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TEXAS DEATH TAXES AND ESTATE PLANNING

by
Herbert S. Kendrick*

A PERSON attempting to minimize the tax assessment on the devolution of his estate must necessarily consider the state tax liability as well as the federal tax assessment. In Texas, the absence of a state income or gift tax restricts the scope of an examination to death taxes. Hence, this Article will review in detail the Texas death taxes which are important to any estate plan.

The Texas Legislature has enacted both an inheritance$1 and an estate$2 tax to be levied on property passing at death. In distinguishing between inheritance and estate taxes, it should be remembered that an inheritance tax is assessed on the right of succession to property,$\text{4}$ while an estate tax is imposed on the right of the grantor to transfer property.$5$ To the extent that state taxes bear directly upon estate planning decisions, the inheritance tax is primarily important. The Texas estate tax is assessed only to assure the maximum credit permitted for payment of state death taxes in computing the federal estate tax liability$6$ and is seldom of any consequence in estate planning decisions.$7$ Therefore, the subsequent analysis shall essentially be restricted to an examination of the Texas inheritance tax and its impact on an estate plan.

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2 Tex. Tax—Gen. Ann. art. 15.01 (1959). Though this tax is labeled an "Additional Inheritance Tax" by the statute, it is an estate tax by definition and for purposes of this Article will be classified as an estate tax. See Strauss v. Calvert, 246 S.W.2d 287 (Tex. Civ. App. 1952—Austin) error ref. n.r.e.
3 Knowlton v. Moore, 178 U.S. 41 (1900); State v. Hogg, 123 Tex. 568, 72 S.W.2d 593 (1934).
6 For a situation when the Texas estate tax is an important consideration see note 150, infra.

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I. Problems of the Gross Estate

A. Powers Of Appointment

A power of appointment is important in the consideration of any estate plan. Through the proper employment of such a power, otherwise unavailable flexibility may be obtained. The proper utilization of a power of appointment requires decisions concerning the creation of powers as well as the possible exercise of powers already possessed by the person whose estate is being planned.

In Texas an inheritance tax is assessed on property passing under a general power of appointment exercised by the decedent in a will. Therefore it is necessary to distinguish between a general and a special power of appointment. Any power classified as a special power, or any power, general or special, exercised by the donee inter vivos, will not be subject to a Texas tax.

For example, suppose A transfers property in trust with the income to B for life, then to such person or persons as B may appoint inter vivos or by will, and in default of appointment, the property shall pass equally to C's children. In an estate plan involving the property of B, only compelling reasons should prevent an inter vivos exercise of the power. Thus, the Texas inheritance tax could possibly

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2 Since this Article deals with estate planning the following discussion will be in relation to powers created after October 21, 1942. See Int. Rev. Code of 1954, § 2041(a)(2). For the provision relating to powers created on or before October 21, 1942, see Int. Rev. Code of 1954, § 2041(a)(1).

3 A power of appointment is a power created or reserved by a person (the donor) having property subject to his disposition enabling the donee of the power to designate, within such limits as the donor may prescribe, the transferees of the property or the shares in which it shall be received.

The term, power of appointment, does not include a power of sale, a power of attorney, a power of revocation, a power to cause a gift of income to be augmented out of principal, a power to designate charities, a charitable trust, a discretionary trust, or an honorary trust. See Republic Nat'l Bank v. Fredericks, 155 Tex. 79, 283 S.W.2d 39 (1955); see also Restatement, Property § 318 (1940).


10 Ibid.

11 Tex. Tax—Gen. Ann. art. 14.01 (1959) provides for the inheritance tax to be assessed on "All property . . . including property passing under a general power of appointment exercised by the decedent by will . . ." (Emphasis added.)

12 A power is general if, being exercisable before the death of the donee, it can be wholly in favor of the donee or, being testamentary, it can be exercised wholly in favor of the estate of the donee. Restatement, Property § 320(1) (1940).

13 A power is special if it can be exercised only in favor of persons, not including the donee, who constitute a group not unreasonably large and the donor does not manifest an intent to create or reserve the power primarily for the benefit of the donee. Restatement, Property § 320(2) (1940).

14 See Sheppard v. Desmond, 169 S.W.2d 788 (Tex. Civ. App. 1943—Austin) no writ hist. Of course an inheritance tax will be imposed on the property if it is deemed a transfer intended to take effect in possession or enjoyment after the death of the grantor or it is found to be a transfer made in contemplation of death within the meaning of the statute. See Tex. Tax—Gen. Ann. art. 14.01 (1979).
affect any decision regarding the exercise of a general power. Indeed, under certain circumstances the inheritance tax on the testamentary exercise of a general power may be greater than the federal gift tax on an inter vivos exercise of that power. Also, in the creation as well as the exercise of a general power, inter vivos disposition of the property should not be dismissed without careful consideration. Flexibility in the estate plan is more readily ascertained with an inter vivos power, and the inheritance tax advantage is apparent.

