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Notes on the Estate Tax Apportionment Act of 1951

John E. Williams

NOTES ON THE ESTATE TAX APPORTIONMENT ACT OF 1951

Act 338 of August 24, 1951

(Senate Bill 303)

The Estate Tax Apportionment Act of 1951 had its genesis in a suggestion during the summer of 1950 that there should be a provision for apportioning estate tax even though the tax had not been paid by the executor.

The official "Comments" that have been prepared by the draftsmen will afford substantial help to persons applying the act and are replete with explanations and citations.

The notes that follow are unofficial observations by one who had the opportunity to study and comment on the successive drafts for Senate Bill 303. It is hoped that the small histories of certain sections and bits of phraseology may be of interest and help to those who encounter a problem in this complicated field of tax accounting.

The punctuation used in quoting the sections of the Act is also unofficial, inasmuch as the official punctuation is not available at the time of writing.

During the summer of 1950 the Bank and Trust Company Tax Association of Philadelphia was asked to review the Pennsylvania Act for Apportionment of Federal and State Estate Taxes (Act No. 565, P.L. 2762, Laws of 1937), for the purpose of sponsoring an amendment that would give the Orphans' Court the authority to apportion estate taxes even though the tax had not actually been paid. Under the Act of 1937, the Pennsylvania courts had held that proration proceedings could not be entertained until the tax was paid. *Lucey Estate,* 63 D. & C. 645; *Cardeza Estate,* 51 D. & C. 461.

The Bank and Trust Company Tax Association referred the matter to the writer as Chairman of its Legislative Committee, and a study was made of estate tax apportionment legislation of the various states to determine the feasibility of an amendment for Pennsylvania. The survey indicated that seven states required payment before proration proceedings, and eight did not. In general the more recently enacted laws eliminated the requirement of payment before proration. A detailed comparison was made of the Pennsylvania Act of 1937 with the New Jersey Act of 1950 and the New York amending Act of 1950. Both of the latter approved apportionment prior to payment.

Contact was made with the Advisory Committee to the Sub-committee on Decedents' Estates Laws for the Joint State Government Committee of the General Assembly of Pennsylvania, and that Committee was asked to sponsor the proposed legislation.

By this time, comparisons and studies indicated that two additional changes in the apportionment act would be helpful:

1. Clarification of the effect of the marital deduction for Federal estate tax on the apportionment formula, where the surviving spouse takes against the will or by intestacy or there is otherwise no applicable tax clause.
2. Clarification of the effect on apportionment of the 80% credit for state death taxes against Federal estate tax computed at the basic 1926 rates.

Drafts of the proposed Estate Tax Apportionment Act of 1951 were prepared and Draft 3 dated October 3, 1950 was submitted to the Advisory Committee. This draft followed as closely as possible the form of similar acts in New York and New Jersey, and the Pennsylvania Act of 1937. It was believed at that time that wording and form similar to those used in our sister states would be advantageous, in that constructions and decisions in the other two states would then be of particular help to practitioners, attorneys and courts in Pennsylvania.

However, the writer had discussed the New York Act of 1950 with a member of the New York Bar who had been active in the revision of their Act, and it was indicated that there had been some doubts and dissention as to the form and wording in New York and New Jersey, resulting in a stalemate over a period of approximately three years. The New Jersey Act of 1950 and the New York amending Act of 1950 thereupon resulted from attempts to resolve differences of opinion and the acknowledged need to enact legislation promptly.

Therefore, when the Advisory Committee to the Committee on Decedents' Estates Laws agreed to sponsor a Bill and after study recommended substantial changes in form, the writer relinquished the burden of draftsmanship to the Advisory Committee, and thereafter supplied comments and suggestions for the successive "Initial Rough Draft" of November 1, 1950, "Preliminary Draft" of November 20, 1950, "Tentative Draft 1" of November 22, 1950, "Tentative Draft 2", of December 26, 1950, "Draft of February 5, 1951", "Draft of February 15, 1951" and "Proposed Estate Tax Apportionment Act of 1951" which as introduced March 6, 1951 as Senate Bill 303.

> "*Section* 1. *Definitions.* The following words when used in this Act unless the context clearly indicates otherwise shall have the meanings ascribed to them in this section:"
>
> "*Section* 1. (1) 'Person' includes a corporation, partnership and association, as well as a natural person whether acting in a separate or in a fiduciary capacity."

The draft of November 1, 1950 defined "Person" to include "A corporation as well as a natural person". The draft of December 26, 1950 stated that "Person includes a corporation, partnership and association as well as a natural person". It was requested that the definition be reworded to make certain that the word

"corporation" would clearly apply to a corporation acting in a fiduciary capacity, and accordingly the definition was finally worded: "Person includes a corporation, partnership and association, as well as a natural person whether acting in a separate or in a fiduciary capacity". It should be understood that the phrase "whether acting———" applies to a corporation, partnership and association as well as to a person.

