Michigan Law Review

Volume 40 | Issue 6

1942

TAXATION - FEDERAL ESTATE TAX - DEDUCTION ALLOWABLE FOR GIFTS TO CHARITY WHEN THERE HAS BEEN A COMPROMISE

William H. Shipley
University of Michigan Law School

TAXATION — FEDERAL ESTATE TAX — DEDUCTION ALLOWABLE FOR GIFTS TO CHARITY WHEN THERE HAS BEEN A COMPROMISE — The testator gave the residue of his estate to a charity. When the widow of the testator made known her intention to contest the will, the charity offered to give her "a sum equivalent to twenty-five per cent"[1] of the amount it was to receive under the will. The widow then agreed to withdraw all objections to the probate of the will. The executors were not parties to the compromise agreement, nor was it incorporated in, or made a part of, the probate proceedings. The executors filed an estate tax return in which a deduction from the testator's gross estate was claimed for the full amount of the residuary estate as a bequest to charity. The commissioner of internal revenue contended that the twenty-five per cent of

[1] This is the language of the compromise agreement. Principal case, 122 F. (2d) 480 at 481.

the residue going to the widow by the terms of the compromise agreement was not deductible. *Held*, the amount received by the widow cannot be deducted from the gross estate since she took by "inheritance." The amount to be deducted for testamentary charitable gifts must be the amount the charity actually receives, and not the amount provided for in the decedent's will. *In re Sage's Estate*, (C. C. A. 3d, 1941) 122 F. (2d) 480.

In *Robbins v. Commissioner*[2] it was held that if a charity receives nothing under the will but takes by virtue of a compromise agreement, the amount thus received cannot be deducted from the gross estate as a charitable bequest. Thus the executors in the principal case contended that the compromise agreement[3] should not be considered in determining the amount deductible as a charitable bequest. The court, in meeting this argument, relies on the decision in *Lyeth v. Hoey*,[4] where it was held that the amount received by an heir as the result of a compromise agreement is not income but an "inheritance" for purposes of the income tax law. The *Robbins* case is distinguished from the principal case on the ground that the charity in the *Robbins* case had no standing as an heir to contest the will, so that whatever it received was the result of a bargain and not an "inheritance." Thus the court concludes that since the widow in the principal case takes by "inheritance" because of her standing to contest the will, the share she receives cannot be deducted from the gross estate. But this reasoning appears to rest on the premise that in such cases whatever is not income under the income tax law is an inheritance under the estate tax law and thus must be included in the gross estate. However, it would seem that a better ground for distinguishing the *Robbins* case is that Congress provided for the deduction of charitable bequests in order to encourage testators to make such gifts.[5] In the *Robbins* case the testator had no intent to make a definite gift[6] to the charity, so no deduction should be allowed. The testator in the principal case had the intent to make a charitable gift. But there can be no deduction because the statute[7] clearly contemplates that the money should be received by the charity and used by it only for charitable purposes. The charity in the principal case will receive all the funds in the residue of the estate, and thus it is bound by

[2] (C. C. A. 1st, 1940) 111 F. (2d) 828.

[3] It is immaterial whether or not the compromise agreement is probated with the will. Robbins v. Commissioner, (C. C. A. 1st, 1940) 111 F. (2d) 828, overruling Smith v. Commissioner, (C. C. A. 1st, 1935) 78 F. (2d) 897.

[4] 305 U. S. 188, 59 S. Ct. 155 (1938). See also Charlotte Keller, 41 B. T. A. 478 (1940); Chase National Bank, 40 B. T. A. 44 (1939).

[5] There can be no deduction for the amount of an unpaid pledge paid by the executor to a charity because there is no transfer from the decedent. Taft v. Commissioner, 304 U. S. 351, 58 S. Ct. 891 (1938).

[6] The terms of the transfer must be certain and enforceable. Mississippi Valley Trust Co. v. Commissioner, (C. C. A. 8th, 1934) 72 F. (2d) 197. The possibility of a will contest does not defeat its certainty. Commissioner v. First National Bank of Atlanta, (C. C. A. 5th, 1939) 102 F. (2d) 129.

[7] The statute allows a deduction from the gross estate for "The amount of all bequests, legacies, devises, or transfers . . . to a trustee . . . but only if such contributions or gifts are to be used by such trustee . . . exclusively . . . for charitable . . . purposes. . . ." 44 Stat. L. 72, § 303 (a) (1926), 26 U. S. C. (1934), § 412 (d).

the compromise agreement then to pay the widow "a sum equivalent to twenty-five per cent" [8] of the amount it receives. It is quite possible that this amount may be paid to the widow from other funds belonging to the charity, but in substance the charity has received only seventy-five per cent of the residue. The court is clearly following the intent of Congress [9] in looking through the form of the transaction to see what the charity actually receives.[10]

William H. Shipley

[8] Principal case, 122 F. (2d) 480 at 481.

[9] Bequests for charities are of value to the government because the government is relieved of the expense of supporting the charity. Union & New Haven Trust Co. v. Eaton, (D. C. Conn. 1937) 20 F. (2d) 419. See H. REP. 1860, 75th Cong., 3d sess. (1938), p. 19. Thus a deduction should be allowed only to the extent the government is relieved of support.

[10] The Board of Tax Appeals reached the same result in its decision, which is reported in 42 B. T. A. 1304 (1941). Apparently Continental Illinois National Bank & Trust Co., 38 B. T. A. 220 (1938), is overruled.