An additional consideration in the creation or exercise of a general power of appointment is the passing of the property in default of appointment. Since the Texas inheritance tax is assessed only upon an "exercise" of a general power by will, the donee of such a power should not exercise the power if the takers in default of appointment consist of persons whom the donee wishes to benefit. Furthermore, if the gift in default of appointment meets the donee's approval, no inter vivos gifts should consist of property subject to the power; in such a situation the donee will not incur a Texas tax on property transferred inter vivos, and the property passing in default of appointment will not be subject to the inheritance tax. By prudent planning, the donee of the power may thus avoid payment of any taxes in transferring the property. Therefore, the possibility

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16 Suppose A is made the income beneficiary of a trust for life with a general power over the trust corpus exercisable either by inter vivos or testamentary dispositions and with a gift in default of appointment to X. The value of the property is $100,000. A testamentary exercise of the power to A's wife will permit an inheritance tax assessment of $1,250. See Tex. Tax—Gen. Ann. art. 14.02 (1959). The federal gift tax (after applying the gift tax marital deduction, specific exemption, and annual exclusion) upon an inter vivos exercise of the power, however, will be only $912. See Int. Rev. Code of 1954, §§ 2502-23.

17 Suppose A is the life beneficiary of a trust with a general power over the corpus; in default of appointment the property will pass to A's children. This case presents a classical situation wherein the donee of the power, A, should permit the property to pass in default of appointment and thereby avoid the Texas inheritance tax. See Tex. Tax—Gen. Ann. art. 14.01 (1959).

18 It is assumed that the transfer is not intended to take effect in possession or enjoyment at or after death of the donee, nor is the transfer one in contemplation of death, since in both instances the inheritance tax would be assessed. See Tex. Tax—Gen. Ann. art. 14.01 (1959).

19 For example, W, a widow, has property valued at $200,000 and a life interest with a general power of appointment in a $200,000 trust created by her husband, H. The corpus of the trust passes to the children of H and W upon default of appointment of the property. W institutes an inter vivos gift program to pass one-half the property, $200,000, to the children during her life. By utilizing property outside the trust to make the inter vivos gifts, no Texas tax is imposed on the inter vivos transfers; furthermore, there will be no inheritance tax on the passing of the $200,000 in default of appointment. See Tex. Tax—Gen. Ann. art. 14.01 (1959). The federal estate and gift taxes will be the same, irrespective of what property is transferred inter vivos by W.
of allowing the property to pass in default of appointment should be utilized unless other factors override the tax advantage.\(^2\)

Whenever an estate plan calls for the property subject to a power to pass in default of appointment, a provision in the donee’s will should specifically negate any intention to exercise the power.\(^3\) Though the Texas rule requires that the intent to exercise a power be so clear that no other reasonable intent may be imputed under the will,\(^4\) the uncertainty in determining a testator’s intent suggests that a specific provision rejecting the exercise of the power will not be superfluous.

The Texas case of \textit{Calvert v. Thompson}\(^5\) appears to justify a devise or bequest of a life estate with a general power of appointment in every case in which an absolute gift is contemplated. In that case the court refused to consider an unlimited power of invasion possessed by a life tenant in assessing the inheritance tax, but the basis of the tax assessment was held to be the value of the life interest and the remainder without reference to the power.\(^6\) As in the case of a life tenant with a power of invasion, it has long been the Texas rule that a life estate is not enlarged because it is coupled with a general power of appointment.\(^7\) Therefore, the creation of a general power of appointment should not only permit the property to pass in default of appointment by the donee without being subject to inheritance tax, but the power should reduce the Texas in-

\(^1\) For a discussion of the question concerning whether to exercise a power of appointment, see Casner, \textit{op. cit. supra} note 9, at 699.
\(^2\) Casner, \textit{op. cit. supra} note 9, at 695.
\(^3\) Republic Nat’l Bank v. Fredericks, 135 Tex. 79, 283 S.W.2d 39 (1955). The court, in deciding whether or not a power had been exercised, stated:

The tests are (1) where there is a reference to the power in the instrument; (2) where there is a reference to the property on which it is subject to be executed; and (3) where the provisions of the will or deed executed by the donee would otherwise be ineffectual; i.e., would have no operation except as an execution of the power.