> "*Section* 1. (2) 'Estate Tax' means gross Federal Estate Tax including interest and penalty thereon."

The draft of November 1, 1950 provided for apportionment of both Federal estate tax and Pennsylvania estate tax "including interest thereon". The draft of December 26, 1950 initiated the wording used in S. B. 303, which provides for apportionment of "gross Federal estate tax including interest and penalty thereon". It of course is unusual to have a penalty assessed in respect to Federal estate tax, but Internal Revenue Code Section 3612 (d) (1) does provide a penalty for lateness in filing Federal tax returns and Regulations 105 Section 81.89 refer specifically to the penalty for delinquency in filing a Federal estate tax return.

Reference to apportionment of Pennsylvania estate tax was omitted in the later drafts as unnecessary inasmuch as it is the gross Federal estate tax that is apportionable under the new Act, before any credit for state taxes. See *Mellon Est.* 347 Pa. 520 for background on this point. Pennsylvania estate tax will redound to the credit of whoever pays it (see Section 4(b) (3) of S. B. 303) and thus an equitable result will follow. Only in very exceptional instances will failure to apportion Pennsylvania estate tax produce an inequity, such as a case where a refund of Federal estate tax is received, reducing the credit for state taxes, and the estate is unable to obtain a corresponding refund of Pennsylvania estate tax because a petition for refund was not filed within two years of the date of payment.

The suggestion was made that the "estate tax" to be apportioned might be more accurately defined as "tentative Federal estate tax imposed by Section 935 (b) of the Internal Revenue Code". However, the definition finally adopted was "gross Federal estate tax", which should be taken to mean the same as that covered by the suggested definition quoted above. It was considered inadvisable to refer to a specific section of the Internal Revenue Code for fear of some future change in the wording or arrangement of the code.

> "*Section* 1. (3) 'Persons' interested in property includible in gross estate' includes persons liable for payment of estate tax and persons whose property is subject to a lien for the estate tax. It includes personal representatives, Guardians and Trustees, individual or corporate."

Some small controversy arose in regard to the wording "persons interested in property includible in gross estate". The suggestion was made that reference to "persons benefited" might be more accurate and discourage any conjecture as to creditors as well as the merely curious being "persons interested". There was also

a suggestion that "includes" should be changed to "means". The draftsmen decided that such a change might clarify their intent, but believed that the meaning was sufficiently clear and retained "includes". However, "interested" is used in our own Act of 1937 and in the 1950 Acts of New York and New Jersey, and the purpose of S. B. 303 as well as the context can only be construed to rule out the conjecture mentioned above.

> "*Section* 1. (4) 'Gross Estate' means all property of every description required to be included in computing the estate tax."
>
> "*Section* 1. (5) 'Fiduciary' includes executors, administrators of any description and trustees."
>
> "*Section* 2. *Equitable Apportionment.* Estate Tax, except as pro-provided in subsection (a) of section three shall be apportioned equitably, as near as may be in accordance with the principles hereinafter stated, among all persons interested in property includible in gross estate whether residents or nonresidents of the Commonwealth, and they shall pay the amounts apportioned against them."

The draft of October 3, 1950 used the words "shall contribute to the tax". This was changed in the November 1, 1950 draft to "shall contribute". The next draft used "shall pay to the fiduciary". Finally this was shortened to "shall pay", so that payment may be made to the executor, the Collector of Internal Revenue, or to whomever equity or practicability indicates. This procedure is more workable than that prescribed in our 1937 Act which provided for payment "to such executor, administrator or other fiduciary". See notes on Section 5(a) and 5(b).

The draft of November 1, 1950 provided that the tax should be "equitably apportioned in accordance with the rules hereinafter stated". A question was raised as to the possibility of someone claiming an inconsistency in the wording to their own benefit, arguing that "the rules hereinafter stated" are not "equitable". Therefore the final wording for S. B. 303 was "shall be apportioned equitably, as near as may be in accordance with the principles hereinafter stated". It should be noted that the draftsmen, by the comma after "equitably", intended to stress equitable apportionment, with the "principles hereinafter stated" to be followed to the extent possible to achieve equitable apportionment. That is, equity comes first and the rules come second.

> "*Section* 3. *General Rules*
>
> (a) *Powers of Testator or Settlor.* A testator, settlor, or possessor of any appropriate power of appointment may direct how the estate tax shall be apportioned or allocated or grant a discretionary power to another so to direct. Any such direction shall take precedence over the provisions of this Act in so far as the direction provides for the payment of the estate tax or any part thereof from property the disposition of which can be controlled by the instrument containing the direction or delegating the power to another."

