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Liability of the Entire Community Estate for the Payment of State Inheritance Tax Where Husband Undertakes to Dispose of Entire Community Estate by Will and Wife Elects to Take under the Will

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LIABILITY OF THE ENTIRE COMMUNITY ESTATE FOR THE PAYMENT OF STATE INHERITANCE TAX WHERE HUSBAND UNDERTAKES TO DISPOSE OF ENTIRE COMMUNITY ESTATE BY WILL AND WIFE ELECTS TO TAKE UNDER THE WILL.

The question suggested by this topic has not been passed upon by the Supreme Court of this state and has already proven troublesome in a good many pending estates. In this paper, the problem will be discussed from the standpoint of the local inheritance tax and community property statutes, without any especial attention to the similar question which arises under the federal estate tax laws. However, while the state tax and the Federal tax are undoubtedly fundamentally different in their nature, it is thought that the solution of the problem as to the state tax will likewise solve it as to the Federal tax, and that any discussion of the problem with reference to one tax is largely applicable to the other.

The importance of this question lies not only in the determination of the tax in pending estates and in estate of men whose wills have already been executed, but in its vital bearing upon the attitude of men of considerable means who will hereafter from time to time desire to give careful thought to the proper testamentary disposition of their estates. The usual will which undertakes to dispose of the entire community estate in trust, giving to the wife the income or the major part of the income during her lifetime, is considered by many men and many lawyers as near an ideal arrangement as can be devised under our present community property statutes in the disposition of larger estates.[1] Such wills offer the greatest protection to the estate, and at the same time give to the widow as nearly an assured income as possible without any of the responsibility or hazard of caring for the property

It seems remarkable in a way that no adjudication on this point

[1] On widow's election where husband undertakes to will all of the community property as his own, see *Collins v. Collins*, 152 Wash. 499, 278 Pac. 186 (1929) *In re Williams Estate*, 145 Wash. 19, 258 Pac. 851 (1927) *Andrews v. Kelleher* 124 Wash. 517, 214 Pac. 1056 (1923) *In re Curtis's Estate*, 116 Wash. 237, 199 Pac. 309 (1921) *Herrick v. Miller*, 69 Wash. 256, 125 Pac. 974 (1912). As to time when widow's election is made, and manner of making, see 40 Cyc. 1974, *et seq.*

has yet been secured in this state, and yet the fact is that in most of the cases where the matter has been presented to the Inheritance Tax Department, the additional tax demanded by that department and by the Internal Revenue Department of the Federal Government has been relatively small and has not justified litigation. Unquestionably, however, the time will soon arrive when the amount of the additional tax demanded will justify the interested parties in going to the expense of securing a decision on the question.

While it is believed that the proper determination of the question lies in a logical application of the fundamental conceptions of our community property system,[2] it is nevertheless interesting and important, before attempting such an analysis, to refer briefly to the decisions of courts of other states which have passed upon this and similar questions.

The cases from common law states bearing upon the somewhat analogous question of whether a widow, who elects to take under the will and waive her dower right, which would otherwise be untaxed, is subject to a tax on the entire estate received are not harmonious.

In Arkansas[3] it was held that under a statute similar to ours, imposing an inheritance tax upon all property bequeathed under a will, where the widow accepted and retained the property bequeathed under the will, electing thereby to waive her dower right, all such property was subject to an inheritance tax since she took no dower whatever under the circumstances.

The obvious distinction, however, between the widow's dower right and her right in community property should be noted at this point. While under our community property system, the widow undoubtedly has an absolute legal ownership of one-half of the community estate, it is generally true in common law states that the legal title to the property is in the husband and that the dower right of the wife rises to nothing more than an equitable interest or an expectancy in the estate, which is dependent upon her sur vivorship.

In Utah it is provided by statute that "one-third of all real property possessed by the husband at any time during the marriage shall be set apart as her property in fee simple if she survives

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See for a discussion of the fundamental nature of the community property system, George Donworth, "Federal Taxation of Community Incomes," 4 Wash. L. Rev. 145 (October, 1929).

[3] *State v. Lane*, 134 Ark. 71, 203 S. W 17 (1918).

him. " The statute also provides that if provision is made for the wife in the will, she must elect whether she will take under the will or under the statute first referred to.

In a leading Utah case on the subject[4] it appeared that provision was made for the wife in the will, and she elected to take under the will. She then claimed that the value of her statutory one-third interest in the real estate should be deducted from her share under the will in figuring the inheritance tax. The Supreme Court of Utah held, however, that by taking under the will, she was in the same position as any other devisee or legatee and no deduction could be allowed, and that by taking under the will "she relinquishes the right given to her by the statute just as effectually as though she had conveyed such rights by deed either before or after the death of her husband and thus whatever share she receives from her husband's estate under the will passes to her by such will and not otherwise." This decision was again approved by the Supreme Court of Utah as late as March, 1920.[5]

Substantially the same conclusion was reached by the Indiana court in 1925.[6] In that case, the husband devised property in trust for his wife, with the provision that if she elected to accept the provisions made for her by law, the provisions of the will would be ineffectual. She accepted the provisions of the will, and the court held that the entire estate received by her was subject to an inheritance tax.