The general rule is that in order for a will or deed to constitute the exercise of a power of appointment the intent to exercise such power must be so clear that no other reasonable intent can be imputed under the will. The will must refer to the power of appointment or to the property subject to such power, or the donee of the power must have owned no other property to which the will could have attached and thus the will have been a vain and useless thing except it be held to be an exercise of the power. (Citations omitted.) . . . If, from the circumstances or the instrument executed, it be doubtful as to whether it was the intention to execute the power possessed by the grantor, then it will not be held that by such act or conveyance that power was in fact executed. Hill v. Conrad, 91 Tex. 341, 43 S.W. 789 (1897). 155 Tex. at 89-90, 283 S.W.2d at 47.
\(^4\) 155 S.W.2d 683 (Tex. Civ. App. 1960—Austin) \textit{error ref}.
\(^5\) Id., at 688.
inheritance tax at the death of the donor without reducing the donee's control of the property.\footnote{37}

**B. Future Interests**

The creation of a future interest is a useful device in any attempt to reduce inheritance taxes. When property subject to imposition of the tax passes divided into two or more estates, each estate is taxed separately and according to its value at the death of the decedent.\footnote{38} Thus, if a testator dies leaving a life estate in his widow, remainder in their two children, the transfer will receive the statutory exemption\footnote{39} upon the life estate of the widow as well as the exemption on the remainder interest in each child.\footnote{40} Of course, it is normally undesirable in an estate plan to create a future interest that may pass through the estate of a deceased person while it is still a future interest.\footnote{41}

*Calvert v. Thompson*\footnote{42} may also avail a taxpayer of previously denied inheritance tax benefits through prudent estate planning. In that case the testator devised and bequeathed all his property to his wife for life with full power to sell or otherwise to dispose of the property. At the death of the wife the remainder of the property was to pass equally to their two children in fee simple. The court held that the power of disposal given the life tenant did not change the estate to something other than a life estate.\footnote{43} In addition, the trial court was

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\footnote{37} Apparently the inheritance tax saving available under the *Thompson* case is limited only by the tax assessed against the life estate. For example, a devise of a life estate with a general power of appointment (or general power of sale or disposition) coupled with a remainder to a qualified charity would be taxed only on the life estate interest, the remainder being exempt because of the qualified charity. The life tenant could then exercise the power and prohibit the charity from ever receiving the property, even though the remainder was not subject to inheritance tax upon the testator's death. If the power is exercised inter vivos or is a special power, no Texas tax will ever be assessed on the remainder.

\footnote{38} *Tex. Tax—Gen. Ann. art. 14.08 (1959):* If the property passing as aforesaid shall be divided into two or more estates, as an estate for years or for life and a remainder, the tax shall be levied on each estate or interest separately, according to the value of the same at the death of the decedent. The value of estates for years, estates for life, remainders, and annuities shall be determined by the "Actuaries Combined Experience Tables," at four per cent compound interest.


\footnote{40} *Casner, op. cit. supra note 9, at 436.*

\footnote{41} 339 S.W.2d 685 (Tex. Civ. App. 1960—Austin) error ref.; see note 27 supra and accompanying text.

\footnote{42} By reaching this decision the court, relying on *Weir v. Smith*, 62 Tex. 1 (1884), stated the general rule that if a particular estate is expressly created with a general power of disposition to the person to whom such estate is given, then the power will not enlarge the estate given. Furthermore, the court quotes with approval Edds v. Mitchell, 143 Tex. 307, 184 S.W.2d 823 (1945), where the Texas Supreme Court said:

The power of disposition is not an estate. It is merely authority derived from the will to dispose of the fee. It is not repugnant to an estate for life.
sustained in its computation of the inheritance tax without regard to the power possessed by the life tenant. This latter holding completely repudiates the policy of assessing the inheritance tax according to the most probable disposition of the estate by the life tenant. Instead, it establishes the requirement of valuing each estate or interest at the death of the decedent, irrespective of any power possessed by one of the parties. Therefore, a devise of a life estate with a power and remainder over can be used to reduce the inheritance taxes without hindering the use of the property by the life tenant.

Prior to Thompson the Attorney General had classified all remainders, vested and contingent, as "uncertain future interests," and the inheritance tax had been assessed according to the probability that the particular interest would eventually come into the possession and enjoyment of the beneficiary. However, the broad language of the Thompson case should be interpreted as a rejection of any method of computing the inheritance tax other than the method set forth in the statute. The statutory language is "clear and unambiguous" in requiring a valuation of the estates and interests in the property at the date of the decedent's death. The holdings of both Thompson and

34 The "most probable future disposition" test permitted the disregard of the remainder interests in the computation of the inheritance tax due. Thus, the life tenant could be taxed on the entire value of the property if the "most probable future disposition" would be found to be an exercise of the power. For example, testator devised all of his property valued at $100,000 to his wife for life, and the wife had full power to sell, convey, and dispose of the property; upon death of the wife any property that remained in her possession should pass to their daughter. The "most probable future disposition" test would permit the entire value of the property to be taxed as though it passed to the wife in fee. See Ops. Tex. Att'y Gen. No. 0-2351 (July 25, 1940).