The draft of November 1, 1950 provided that: "The creator of any interest included in the gross estate may direct the manner of apportionment or grant a discretionary power of apportionment to another". This wording restricted the field, for a power to provide for apportionment, to an "interest included in the gross estate". Furthermore it did not include the possessor of a power of appointment. These ommissions were later corrected, as is apparent in the wording used for S. B. 303. Therefore the donee of a power or appointment, even one that is not includible in the gross estate, or the settlor of a deed of trust even though it is excludable from the gross estate, may provide that all or a part of the federal estate tax of his estate is to be paid from the fund over which he has the power of appointment, or from the trust of which he is the settlor, or he may grant a discretionary power in this respect to another.

> "(*b*) *Present and Remainder Interests.* When estate tax shall be apportioned in a situation involving both a present and future interest the amount apportioned including interest and penalties shall be paid entirely from principal even though the holder of the present interest also has rights in the principal."

The problem of charging interest on late payments and deficiencies against Income or Principal where both present and future interests are involved was carefully considered by the draftsmen. The draft of November 20, 1950 followed Section 11 (4) of the Principal and Income Act of 1947 and provided that "interest on taxes shall be paid out of Principal to the extent that such interest and penalties are in excess of the rate of return which has been or shall be realized from the estate during the time that such interest and penalty have accrued". The draft of December 26, 1950 omitted "or shall be", so that the phrase then read "the rate of return which has been realized". Then a strong feeling developed that calculation of the rate of return involved so many uncertainties and variables and so much work, that consideration should be given to Mellon's Estate, 247 Pa. 520, where interest on Federal estate tax was considered to be a part of the tax and apportioned as such. If the theory that interest was not part of the tax was not adopted, and if the the "rate of return" determined the amount of interest chargeable to Income, great difficulty might be met in determining the "rate of return". The numerator of the fraction (the income of the fund) would require detailed analysis. The denominator of the fraction (the value of the principal of the fund) would present an even greater difficulty, especially if the wording of the Principal and Income Act of 1947 were used. The question might arise as to whether the accountant should use the value of the gross estate for purposes of inventory and appraisement as of the date of death, or the value of the net estate, or the value of the gross estate as revised for Pennsylvania Inheritance Tax, or the value of the gross estate at date of death as revised for Federal estate tax, or under optional valuation, or the value of the net estate after all assets were sold, debts and expenses and preliminary taxes paid. Where there was a change in book value of the estate through sales, distributions, payments, etc., would each new book value

have to be taken into consideration? Computation of "the rate of return" might even mean that there would have to be a daily appraisement of the corpus during the period of time (often several years) that the interest accrued. In spite of the prohibitive expense, any other method might be considered a compromise and subject to question by the parties-in-interest. It was brought to the attention of the draftsmen that at least one trust company was taking the position under the 1947 Act that there should be charged against income only the rate earned on the specific tax reservation.

It seemed an apppropriate time to simplify the problem and hence the final draft charged interest (and penalties) to Principal, together with the tax itself.

Section 8 repeals Section 11 (4) of the Principal and Income Act of 1947 insofar as it prorates interest on Federal estate tax between Income and Principal.

Attention is directed also to Section 3 (c) which gives the Orphans' Court the right to apportion interest and penalties in a different manner than the tax, in special circumstances.

> "*Section* 3. (*c*) *Separte Apportionment of Interest and Penalties—Special Circumstances.* When the Orphans' Court shall find that it is inequitable to apportion interest and penalties in the same manner as the principal of the estate tax by reason of special circumstances, it may direct apportionment of interest and penalties in a manner different from principal."
>
> "*Section* 4. *Method of Apportionment.*
>
> (*a*) *Basis of Apportionment.* Apportionment of the estate tax, except as provided in Section 3, shall be made among the persons interested in property includible in gross estate in the proportion that the value of the interest of each such person bears to the value of the net estate before exemption. The values used in determining the amount of tax liability shall be used for this purpose."

The draft of November 20, 1950 provided that apportionment was to be made "in the proportion that the value of the interest of each such person bears to the total value of the interests of all such persons". For clarification and simplification the wording was later changed to "——— bears to the value of the net estate before exemption as finally determined for federal estate tax purposes". Then attention was called to the occasional dilemma of having the Federal Government insist that the local courts apportion the tax before it is finally determined, and of having the state courts refusing to apportion until the Federal tax is finally determined. In the final draft the phrase "as finally determined for federal estate tax purposes" was omitted, to avoid emphasis of the difficulties inherently involved as noted above. The wording which was adopted omitting "as finally determined ———" suggests a fluid situation depending on the tax liability negotiated as of any date. There could be an apportionment when the Federal estate tax is originally paid, another if a change in liability is made after audit, a third if liability is

again changed by a post-audit review, and even a fourth apportionment after refund of tax as a result of the honoring of a claim for refund.