The rule is the same in New York.[7]

The foregoing are typical of a considerable number of cases from several common law states on a question which it must be candidly admitted is very close to the one under consideration. Yet, as pointed out above, it seems that there is an obvious distinction between this line of cases and the situation with which we are here confronted in view of the difference in the character of the wife's estate prior to the death of the husband.

Some of the common law states, however, have arrived at a different conclusion by a process of reasoning which seems to be much more logical. Typical of these is a decision of the Supreme Court of Nebraska.[8] In that decision the court said

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[4] *In re Osgood's Estate*, 52 Utah 185, 173 Pac. 152 (1918).
[5] *In re Kohn's Estate*, 56 Utah 17, 189 Pac. 409 (1920).
[6] *In re Arp's Estate*, 83 Ind. App. 371, 147 N. E. 297 (1925).
[7] *In re Stuyvesant's Estate*, 131 N. Y. Supp. 197 (1911).
[8] *In re Sanford's Estate*, 91 Neb. 752, 137 N. W 864 (1912).

> "It was contended on the argument of the motion for a rehearing that the recently adjudicated cases hold that, notwithstanding the fact that the widow of one who dies testate takes under the will and thus relinquishes dower, the value of her dower interest in the lands of which her husband died seized is not chargeable with an inheritance tax. In other words, the value of her dower interest should be deducted from the appraised value of the estate, and the inheritance tax should be computed on the remainder thereof. It would seem from a review of the cases decided since our opinion was adopted, that such is the weight of authority The reason for the rule seems to be that the widow takes her dower interest in the estate of her deceased husband by operation of law, that she could not be deprived of it by his will, that it is something which belongs to her absolutely and independent of any right of inheritance or succession, and therefore so much of the estate as belonged to her by right is not chargeable with an inheritance tax. We are not inclined to place ourselves in opposition to the weight of authority on this question, and to this extent our former judgment is modified."

The only decision from a community property state which bears directly upon the question presented is *Texas v. Jones*,[9] decided by the Supreme Court of Texas on May 9, 1928. In that case the husband by his will devised to the wife certain specific property in lieu of her community interest in the entire estate. The specific property devised was approximately equal to her undivided half in the entire community property She elected to take under the will, and the State of Texas sought to impose a tax on the undivided one-half interest of the husband in the specific property devised to her. The lower appellate court of the State of Texas, citing the dower cases which have been referred to above, held that where a person accepts the benefits under a will, he must adopt the whole contents of the instrument so far as it concerns him, renouncing every right inconsistent with the will, and that, therefore, an undivided one-half interest in the specific property devised to the wife must be considered as passing to her by the will so as to subject that undivided one-half interest to the tax under the Texas Inheritance Tax Statute, which is almost identical with ours. The Supreme Court of Texas, however, reversed the decision of the intermediate appellate court, and in so doing used the following language

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[9] 290 S. W 244, 5 S. W (2nd Series) 972.

"It cannot be said broadly that the surviving widow has not taken anything under the will which she would not otherwise have received, since she has received specific property under the will, whereas in the absence of the will she would have owned an undivided one-half interest in all the property But this is of no moment in the consideration, for we have seen that by the terms of the statute before the tax is imposable the property must have passed by the will. We are of the opinion no property passed to the widow by the will in any event. It is undisputed that all of the estate possessed by the testator was community property As matter of law, the wife was the equal owner in her own right of one-half of that estate. To be sure, their estates existed in common, and during the marriage the common estate was indissoluble, but nevertheless her right, subject to certain statutory control, was the equal of the husband's. Upon the husband's death, the community estate passes, one-half to the widow and one-half to the children (where there are children. But, while this provision of the law is found in our statutes of descent and distribution, nevertheless the wife's taking her one-half of the community is not the taking by an heir. She does not inherit such one-half, but she takes it as owner in her own separate right after the dissolution of the marriage. *King v. Morris* (Tex. Com. App.), 1 S. W (2d) 605. So that it is plain, if there had been no will, the surviving widow would not have been taxable for the one-half of the community which she would have taken, because the same would not have passed 'by the laws of descent or distribution.'

"Now, if the surviving widow owned in her own right an undivided one-half interest in the community property of herself and husband, then she had title to that extent to such property, and, if the will of deceased did not pass any property to her, clearly she is not taxable. The will did not pass any property whatever to her, because it operated only as an effective partition of the community property after death.