35 The court stated:
The statute . . . is plain in providing the method for determining the value of estates for life and remainders and any other method of determining such values would violate the statute.

36 Appellants urge us to accept opinions of the Attorney General and departmental construction of [art. 14.08] as to the proper method of computing inheritance taxes which are contrary to what we have said. There is no ambiguity in the statute but the ambiguity arises if at all because of the power of disposition granted to the life tenant. The effect of this power has been determined by our Supreme Court and the opinions of the Attorney General and departmental construction must yield. 339 S.W.2d at 688.

37 The testator left property in trust for the lives of her two sisters with the remainder in a nephew. If the nephew did not survive the two life tenants the property was to pass to a tax exempt charity. The Attorney General held that the inheritance tax was to be assessed on the basis of the happening of the "most probable contingency" and disregarded the charity. Ops. Tex. Att'y Gen. No. 0-4751 (Aug. 26, 1942).


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the Attorney General are consistent only in that they disregard common law distinctions among remainders in the determination of the tax.

The use of future interests in an estate plan may be the most significant device in the reduction of inheritance taxes without suffering adverse consequences in the federal estate tax assessment. Since the exemptions available under the Texas statute are not affected because the future interest created is contingent, and the tax is assessed without regard to the contingency, the use of such future interests will not only permit a reduction in the inheritance taxes on the passing of the donor's estate but will also avoid any inheritance tax consequences on the passing of the life beneficiary's estate. The division of the property among several beneficiaries will permit additional exemptions which normally reduce the inheritance tax assessment.

C. Life Insurance

The Texas inheritance tax is imposed on all insurance proceeds taken out by the decedent on his own life with the exception of a forty thousand dollar exemption for policies payable to named beneficiaries.

The Texas Supreme Court has held that where life insurance is taken out by a husband on his own life, the premiums are paid from the community estate, and the wife is beneficiary of the insurance, only one-half of such insurance proceeds, less the statutory exemption, will be subject to the inheritance tax on the death of the insured. This result has been extended by the Attorney General to situations where the beneficiary is not the wife, but a third party. Similarly, it has been held that the estate of a deceased wife includes one-half of the cash surrender value of a policy on her husband's life if the insured husband survives his wife, the premiums are paid

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41 Suppose the testator devised his property in trust for his wife for life, remainder to his children who attain twenty-one years. It is submitted that this basic situation can reduce the assessment of inheritance tax at the testator's death and yet the property will not be in his children's gross estate if death should come prior to their twenty-first birthday. The contingency of the children's interest will not prohibit the reduction of the inheritance tax by dividing the estate with the contingent remainders.
All property within the jurisdiction of this state . . . including the proceeds of life insurance to the extent of the amount receivable by the executor or administrator as insurance under policies taken out by the decedent upon his own life, and to the extent of the excess over Forty Thousand ($40,000) Dollars of the amount received by all other beneficiaries as insurance under policies taken out by the decedent upon his own life . . .
43 Blackman v. Hansen, 140 Tex. 536, 169 S.W.2d 962 (1943).
from community funds, and the policy is acquired during marriage. These interpretations emphasize the basic question in considering life insurance, namely, when is life insurance "taken out by the decedent upon his own life" within the meaning of the Texas inheritance tax statute?

The Texas life insurance provision (in regard to inheritance taxes) is based on the federal statute in effect in 1939. It has long been the Texas rule to presume that the Texas Legislature knows of the construction given a statute at the time of its adoption and that it intends to adopt the statute as construed by the federal and state courts. Therefore, the interpretation of the federal statute in Lang v. Commissioner is of particular significance.

That case involved a life insurance contract which had been purchased with community funds and which gave the decedent-insured power to change the beneficiary at any time. Under the applicable state law, as in Texas, such contracts were community property whose character the insured could not alter by changing the beneficiary. The Court assessed the tax only on the portion of the proceeds that were purchased by premiums from the decedent’s property; thus, only one-half the proceeds were includable in the decedent’s estate. In determining what constitutes a policy “taken out by the decedent,” the Court reasoned that Congress had not intended that proceeds of insurance policies bought and paid for with funds of a person other than the insured and not payable to the insured’s estate,