> *"Section 4 (b) Treatment of Deductions and Credits.*
> The following principles shall apply with respect to deductions and credits allowable:"
>
> *"Section 4 (b) 1 Deductions allowed by Federal revenue laws in determining the value of decedent's net estate.*
> Any interest for which deduction is allowable under federal revenue laws in determining the value of decedent's net estate such as property passing to or in trust for a surviving spouse and charitable, public or similar gifts or bequests to the extent of the allowed deduction shall not be included in the computation provided in subsection (a) of section four hereof, and to that extent, no apportionment shall be made against such interest, except that when such an interest is subject to a prior present interest which is not allowable as a deduction, the estate tax apportionable against the present interest shall be paid from principal."

For clarification of the effect of a marital or charitable deduction on apportionment, the draft of October 3, 1950 had the following wording: "any deduction allowed under the law imposing the tax by reason of the relationship of any person to the decedent or by reason of the deductibility of a transfer under Internal Revenue Code, Section 812 (d) relating to transfers to or for charities, etc., shall inure to the benefit of the person bearing such relationship or receiving such transfer deductible under Internal Revenue Code, Section 812 (d) as the case may be . . ." The draft of November 1, 1950 worded Section 4(a) 1 as follows: "Relationship or Characted of Recipient. Whenever the interest of any person shall be allowable as a deduction in computing the amount of tax liability, its value shall not be included in the computation provided in Section 4 (a) hereof, and no apportionment shall be made against such interest." A question was raised as to interpretation if the interest of a charity were only partly deductible, and in the draft of November 20, 1950 the words "to the extent of the allowed deduction" were added after "value".

The draft of December 26, 1950 changed the wording to the following:

"Marital and charitable deductions. Property given to a surviving spouse and charitable, public or similar gifts or bequests to the extent of the allowed deduction shall not be included in the computation provided in Section 4 (a) hereof, and to that extent, no apportionment shall be made against such interests. When such an interest is subject to a prior interest which is not allowable as a deduction, the tax apportionable against the present interest shall be paid from Principal". The drafting comment states that this section makes it clear that the surviving spouse would not pay tax on property qualifying for the marital deduction.

In the draft of February 5, 1951, this section was changed to read as follows: "Deductions allowed by Federal Revenue Laws in determining the value of decedent's net estate. Any deduction allowed under Federal Revenue Laws in determining the value of decedent's net estate such as property passing to or in trust for a surviving spouse and charitable, public or similar gifts or bequests to the extent of the allowed deduction shall not be included in the computation provided in Section 4(a) hereof, and to that extent no apportionment shall be made against such interests, except that when such an interest is subject to a prior present interest which is not allowable as a deduction the tax apportionable against the present interest shall be paid from Principal."

In the draft of February 15, 1951, and in S. B. 303 "Any deduction allowed under Federal Revenue Laws" was changed to "Any interest for which deduction is allowable under Federal Revenue Laws"; "no apportionment shall be made against such interests" was changed to "no apportionment shall be made against such interest"; and "the tax apportionable" was changed to "the estate tax apportionable". The drafting comment referred to above in connection with the draft of December 26, 1950 remained unchanged, and it is clear that the revision culminating in the wording of S. B. 303 were solely for the purpose of clarity.

See also notes on Section 4 (b) 4.

"Section 4 (b) 2. Property previously taxed and Gift Tax.

Any deduction for property previously taxed and any credit for gift taxes or taxes of a foreign country paid by the decedent or his estate shall inure to the proportionate benefit of all persons liable to apportionment."

The first draft, of September 13, 1950, provided that "any deduction for property previously taxed and any credit for gift taxes of the decedent shall inure to the benefit of all persons benefited, and the tax to be apportioned shall be the tax after allowance of such deduction and credit".

The second draft inserted "without apportionment of such deduction or credit" after "to the benefit of all persons benefited".

The third draft substituted "without direct credit of such deduction or credit" for "without apportionment of such deduction or credit".

The draft of November 1, 1950 used the wording: "Any deduction for property previously taxed and any credit for gift taxes of the decedent shall inure to the proportionate benefit of all persons liable to apportionment".

The draft of February 5, 1951 used the wording: "Any deduction for property previously taxed and any credit for gift taxes *paid by the decedent or his estate* shall inure———". (Italics supplied).