"Under the undisputed facts, the surviving widow having received no more than her just share of the community property fully owned by her prior to the death of her husband, she has received no property through the operation of the will. The only effect of that instrument was to partition the community property between the surviving widow and the other beneficiaries, in other words, to make definite the particular portion of the community property owned by her, and not in anywise to affect, by increasing or diminishing, her estate. This is not the passing of property contemplated by the Inheritance Tax

> Act. To impose the tax under such circumstances would be to visit the tax upon the real owner whose real right to the property has not been affected one way or the other by the death of a co-owner."

The State Inheritance Tax Department has relied largely upon the decision of the intermediate appellate court of Texas in the *Jones* case, and it would seem very significant, therefore, that the Supreme Court of Texas in its recent decision has entirely over ruled the reasoning of the lower Texas court.

So much for the outside cases. It is sufficient to say that an investigation of the decisions of other states upon this and closely analogous questions shows that there is a hopeless conflict in those decisions. It is submitted, however, that the language used by the Nebraska court and by the Supreme Court of Texas which has been referred to is logical and entirely in conformity with our fundamental notions of the community property system, and that a simple application of these fundamental conceptions demonstrates not only that the state, under our present Inheritance Tax Statute, is not entitled to a tax upon the wife's share in the community property, even where she elects to take under the will, but that an attempt on the part of the state to levy such a tax raises a serious constitutional question as to its right to do so.

It cannot be seriously contended that the husband has any other or greater interest in the community property than the wife. They are equal owners in every respect and the character of their title to the community property is absolutely identical. The mere fact that under the statute the husband is made the managing agent of the community of course does not change in any respect the wife's equal legal ownership of one-half of the community estate.

The Supreme Courts of Idaho and Nevada (both community property states) have clearly expressed the character of the wife's interest in the community property in their decisions, holding specifically that the wife's half of the community property is not subject to an inheritance tax upon the death of the husband. While these cases, of course, are not directly in point, they are valuable in apprising us of the true character of the community

Before quoting from these cases it is also worth while mentioning that the inheritance tax statutes and the statutes governing the descent of community property in Idaho and Nevada are practically identical with ours. In the Idaho case,[10] the court said.

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[10] *Kohny v. Dunbar* 21 Idaho 258, 121 Pac. 544 (1912)

"The foregoing section of the statute recognizes the husband and wife as equal partners in the community estate, and it authorizes each to dispose of his or her half by will. It also provides that the survivor shall continue to be the owner of half of such property, subject only to the payment of the community debts. This statute clearly and unmistakably provides that the surviving spouse take his or her half of the community property, not by succession, descent, or inheritance, but as survivor of the marital community or partnership. The same section provides, further, that in the event there be no issue of the marriage living at the time of the death of one of the spouses, and he or she leaves no will or testament, the half of the community property which belonged to the deceased shall go to the survivor as an heir, and, therefore, by descent and under and by virtue of the 'intestate laws of this state.' While, therefore, the survivor in this case receives the entire community estate by reason of the death of her husband, half of it was already hers, and the only additional interest or right she acquires in that half by reason of the death of her husband is the right of management, control and disposition. The death of the statutory managing agent and trustee leaves the wife without such agent, and reduces her to the status of a feme sole, and the law authorizes her to act in her own right. Death has worked a dissolution of the community partnership, and left the surviving partner to act for herself. She also receives the other half of the community property, but by an entirely different means. It comes to her likewise by reason of the death of the husband, but through the means of her heirship. The statute makes her an heir of her husband, and so, in the absence of testamentary disposition of the husband's share of the community property, she inherits his half, and therefore takes his share under the intestate laws of the state. It is clear however, that she does not inherit her share of the common property"

In the Nevada case,[11] the court said.

"It is not necessary to dwell on this principle here, because, viewing the matter as we do in the light of the great weight of authority, and especially under statutes providing for the community system, there is no 'taking property from another, either by will or legal devolution.' The property here going to the appellant was property which she at all times under our statutory provision 'held

[11] *In re Williams*, 40 Nev. 241, 161 Pac. 741 (1916).

> in common with her husband.' Hence there was no privilege to be taxed, but rather a 'right' in property recognized by statutory prescription 'held' by her at all times 'in common with her husband.' The death of the husband only dissolved the community, and released that which she held from the statutory dominance of her deceased spouse."

Mr. Ross, in his work on Inheritance Taxation,[12] makes the following statement in reference to the liability of the wife's share of the community property to an inheritance tax.