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42 Calvert v. Thompson, 301 S.W.2d 496 (Tex. Civ. App. 1957—Austin) no writ hist.
43 In an opinion controlled by this case the Attorney General ruled that where a decedent willed the residue of her estate to three named beneficiaries, for inheritance tax purposes the decedent’s one-half community interest in the cash surrender value of certain insurance policies on the surviving spouse’s life passed to the beneficiaries and the inheritance taxes should be computed accordingly. Ops. Tex. Att’y Gen. No. WW-446 (June 6, 1958).
45 Revenue Act of 1926, ch. 27, § 302(g), 44 Stat. 9, provided:
   The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property . . .
   (g) Proceeds of life insurance.—To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life and to the extent of the excess over $40,000 of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life.
46 Blackman v. Hansen, 140 Tex. 536, 169 S.W.2d 962 (1943); Board of Water Eng’rs v. McKnight, 111 Tex. 82, 229 S.W. 101 (1921); City of Tyler v. St. Louis Ry., 99 Tex. 491, 91 S.W. 1 (1906); Brothers v. Mundell, Mungesheimer & Co., 60 Tex. 240 (1884).
47 304 U.S. 264 (1938).
48 In Blackman v. Hansen, 140 Tex. 536, 169 S.W.2d 962 (1943), the supreme court held that the proceeds of a life insurance policy taken out by the husband and payable to the estate of the decedent, the premiums of which were paid for with community funds, are one-half the property of the wife and that that portion is no part of the estate of the husband.
would be considered as part of the decedent's estate for purposes of taxation.\textsuperscript{51}

The Texas Supreme Court expressly approved this decision in an interpretation of the inheritance tax statute in \textit{Blackman v. Hansen}.\textsuperscript{52} Furthermore, the Attorney General, following the \textit{Lang} and \textit{Blackman} cases, has ruled that "taken out by the decedent" means the expenditure of the decedent's funds.\textsuperscript{53}

These decisions indicate that the maximum benefit from the assignment of an insurance policy can be obtained only when the premium payments are made by someone other than the insured. Although this problem is easily solved when the third party beneficiary has separate property from which to make the premium payments, a more difficult situation is presented when the beneficiaries of the policy are the spouse or minor children of the insured who have no separate property. In the situation of the spouse serious consideration should be given the possibility of partitioning a portion of the community property,\textsuperscript{54} thereby permitting the wife to make the premium payments from her separate estate. The partition will cause no adverse federal tax consequences, and since the premiums are all paid by the wife's separate estate, she will avoid the inheritance tax assessment.

\textsuperscript{51} The Supreme Court also relied on Treasury Regulations promulgated under the Revenue Act of 1926. The Court stated:

\textit{Art. 25} . . . .

The term "insurance" refers to life insurance of every description . . . . Insurance is deemed to be taken out by the decedent in all cases where he pays all the premiums, either directly or indirectly, whether or not he makes the application. On the other hand, the insurance is not deemed taken out by the decedent, even though the application is made by him, where all the premiums are actually paid by the beneficiary; where a portion of the premiums were paid by the beneficiary and the remaining portion by the decedent the insurance will be deemed to have been taken out by the latter in the proportion that the premiums paid by him bear to the total of premiums paid.

\textit{Art. 28}.

The amount to be returned where the policy is payable to or for the benefit of the estate is the amount receivable. Where proceeds of a policy are payable to a beneficiary other than to or for the benefit of the estate, and all the premiums were paid by the decedent, the amount to be listed on Schedule C of the return is the full amount receivable, but where the proceeds are so payable and only a portion of the premiums were paid by the decedent, the amount to be listed on such schedule is that proportion of the insurance receivable which the premiums paid by the decedent bears to the total premiums paid . . . . 304 U.S. at 269.

\textsuperscript{52} 140 Tex. 536, 540, 169 S.W.2d 962, 964. The supreme court stated:

Before the 1939 amendment of [art. 14.01] the Federal statute had been construed by the United States Supreme Court in \textit{Lang v. Commissioner of Internal Revenue} . . . . That was the construction of the Federal statute at the time of its adoption by the Legislature of this State.

\textsuperscript{53} 5 Ops. Tex. Att'y Gen. No. 0-5211 (May 15, 1943).

upon the death of her husband. This follows from the Lang and Blackman cases in that the policies are not “taken out by the decedent.” Moreover, when the assignment of a policy is to the children (or any third party) the insured may make an outright gift of funds to the beneficiary (and such funds becoming the separate property of the beneficiary would be used to make the premium payments) or possibly arrange for a trust to make the premium payments.

The method in which the inheritance tax is assessed on life insurance proceeds is an important consideration in deciding the question of whether to assign a policy to a third party. In the situation where the life insurance premiums have been paid with community funds and the proceeds are payable to a third party beneficiary, upon the death of the insured, only one-half of the proceeds is included in the insured-decedent’s gross estate. The remaining one-half of the proceeds will be subject to the federal gift tax, as a gift from the surviving spouse to the third party beneficiary. However, if an assignment is made of the policy before the insured’s death, instead of the federal gift tax being assessed on the face value of the policy at the time of the death of the insured, the tax will be assessed on one-half the cash surrender value of the policy at the time of the inter vivos transfer. Thus, such an assignment represents an important potential method of lessening taxes at death.