The draft of February 15, 1951 used the wording: "Any deduction for property S. B. 303: "Any deduction for property previously taxed and any credit for gift taxes *or taxes of a foreign country* paid by the decedent or his estate shall inure

to the proportionate benefit of all persons liable to apportionment". (Italics supplied).

It should be noted here that foreign taxes *paid by the decedent or his estate* are apportionable by this section, i.e. do not act as a direct credit for the payor. However Section 4 (b) (3) provides for a direct credit to the benefit of the payor in respect to "inheritance, succession or estate taxes or taxes in the nature thereof", and this listing does not specifically exclude "taxes of a foreign country". It may be that foreign taxes *paid by the estate* are not direct credits but inure to the benefit of all, while foreign taxes paid from other funds includible in the gross tax estate, such as a revocable trust, are direct credits inuring to the benefit of the payor. If Section 4 (b) (3) is limited to "state taxes" as its heading might indicate, then the statute would be silent as to death taxes of a territory of the United States or the District of Columbia. See also the comments for Section 4 (b) (3).

Tax men in Pennsylvania have from time to time been faced with the problem of applying the credit under the estate tax law for federal gift tax paid on property includible in the gross estate for federal estate tax purposes. There has been doubt as to whether the credit for gift tax is apportionable or is a direct credit to the decedent's testamentary estate, or to the donee of the gift. The problem can be illustrated more clearly by an example. Assume that the decedent, A, during his lifetime made a gift of $100,000. to B and thereby incurred a gift tax liability of $10,000. Assume that the gift was disclosed in the federal estate tax return but not included in the gross estate because not considered to be in contemplation of death. Assume that the agent examining the federal estate tax return sucessfully held that the gift was in contemplation of death and increased the federal estate tax liability from $102,100. to $120,500. after allowing the gift tax of $10,000, as a credit. The net estate before exemption was increased from $450,000. to $550,000. In apportioning the federal estate tax, the executor might take the position that the $10,000. credit for gift tax should act as a credit to the testamentary estate, inasmuch as the decedent depleted his funds by that amount in paying the tax. The executor would charge the donee with federal estate tax of $23,727.27 (100,000/550,000 x 130,500). The donee might take the position that it was the inclusion of his gift in the gross estate that produced his liability for a share of federal estate tax, and that he could not be charged with more than the increase in tax, $18,400. (120,550 - 102,100); or he might argue for apportionment to himself of only $13,727.27 (100,000/550,000 x 130,500, less the $10,000 gift tax credit). Another method would be to apportion the net tax and charge the donee with $21,909.09 (100,000/550,000 x 120,500). In this situation the donee might have to pay as little as $13,727.27 or as much as $23,727.27. In these computations for the sake of simplicity no attention has been paid to apportionment of state death taxes. There are no judicial decisions on record in Pennsylvania as to the proration or the direct crediting of the gift tax credit. The New York courts met the problem in the *Blumenthal Estate* (293 N. Y. 707) and the New York pro-

ration Act of 1950 codified the final decision in the *Blumenthal Estate,* so that "credit for gift taxes paid by the decedent shall inure to the benefit of all persons benefited, and the tax to be apportioned shall be the tax after allowance of such ——— credit". The New Jersey Act of 1950 used similar wording. In summary, then, the new Pennsylvania rule follows New York and New Jersey and eliminates the perplexing problem detailed above.

The deduction for property previously taxed is also to "inure to the proportionate benefit of all persons liable to apportionment". There was some contrary thinking by those who reviewed the early drafts. The thought was expressed that the deduction for property previously taxed should benefit only the particular party or parties who received that property in a manner similar to a marital deduction or charitable deduction. It was decided however to follow the New York and New Jersey rule as the more equitable, as it would be most unusual for a prospective decedent to intend that the recipient of previously taxed property would enjoy a special tax advantage. If he did so intend, he could specify a particular manner of apportionment or nonapportionment in his will or deed of trust. Generally it would not be intended by the average testator that the happenstance of his death *within a certain period of time* should change the tax burden of one class of beneficiaries as compared with another class.

> "*Section* 4 (*b*) 3. *Credit for State Taxes.* Any credit for inheritance, succession or estate taxes or taxes in the nature thereof in respect to property or interests includible in the gross estate shall inure to the benefit of the persons or interests chargeable with the payment of such taxes to the extent or in proportion that the tax paid or payable reduces the estate tax."

To clarify the effect on apportionment of the 80% credit for state death taxes, the draft of October 3, 1950 provided:

> "Any Pennsylvania Inheritance Tax of direct or collateral heirs or transferees or similar tax by another State or Territory of the United States of America or the District of Columbia of property or interest included in the gross estate for estate tax purposes shall inure to the benefit of such persons or funds chargeable with such inheritance tax to the extent or in the proportion that the inheritance tax or similar tax reduces the Pennsylvania or Federal Estate Tax payable; and any discount allowed for prepayment of such inheritance tax shall inure to the persons or the corpus of the fund contributing the moneys used for prepayment in proportion to the contribution made or to be made."