> "The legislature, in adopting the community system, intended to provide a real marital community in property and accord to the wife a fuller measure of property rights than was hers under the common law The legislature did not suppose it was providing her a mere expectancy during the husband's life and an inheritance on his death. That would be far from what is contemplated in the very nature of community property And certainly, in adopting the inheritance system of taxation, the legislature did not have in mind the exaction of tribute from the community interest of a wife upon the death of her husband. In his lifetime such interest is her own property, practically in the fullest sense, except that the law constitutes him the agent for its control and management, and the removal of the agent by death in no wise works a transmission of title to be subjected to the succession tax."

From the foregoing it clearly appears that upon the death of the husband the wife does not take her half of the community property by inheritance, but that she simply retains what she already owns, and, this being so, it is beyond the power of the state as a general rule to levy an inheritance tax upon her half of the community property At this point we should also remember that under the statute the husband has absolutely no right to make any testamentary disposition of the wife's half of the community property, for the obvious reason that it is hers and not his to dispose of.

Now, upon the death of the husband, either with a will or without a will, the wife is still the absolute owner of one-half of the community property, and nothing that the husband can do or say in his will can change that situation or can in any way affect this absolute ownership of the wife.

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[12] Ross, Inheritance Taxation, p. 84.

Bearing in mind that the death of the decedent is the time that the rights of all parties, including the rights of the commonwealth to tax, are determined,[13] it seems that we have now arrived, by the simple application of elementary principles, at the correct solution of the problem. For it is manifest that at the time of the death of the husband, under a will such as we are here discussing, the state is in no position to levy any tax whatever upon the wife's half of the community property

Before the state can plausibly make such an attempt, a further voluntary and affirmative action on the part of the wife is required. In other words, she must agree and consent, either by a formal written acceptance of the will and relinquishment of her interest in the community property, or by virtue of an estoppel, that her half of the community property shall, along with the husband's half, be turned into the trust.[14] But this amounts to nothing more than a conveyance by the wife to the trustee, after the death of the husband, of her interest in the community property The fact that the entire community property finds its way into the trust does not mean that the trustee or the beneficiaries under the trust receive the property by will or inheritance, it simply means that one-half of the community property goes to the trustee for the benefit of the named beneficiaries by virtue of the will of the husband, and the other half of the community property goes into the trust because of the voluntary and, what clearly seems to be, the legally affirmative act of the wife.

Our statute[15] levies an inheritance tax upon "all property which shall pass by will or by the statutes of inheritances of this or any other state. " To say that the wife's half of the community property passes to the trustee "by will" is to do violence to every fundamental principle of community property law.

Other broad principles of law support this conclusion, for it is accepted law in this state that an inheritance tax is a tax on the right to inherit,[16] or, as otherwise expressed, a tax on the privilege of succeeding to the inheritance or of becoming a beneficiary under a will.[17] Again, it is unquestionably the law that an inheritance tax is not applicable where the property or interest there passes

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[13] *Kingsbury v. Chapin*, 196 Mass. 533, 82 N. E. 700 (1907) *Old Colony Trust Co. v. Treasurer*, 238 Mass. 544, 131 N. E. 321 (1921).

[14] See footnote 1, *supra.*

[15] Rem. Comp. Stat. sec 11201, P. C. sec. 7051.

[16] *In re Corbin's Estate*, 107 Wash. 424, 181 Pac. 910 (1919).

[17] Cooley, on Taxation, paragraph 1721.

independently of the death of the decedent.[18] And even though the transmission of property depends upon the death of the decedent, it is not within the descriptive words of the statute where it passes from an outside source rather than from the decedent.[19]

Moreover, our own Supreme Court, in passing upon the validity of the inheritance tax statute, says that the right to levy such a tax depends upon the state's plenary power to direct the disposition of the property of decedents, the right of the owner of property to make testamentary disposition of the same not being a natural right which follows from mere ownership, and. therefore, the state being permitted to take the whole of a man's estate upon his death, it may, if it chooses, take any part less than the whole.[20] But if it be contended that the state has the right to tax the wife's half of the community property, even where she takes under the will, it would seem that the state is undertaking to levy an inheritance tax on property which was not at all owned by the decedent, and thus a serious constitutional question arises. Consequently any attempt to levy such a tax on the wife's share, even though she takes under the will, is not only to disrupt our well-settled ideas of the community property system, but, beyond that, appears to run counter to other broader and well recognized principles of law.

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[18] *Dexter v. Treasurer* 243 Mass. 523, 137 N. E. 877 (1923).

[19] *Tyler v. Treasurer* 226 Mass. 306, 115 N. E. 300 (1917)

[20] *In re Sherwood's Estate*, 122 Wash. 648, 211 Pac. 734 (1922).

* Of the Seattle Bar. The foregoing paper was originally prepared and delivered as an address before the Seattle Association of Trust Men.