D. Annuities And Employee Death Benefits

The federal estate tax provision regarding employee death benefits has no counterpart in the Texas statute. Consequently, such benefits in Texas probably will be taxed as a transfer “made or intended to take effect in possession and enjoyment after the death of the grantor or donor.” The assessment of the Texas tax under this provision eliminates most, if not all, of the distinctions and factors in determining taxability under the federal estate tax. Although no Texas court has ruled on the matter, in most jurisdictions assessing an inheritance tax it has been uniformly held that retirement and pension

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88 Should the beneficiary spouse predecease the insured, the cash surrender value of the policy will be subject to the inheritance tax. However, it is submitted that the reduction in the inheritance tax will justify the inclusion. It will be remembered that if the premiums are paid with community funds and the beneficiary spouse survives the insured, one-half of the cash surrender value will be subject to the Texas tax. See Calvert v. Thompson, 301 S.W.2d 996 (Tex. Civ. App. 1947-Austin) no writ hist.
89 See notes 49, 52 supra and accompanying text.
plan annuities, as well as benefits from employee profit sharing plans, are subject to the tax. The courts reason that the shifting of the economic benefits at the death of the transferor sustains the imposition of the tax as a "transfer intended to take effect . . . after the death of the grantor or donor."

The Texas Attorney General has consistently ruled, with one exception, that employee death benefits are subject to the inheritance tax. The basic standard used in each ruling seems to be the control of the decedent over the property at the time of his death. The most enlightening interpretation of the taxability of survivorship benefits under the Texas statute involved a ruling on an employee pension plan where the bulk of the benefits were directly financed through the purchase of annuity contracts from insurance companies. In taxing the benefits under the plan the controlling factor apparently was the power of the decedent at the time of his death to change the beneficiary. The Attorney General also ruled that an employer's con-

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62 In assessing the inheritance tax, the courts have relied on the provision taxing transfers "intended to take effect in possession or enjoyment at or after death." In regards to profit sharing funds, see In re Brackett's Estate, 342 Mich. 195, 69 N.W.2d 164 (1955). In regards to annuity contracts, see Dolak v. Sullivan, 145 Conn. 497, 144 A.2d 312 (1958); Borchard v. Connelly, 140 Conn. 491, 101 A.2d 497 (1953); Cruthers v. Neeld, 14 N.J. 497, 103 A.2d 113 (1954). Contra, In re Wilson's Estate, 143 Misc. 742, 217 N.Y. Supp. 230 (Surr. Ct. 1931).

63 The so-called "economic benefits" theory is based on the apparent intent of the Legislature to tax the shifting of the enjoyment of property—the "economic benefits"—from a former owner at his death, even though such shifting of enjoyment followed necessarily from a prior inter vivos transfer of title. See In re Brackett's Estate, supra note 62; Borchard v. Connelly, supra note 62.

64 This exception pertained to the lump sum death payment of a widow under the Social Security Act. In holding such a payment not to be a "transfer intended to take effect in possession or enjoyment after the death of the grantor or donor," the Attorney General stated: The covered employee having no choice in the matter of coverage, nor in the selection of beneficiaries, nor indeed any assurance that either he or anyone else will ever receive any Social Security benefits, can scarcely be said to have made a gift intended to take effect in possession or enjoyment after death. Ops. Tex. Att'y Gen. No. WW-698 (Sept. 9, 1959).

65 The following benefits have been expressly ruled subject to tax: (1) death benefits under the Teachers' Retirement System, Ops. Tex. Att'y Gen. No. WW-92 (Oct. 17, 1957); (2) Series E United States Government Bonds, Ops. Tex. Att'y Gen. No. 0-7495 (Dec. 17, 1946); (3) the portion of a widow's annuity which is attributable to the decedent's contributions to the Civil Service Retirement and Disability Fund, Ops. Tex. Att'y Gen. No. WW-698 (Sept. 9, 1959).