Drafting comments indicate that *Mellon's Estate,* 247 Pa. 520, is construed by some attorneys as applying only to Pennsylvania Estate Tax and the proposed wording would clarify the situation. The Act of 1937 provides for allowances for "exemptions———and deduction" but does not specifically provide for *credits* for state death taxes.

The draft of November 1, 1950 reworded this section as follows: "Credit for state taxes. Any credit allowed for tax paid to a state, territory or possession

of the United States of America or to the District of Columbia in respect to property or interests includible in the gross estate shall inure to the benefit of the persons or interests chargeable with the payment of such tax to the extent or in proportion that the tax paid reduces the estate tax."

Comment was made that the wording limited coverage to taxes paid within the United States, and that coverage should be extended to taxes paid various foreign nations when credits were allowable against federal estate tax by reason of tax treaties. Therefore the draft of December 26, 1950 changed the wording to:

"Credit for State Taxes. Any credit for inheritance, succession or estate taxes or taxes in the nature thereof———."

Also at the end of the section, "Tax paid" was changed to "tax paid or payable".

It may be noted that the introductory heading of the section in S. B. 303 remained as "credit for State Taxes" in spite of the fact that the subsequent wording had been changed so as not to be restricted to states, territories, etc., of the United States of America. The preferred introductory heading would have been "Credit for other death taxes", but it was considered inadvisable to make the correction after the bill had been submitted to the Legislature. The history of the drafting and the intent, as set forth above, may make it clear that "state" in the introductory heading is to be considered as a generic term and to comprehend credits allowable for death taxes paid to foreign nations. But see the notes on Section 4 (b) (2).

There was some criticism directed toward the wording "to the extent or in proportion that". A credit "to the extent" that it reduces federal estate tax might be different from a credit "in proportion that" it reduces the federal tax. Assume an 80% credit of $1,000 for state taxes against federal tax. Assume that a daughter of the decedent received $40,000 and paid Pennsylvania inheritance tax at 2% or $800, and assume that a sister of the decedent received $20,000 and paid Pennsylvania tax at 10% or $2,000. The daughter might claim under the wording "to the extent that", that she should receive credit for the $800 in the apportionment, leaving only $200 for the sister. The sister might claim that the 2% class should not be favored, and inasmuch as the inheritance taxes exceed the credit, the credit should be apportioned under the wording "in proportion that", so that the credits would be computed:

Daughter	800/2800 x 1000 =	285.71
Sister	2000/2800 x 1000 =	714.29
		1000.00

The difficulty is in the use of the disjunctive "or" without detailing the circumstances under which the first part or the second part of the phrase is to govern.

It can be stated that the draftsmen intended "in proportion that" to govern whenever the payments of state taxes exceed the 80% credit. Since Pennsylvania Estate Tax would be assessed where the inheritance tax is less than the 80% federal credit, the writer believes that the words "to the extent or" are surplusage.

> "*Section* 4 (*b*) 4. *Inheritance or Death Tax Effect.* To the extent that property passing to or in trust for a surviving spouse or any charitable, public or similar gift or bequest does not constitute an allowable deduction solely by reason of an inheritance tax or other death tax imposed upon and deductible from such property, it shall not be included in the computation provided for in subsection (a) of section four hereof, and to that extent no apportionment shall be made against such property."

This section was added in the later drafts to supplement Section 4 (b) 1 relating to marital and charitable deductions for federal estate tax, to make it definite that there should be no federal estate tax apportioned to property qualifying for such deductions, merely because inheritance tax was chargeable thereto. Thus if the widow received $1,000,000 as a legacy or by taking against the will of her husband, and Pennsylvania Inheritance Tax reduced her share to $980,000, the latter amount qualifying for the Marital Deduction, there would be no federal estate tax apportioned against the widow for the $20,000 reduction in the Marital Deduction. In other words, this section was added to make sure there would be no need to calculate a tax on tax. The proposed procedure follows the decision in *Morris Estate,* 1 Fid. Rep. 141.

The draft of February 15, 1951 used the words "——— solely by reason of *an inheritance* tax imposed upon———". (Italics supplied). It was suggested that the reference be amplified to take care of various situations, such as an estate administered in Pennsylvania but including real estate in New York upon which a New York *estate* tax might be imposed. Accordingly the final draft refers to "an inheritance tax *or other death tax*" (emphasis supplied).

