Estate, 72 N. Y. S.2d 905 (Surr. Ct. 1947); *In re* Blumenthal's Estate, 180 Misc. 895, 42 N. Y. S.2d 898 (Surr. Ct. 1943).

[24]*In re* Appel's Estate, 189 Misc. 417, 69 N. Y. S.2d 772 (Surr. Ct. 1947); *In re* Blumenthal's Estate, 182 Misc. 137, 46 N. Y. S.2d 688 (Surr. Ct. 1943), *aff'd*, 293 N. Y. 707, 56 N. E.2d 588 (1944); *In re* Iselin's Will, 41 N. Y. S.2d 808 (Surr. Ct. 1943).

for taxes on proceeds paid directly to beneficiaries on the death of an insured, has provided in Section 3 that the act does not authorize recovery of any taxes from any insurance company on the proceeds of a policy on the life of the decedent. New York has held that an insurer is not a person interested or person in possession of taxable property within the terms of its statute permitting recovery by the executor from such person.[25]

IV. Section 4: Application to Estates of Persons Dying after January 1, 1948

Section 4 of the Florida statute specifically makes it effective retroactively to estates of decedents dying after January 1, 1948, although the statute did not become a law until June 13, 1949. The Florida Constitution contains no general prohibition of retroactive laws as such; and neither does the Constitution of the United States.[26] Consequently this section of the act must be challenged, if at all, on the ground that it contravenes the due process clause of one of these two constitutions.[27]

A retroactive state law, unless running afoul of some other distinct constitutional inhibition, could operate to divest property rights prior to the adoption of the Fourteenth Amendment; but since then the protection afforded by the due process clause has prevented such divestiture.[28] Today the destruction of vested rights would render this section of the Florida apportionment act unconstitutional. This in turn brings us squarely to the question of what constitutes a vested right. The Supreme Court of the United States has defined it as an immediate and fixed right of present and future enjoyment and has made the further qualification that rights are said to be vested in contradistinction to their being contingent or expectant.[29]

In this connection it must be noted that Florida adopts the death

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[25]*In re* Zahn's Estate, 273 App. Div. 476, 77 N. Y. S.2d 904 (1st Dep't 1948).

[26]*E.g.*, Board of Comm'rs of Everglades Drainage Dist. v. Forbes Pioneer Boat Line, 80 Fla. 252, 86 So. 199 (1920), *rev'd*, 258 U. S. 338 (1922); Kentucky Union Co. v. Commonwealth, 219 U. S. 140 (1911).

[27]U. S. Const. Amend. XIV; Fla. Const. Decl. of Rights, §12.

[28]Memphis v. United States, 97 U. S. 293 (1877); Lowe v. Harris, 112 N. C. 472, 17 S. E. 539 (1893).

[29]Pearsall v. Great Northern Ry., 161 U. S. 646 (1896).

of the testator as the event that vests the right to legacies and devises unless the testator has provided in his will that some other event must happen prior thereto.[30] This statute has been applied several times by the Supreme Court of Florida.[31]

Since retroactivity alone does not result in unconstitutionality, the same law may be valid as applied to one set of facts and yet invalid as applied to others.[32] It follows that the specific attempted application of the statute becomes the decisive factor in squaring it with the organic state and federal prohibitions.[33]

Now let us consider some of the factual situations that may arise. Assume that the testator makes his will in 1938 and dies in August of 1949, shortly after the enactment of the apportionment statute. Certain specific legatees claim their shares free and clear of estate taxes, on the ground that the will was drawn in contemplation of the law governing in 1938. Testamentary disposition of property is not a natural right but is rather a creature derived solely from statutes. Accordingly this right is at all times subject to regulation and control by the legislative authority that creates it.[34] It is clear, of course, that there is no vested right in having the law continue as it is; and no contention against constitutionality can be successfully made under this set of facts.[35] All the beneficiary had in this instance was an expectancy, and this does not constitute a vested interest.[36]

Different considerations apply when the testator makes his will in 1938 and dies just prior to the passage of the act, so that upon its enactment his property is still in administration, with the assets undistributed and the taxes unpaid as yet. The first serious question of constitutionality arises here. Before the adoption of the Fourteenth Amendment a Montana case indicated that retroactive application did

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[30]FLA. STAT. §731.21 (1949).

[31]*E.g.*, Hurt v. Davidson, 130 Fla. 822, 178 So. 556 (1937); Sorrels v. McNally, 89 Fla. 457, 105 So. 106 (1925); Jones v. Shomaker, 41 Fla. 232, 26 So. 191 (1899).

[32]Magee v. Treasurer and Receiver Gen., 256 Mass. 512, 153 N. E. 1 (1926).

[33]U. S. CONST. Amend. XIV; FLA. CONST. Decl. of Rights, §12.

[34]Taylor v. Paine, 154 Fla. 359, 17 So.2d 615 (1944).

[35]*In re* Stanfield's Estate, 170 Misc. 447, 10 N. Y. S.2d 613 (Surr. Ct. 1939), *aff'd*, 257 App. Div. 932, 12 N. Y. S.2d 1022 (1st Dep't 1939).

[36]Pearsall v. Great Northern Ry., 161 U. S. 646 (1896); Cusick v. Feldpausch, 259 Mich. 349, 243 N. W. 226 (1932).

not violate federal organic law.[37] After the passage of the Fourteenth Amendment, however, in view of inferences gathered by the Montana court from certain United States Supreme Court decisions,[38] it squarely reversed its previous holding.[39] This limitation was not strictly necessary. The true federal position, taken in *Cahen v. Brewster*,[40] was that in defining an inheritance tax as a tax on succession, and not on the property itself, it was merely determining the nature of the tax rather than prescribing the time of imposition; federal law does not prevent a state from fixing the time of vesting at the death of the testator, at distribution, or after payment of taxes. This determination has been amply sustained.[41] Accordingly, from the standpoint of federal law, the constitutionality of the 1949 Florida provision swings on the Florida law governing the vesting. Does this occur at death, or upon completion of probate, or upon distribution of assets, or upon payment of estate taxes, or upon some combination of these factors?