66 After holding that the "transfer intended to take effect in possession or enjoyment after death of grantor" provision was applicable, the opinion stated: In the present case, at the time of his death the decedent had a vested right to at least 120 monthly retirement benefits. We regard as immaterial the fact that this right had not vested at the time he designated the beneficiary. He could have changed that designation at any time after the interest in question vested. We think his failure to do so constituted an effective gift intended to take effect at his death. Moreover, we do not think the nature of the interest as vested or con-
tribution to the plan would be treated as an additional compensation, thereby subjecting only one-half of the pension benefits to the inheritance tax. 68

The broad language used by the courts and the Attorney General in deciding the taxability of survivorship benefits indicates that the inheritance tax will be assessed in almost every instance, although unusual circumstances may cause a relaxing of the rule. In those situations where the annuitant or employee can irrevocably assign a present interest in the enjoyment and possession of the benefits, the tax can effectively be avoided. 69 Usually, however, the inheritance tax considerations with respect to annuities will yield to policies directed at securing the advantages of the federal estate tax. 70

In those instances where the employee death benefits consist of group life insurance proceeds, the previously mentioned considerations pertaining to life insurance should be examined. 71 Of course, it should be noted that an annuity contract is not the same as an insurance contract in Texas 72 and that annuity proceeds do not come within the provision "proceeds of life insurance" in the inheritance tax statute. Therefore, the life insurance exemption is unavailable to such proceeds. 73

E. Trusts

Through proper utilization of the trust device, significant advantages may be attained in both the federal income 74 and estate 75 tax assessments. However, the basic distinction between the estate tax and the inheritance tax permits the imposition of the state inheritance tax even though the estate plan has successfully avoided

69 The test is always whether the property comes into possession and enjoyment of the transferee upon the death of the transferor. If the death of the transferor makes no difference on the rights of the parties there is no tax. See In re Brackett's Estate, 342 Mich. 111, 69 N.W.2d 164 (1951); cf. Bethea v. Sheppard, 143 S.W.2d 997 (Tex. Civ. App. 1940—Austin) error ref. see Int. Rev. Code of 1954, § 2039.
70 See note 48 supra and accompanying text.
71 In Daniel v. Life Ins. Co. of Va., 102 S.W.2d 216, 260 (Tex. Civ. App. 1937—Austin) no will bint, the court reasoned that an annuity contract is essentially a form of investment and lacks the character of "risk which is connected with the business of writing insurance."
the federal estate tax.77 It is in this area of taxation that the Texas statute78 has a much greater scope than its federal counterpart.79

A common situation arises when there is an inter vivos transfer in which the transferor parts with all rights of enjoyment, reversion, or revocation.80 Except in the case of an absolute gift, these transfers normally take the form of an irrevocable trust. Although such a conveyance may be effective to escape the federal estate tax,81 the Texas courts,82 consistent with other jurisdictions,83 have imposed the inheritance tax on these transfers under certain circumstances.

The leading Texas case, Bethea v. Sheppard,84 involved a joint will and trust agreement covering the entire community estate. Upon the husband’s death an irrevocable trust with an income interest and certain powers to invade the corpus was established naming the surviving wife and daughter as beneficiaries. The daughter was the ultimate beneficiary of the trust, provided she survive the death of the surviving spouse by eight years. Texas inheritance taxes were paid on the husband’s one-half of the community estate. Upon the death of the surviving wife, the daughter contested the assessment of the inheritance tax on the surviving spouse’s one-half interest of the community estate. In assessing the tax on the interest, the court held that the transfer of the property was within that provision of the Texas statute which assessed a tax on the passing of property intended to take effect in possession or enjoyment after the death of the donor.85

Although the decision is apparently based on the contingency that the ultimate beneficiary will survive the settlor, the broad language

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80 See Brink, Minnesota Inheritance Tax: Some Problems and Solutions, 43 Minn. L. Rev. 443, 466 (1959).
83 State St. Trust Co. v. Stevens, 209 Mass. 373, 5 N.E. 851 (1911); Chase v. Commissioner of Taxation, 226 Minn. 321, 33 N.W.2d 706 (1948); In re Holland’s Estate, 123 N.J. Eq. 52, 195 Atl. 805 (Ch. 1938). Contra, In re Heine’s Estate, 100 N.E.2d 545 (Ohio P. Ct. 1950).
84 143 S.W.2d 997 (Tex. Civ. App. 1940—Austin) error ref.

All property . . . and any interest therein which shall pass absolutely or in trust by will or by the laws of descent or distribution . . ., or by deed, grant, sale, or gift made or intended to take effect in possession or enjoyment after the death of the grantor or donor. . . (Emphasis added.)
of the court indicates a wide application of the provision. According to this interpretation any interest in the possession or enjoyment of property that becomes effective in the transferee at the transferor's death will be subject to tax. Furthermore, in addition to the Bethea v. Sheppard situation, it seems clear that at least two other types of irrevocable inter vivos trusts will be held taxable. The first such trust involves a transfer in which the settlor has retained the right to income. The other taxable transfer is the creation of a trust providing that income is payable to the beneficiary until the death of the settlor at which time the remainder passes to the beneficiary. Here the succession to the remainder is subject to tax.