> "*Section* 5. *Enforcement of Contribution or Exoneration.* (*a*) *Fiduciary's Duty.* The Fiduciary charged with the duty to pay the tax shall be entitled, and it shall be his duty to recover from persons liable to apportionment or from whoever is in possession of property includible in the gross estate not in the fiduciary's possession, the amounts of tax apportionable thereto."

An early draft referred to "The fiduciary charged with the duty to collect and pay the tax". Following through with the idea that apportionment can be accomplished without the necessity of the primary taxpayer actually collecting the tax apportioned to others, the words "collect and" were omitted in the final drafts. Compare the first note for Section 2 above.

> "*Section* 5 (*b*). *Suspending Distribution.* Distribution of property includible in the gross estate to any person other than a fiduciary charged with the duty to pay the tax shall not be required of any fiduciary until

the tax apportionable with respect thereto is paid, or if the tax has not been determined and apportionment made, until adequate security for such payment is furnished to the person making such distribution."

In an early draft, reference was made to "a fiduciary charged with the duty to collect and pay the tax". In the final draft "collect and" was omitted, consistent with the intent of Section 2 and 5 (a) as noted above for those sections.

"*Section* 5 (*c*). *Court Decrees.* The Orphans' Court upon petition or at an accounting or in any appropriate action or proceeding shall make such decrees or orders as it shall deem advisable apportioning the tax. It may also direct a Fiduciary to collect the apportioned amounts from the property or interest in his possession of any persons against whom such apportionment has been made and direct all other persons against whom the tax has been or may be apportioned or from whom any part of the tax may be recovered to make payment of such apportioned amounts to the Fiduciary. When it is ascertained that the Fiduciary holds property of the person liable to apportionment insufficient to satisfy the apportioned tax the Court may direct that the balance of the apportioned amount of tax shall be paid to the Fiduciary by the person liable. Should an overpayment of the tax be made by any person or on his behalf the Court may direct an appropriate reimbursement for the overpayment. If the Fiduciary cannot recover the tax apportioned against a person benefitted such an unrecovered amount shall be charged in such manner as the Orphans' Court may determine."

The primary purpose of the work on the Apportionment Act was to obtain legislation that would permit proration proceedings without the necessity of the executor or administrator actually paying the tax. In the draft of October 3, 1950, the words "or may be required to pay" were added after "Whenever——— (a) fiduciary has paid". The draft of November 1, 1950 altered the wording to "———has paid or is liable to pay". The draft of December 26, 1950 made rather substantial changes in the wording but retained the concept of apportionment without prerequisite of payment through the following:

"liable for payment of estate tax" Section 1 (3).
"shall be apportioned" and "they shall pay" Section 2.
"The fiduciary charged with the duty to pay the tax". Section 5.
"The Orphans' Court upon petition or at an accounting or in any appropriate action or proceeding shall make such decrees or orders as it shall deem advisable tentatively or finally apportioning the tax." Section 5 (c).

S. B. 303 in Section 5 (c) omitted the words "tentatively or finally" after "advisable". This deletion was made as a result of a comment that a court decree could establish the principles of law to be applied without being a final decree as far as the actual figures are concerned. There was some fear that unless the local decree was final the Federal Government might refuse to fix the tax and therefore it would be better not to refer in any instance to a tentative decree. The drafting comments stress the intention to avoid the prerequisite of payment before

initiating apportionment proceedings: "While the exact sum of tax to be apportioned against interested persons must await final assessment of tax *Lucey Est.* 63 D. & C. 645; *Cardeza's Est.,* 51 D. & C. 461), it is contemplated that court decrees may be entered prior to such time, thereby establishing the principles of law to be applied in determining the amount of tax."

The third sentence in an early draft began, "When it is ascertained that property in the hands of the fiduciary of the person liable to apportionment is insufficient———". It was recommended that "insufficient" be explained (insufficient for what?). The final draft therefore reworded this part as follows: "When it is ascertained that the fiduciary holds property of the person liable to apportionment insufficient to satisfy the apportioned tax———". This provision would be needed, for instance where A's will provides a $1,000 legacy to B, but B had received a $50,000 gift from A during A's lifetime, and the gift is held to be in contemplation of death and includible in the gross estate for federal estate tax purposes. If there was no tax clause in A's will covering the legacy or the intervivos gift, and if the tax apportioned to the $51,000 amounted to $15.000, A's executor could apply the $1,000 legacy against the $15,000 share of tax and the Orphans' Court could direct B to pay the balance of $14,000 to A's executor. Query: following the wording in Sections 2 and 5 (a), would it not have been consistent to require B merely to "pay" the $14,000 (to the Collector, for instance), rather than to provide that the "balance———shall be paid *to the fiduciary*" (emphasis supplied)?