The Massachusetts Supreme Court stated in 1945 that the imposition of an estate tax, pursuant to the local apportionment statute, against an inter vivos trust later included in the gross estate for tax purposes was not unconstitutional as a deprivation of property, even though the statute in question was passed after the testator had died.[42] The reason given was that the property had not yet been distributed, nor had the taxes been paid. The opinion[43] quoted *United States v. Perkins*[44] as authority for the proposition that it is not until the property ". . . has yielded its contribution to the state that it becomes the property of the legatee." This Massachusetts case[45] was cited with approval and followed by New York in *Central Hanover Bank*

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[37]Gelsthorpe v. Furnell, 20 Mont. 297, 51 Pac. 267 (1897).

[38]Binney v. Long, 299 U. S. 280 (1936); United States v. Jones, 236 U. S. 106 (1915); Cahen v. Brewster, 203 U. S. 543 (1906); Knowlton v. Moore, 178 U. S. 41 (1900).

[39]*In re* Clark, 105 Mont. 401, 74 P.2d 401 (1937).

[40]203 U. S. 543 (1906).

[41]Coolidge v. Long, 282 U. S. 582 (1931); Chase Nat. Bank v. United States, 278 U. S. 327 (1929); Salomon v. State Tax Comm'n, 278 U. S. 484 (1929); Watson v. Comptroller, 254 U. S. 122 (1920).

[42]Merchants Nat. Bank of Boston, Ex'rs v. Merchants Nat. Bank of Boston, Trustees, 318 Mass. 563, 62 N. E.2d 831 (1945).

[43]*Id.* at 573, 62 N. E.2d at 837.

[44]United States v. Perkins, 163 U. S. 625, 628 (1896).

[45]See note 42 *supra*.

and Trust Co. v. Peabody[46] in applying a Connecticut apportionment statute to the estate of a Connecticut citizen who predeceased its enactment. The New York court emphasized the fact that at the time such application was sought no taxes had been paid.

The Supreme Court of Pennsylvania In re *Jeffery's Estate*,[47] likewise applied the apportionment statute of that state to the estate of a decedent who died before its enactment but whose estate was in the course of administration when the act was passed. Taxes had already been paid by the fiduciary; yet no significance was accorded this fact.

Florida specifically fixes the time of vesting at the death of the deceased,[48] whereas such a statutory provision is lacking in Connecticut, Massachusetts and Pennsylvania. This fact greatly weakens, if indeed it does not nullify, any persuasive effect that the foregoing decisions of those jurisdictions might otherwise have in sustaining the retroactive application of the new Florida apportionment statute. As long as Section 731.21 of Florida Statutes 1949 remains on the books, it is difficult to see how apportionment can be applied retroactively in this state without destroying vested rights. It is no answer to say that estate taxes must be paid before any net estate can be reckoned. The sole issue is: Which beneficiary must meet the payment? Section 731.21 fixes the date of such determination; and the tax law on that date sets both the tax burden and its effect on the net shares.

Another set of facts presents an even stronger case against retroactive apportionment. A testator makes his will in 1938 and dies prior to the passage of the 1949 statute; in fact, it is passed while administration of the estate is still in progress. Some of the property has been distributed but the taxes have not been paid. In this situation, the time of vesting should still be the determining factor, of course, in considering constitutionality. Our Supreme Court might in this instance have an additional reason for forbidding retroactive application of the statute, in that collection of a retroactive tax after the property has been received, and perhaps dissipated, by the legatee occasions administrative difficulties as well as a hardship on the legatee.

As a final situation, assume that the testator executes his will in 1938 and dies prior to the passage of the statute. Assume further that

[46]190 Misc. 66, 68 N. Y. S.2d 256 (Sup. Ct. 1947).
[47]333 Pa. 15, 3 A.2d 393 (1939).
[48]FLA. STAT. §731.21 (1949).

at the time the statute was passed all estate taxes had been paid out of the residuary estate and the property had been distributed. The residuary legatee now demands apportionment and contribution from the specific legatees. Here it is most unlikely that the Court would sustain retroactive application of the statute, especially when the number of probable adjustments and repercussions are considered. Such application would not only disregard the time of vesting fixed by statute, but even without such a provision the rights to the property should at least have vested by the time the taxes were paid and the property distributed.

V. Section 5: Severability Clause

Section 5 of the apportionment statute is the typical provision that each section of the act is indicative of the legislative intent, independently of the other sections, and that if any section be declared unconstitutional the other sections remain nonetheless valid. This language saves the remainder of the statute, even if the retroactive provisions should be held unconstitutional.

This section also contains the statement that the statute is ". . . declaratory of existing public policy . . . ." Inasmuch, however, as the statute is obviously in derogation of the previously existing law and is intended to effect a change, it could scarcely be declaratory of existing public policy. Hence this statement has no significance other than to indicate that the Legislature is continuing to enact laws conforming to the desires of the electorate.

VI. Conclusion

This statute represents a decided step forward in Florida estate tax law. Formerly, a will frequently failed to carry out the intent of the testator because little or no consideration was given to the payment of estate taxes. Yet today these have assumed mammoth proportions. The practice of making specific bequests to charities, friends, and even distant relatives while naming those nearest in kinship and affection as beneficiaries of the residuary estate is only too familiar. Because of a logical though false assumption as to the law on the part of the deceased, or because of his failure even to consider the impact of the burden of the estate tax, those whom he intended to