The early drafts provided that "When an apportionment is made, there shall be no distinction between residents and nonresidents of the Comonwealth". However it was recognized that there could be difficulties in enforcing the act insofar as persons and assets located outside the Commonwealth might be concerned. Therefore the wording above was omitted, but provision for a practical solution was made by the sentence, "If the fiduciary cannot recover the tax apportioned against a person benefitted, such an unrecovered amount shall be charged in such manner as the Orphans' Court may determine". The quoted sentence is not however limited in its application to persons or assets outside the Commonwealth. It could be applied, for instance, where a "person benefitted" has spent or otherwise disposed of the benefit and has no other assets available to pay the share of tax.

> "*Section 6. Severability.* If any provision of this Act or the application thereof to any person or circumstances is held invalid, the remainder of this Act and the application of such provision to other persons or circumstances shall not be affected thereby, and to this end the provisions of this Act are declared to be severable."
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> "*Section 7. Short Title.* This Act shall be known and may be cited as the Estate Tax Apportionment Act of 1951."
>
> "*Section 8. Repeals.* Section 48.1 of the Act approved June 7, 1917 (Pamphlet Laws 447) entitled as amended "An act relating to the

administration and distribution of the estates of decedents and of minors and of trust estates including the appointment, bonds, rights, powers, duties, liabilities, accounts, discharge and removal of executors, administrators, guardians and trustees herein designated as fiduciaries, the administration and distribution of the estates of presumed decedents, widow's and children's exemptions, debts of decedents, rents of real estate as assets for payment thereof, the lien thereof, sales and mortgages of real estate for the payment thereof, judgments and executions therefor, and the discharge of real estate from the lien thereof, contracts of decedents for the sale or purchase of real estate legacies including legacies charged on land, the discharge of residuary estates and of real estate from the lien of legacies and other charges, the appraisement of real estate devised at a valuation, the ascertainment of the curtilage of dwelling houses or other buildings devised, the abatement and survival of actions and the substitution of executors and administrators therein, the survival of causes of action and suits thereupon, by or against fiduciaries, investments by fiduciaries, the organization of corporations to carry on the business of decedents, the audit and review of accounts of fiduciaries, refunding bonds, transcripts to the court of common pleas of balances due by fiduciaries, the rights, powers and liabilities of nonresident and foreign fiduciaries, the appointment, bonds, rights, powers, duties and liabilities of trustees *durante absentia,* the recording and registration of decrees, reports and other proceedings and the fees therefore, appeals in certain cases, and also generally dealing with the jurisdiction powers and procedure of the Orphans' Court in all matters relating to fiduciaries concerned with the estate of decedents", as added by the act approved July 2, 1937 (Pamphlet Laws 2762) is hereby repealed.

Subsection four of Section eleven of the act approved July 3, 1947 (Pamphlet Laws 1283) entitled "An act concerning the ascertainment of principal and income and the apportionment of receipts and expenses among tenants and remaindermen" is hereby repealed insofar as it is inconsistent with the provisions of this act.

All other acts and parts of acts are hereby repealed insofar as they are inconsistent with the provisions of this act."
See next to last paragraph of notes on Section 3 (b).

"*Section* 9. *Effective Date.* The provisions of this act shall become effective immediately upon final enactment and shall apply to the apportionment of estate taxes with respect to any estate for which the original Federal estate tax return is filed thereafter regardless of when the decedent died."

The effective date to be proposed for the new act was the subject of some deliberation. The first draft was worded for the new law to take effect "upon enactment thereof" and to be applicable "to the estates of all persons dying on or after such date". Draft 3 changed the effective date to September 1, 1951, in order to afford an opportunity to revise tax clauses and to give the Bar and tax practitioners the opportunity to become conversant with the new Act before it actually became effective. The draft of November 1, 1950 used wording similar

to that of the first draft, "shall take effect upon final enactment". The draft of December 26, 1950 would have made the new Act "effective upon the enactment thereof" to apply to "the apportionment of estate taxes thereafter paid, regardless of when the decedent died". This last phraseology might have caused confusion where the original tax was paid before the effective date of the new Act, and a deficiency was paid after the effective date. The draft of February 5, 1951 made its provisions effective upon enactment and applicable to "any estate in which the Federal return is filed thereafter, regardless of when the decedent died". It was pointed out that this wording might grant an unintended opportunity for finesse, if the original return was filed before the effective date and an amended return filed after the effective date. So the final draft provided that the new law should be applicable where the original Federal estate tax return is filed after the effective date of the new Apportionment Act. It is possible that there may be instances where an executor, knowing of the Bill, may have obtained an extension of time for filing the return, to bring the estate under the new Apportionment Act.

John E. Williams, Trust Tax Officer

Provident Trust Company of Philadelphia