These decisions may deter the creation of an inter vivos trust where the benefits of possession and enjoyment pass at the death of the settlor. Even though the federal estate tax benefits may be obtained, the amount of the state inheritance tax assessment may be of sufficient size to require serious consideration of other possible alternatives.

For example, the irrevocable inter vivos trust is often used as a receptacle for the assignment of life insurance policies in an effort to reduce the settlor's federal estate tax liability. Normally, good estate planning prohibits the vesting of a future interest in the trust beneficiary; therefore, the irrevocable trust should require the beneficiary to survive the settlor. However, the Attorney General has ruled that the requirement that the beneficiary survive the settlor

88 Speaking for the court, Justice Blair stated:
Under the Federal Estate Tax Law, the primary question is to determine when the decedent or grantor parted with all property rights. Under our State Inheritance or Succession Tax Statute, the primary question is whether the transfer was made or intended to take effect in possession or enjoyment after the death of the grantor or settlor, particularly in the cases of transfer of property in trust. It is not a question of when the beneficial interest is created, but the tax is imposed upon the right to receive in possession or enjoyment after the death of the grantor or settlor. In consequence, a grantor or settlor may create an irrevocable trust during his lifetime, still if he postpones the right of possession or enjoyment of the beneficiary until after the grantor's death, the property or any interest therein is subject to the inheritance or succession tax at or after death. Under our statute, where either "possession" or "enjoyment" is made contingent upon the death of the grantor or settlor of all or any part of the trust estate, such transfer is taxable. 143 S.W.2d 997, 1002-03 (Tex. Civ. App. 1940—Austin) error ref. (Emphasis added.)

89 Bethea v. Sheppard, 143 S.W.2d 997 (Tex. Civ. App. 1940—Austin) error ref.; Ops. Tex. Att'y Gen. No. 0-1002 (May 5, 1943), provided for the assessment of the tax when the settlor retained an income interest for life as well as a contingent reversionsary interest.

90 State St. Trust Co. v. Stevens, 209 Mass. 373, 95 N.E. 851 (1911); Chase v. Commissioner of Taxation, 226 Minn. 521, 33 N.W.2d 706 (1948); Bethea v. Sheppard, supra note 88.


92 Casner, op. cit. supra note 9, at 456.
is a transfer intended to take effect in possession or enjoyment after the death of the donor, and, therefore, the insurance proceeds are subject to inheritance tax. Thus, the apparent advantage of avoiding the federal estate tax on the value of the life insurance policy, should the trust beneficiary predecease the settlor, may be lost when the Texas inheritance tax liability is determined at the settlor's death and the property passes to the beneficiary.

F. Transfer In Contemplation Of Death

The Texas statute imposing an inheritance tax on transfers in contemplation of death, is distinguishable from the corresponding federal estate tax provision in two important aspects. First, the Texas transfer must involve a "material part of the estate" before the inheritance tax will be assessed. Secondly, the federal statute prohibits any transfer made more than three years before the testator's death from being taxed as a gift in contemplation of death; whereas, the Texas statute has no limitation on the period during which the transfer may be considered as a gift in contemplation of death. Therefore any gift made by a decedent may be considered as made in contemplation of death. Moreover, the Attorney General has ruled that the facts and circumstances of each case will determine whether the transfer involves a "material part" or an "adequate valuable consideration." Although this provision does not promote stability for planning purposes, the distinctions between the Texas and the federal statutes should be kept in mind.

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82 Suppose A, a widower, transfers two $50,000 life insurance policies to an irrevocable inter vivos trust to be paid to his two sons in equal shares. If one of the sons predeceases A, only the value of the policy will be subject to federal estate tax liability, and if this son has no other assets, there will be no federal estate tax due. See Int. Rev. Code of 1954, § 2042. Furthermore, if A predeceases his sons, no estate inheritance tax will be assessed on the policies if the sons were not required to survive A. The tax saving is readily apparent, and the size of A's estate passing to the sons will determine the final amount saved.

83 Tex. Tax—Gen. Ann. art. 14.01 (1959): Any transfer made by a grantor, vendor, or donor, whether by deed, grant, sale, or gift, shall, unless shown to the contrary, be deemed to have been made in contemplation of death, and subject to the same tax as herein provided, if such transfer is made within two (2) years prior to the death of the grantor, vendor, or donor, of a material part of his estate, or if the transfer made within such period is in the nature of a final distribution of property and without adequate valuable consideration.


G. Widow's Election

The doctrine of election has long been an important concept in the devise of Texas property. This concept not only significantly assists in an orderly devolution of an estate, but in many instances its proper utilization affords important federal tax benefits.99

An election by a surviving widow to take under a will removes the value of her community interest plus the value of the statutory exemption from an inheritance tax assessment.100 However, to the extent that property received under a will exceeds these two amounts, an assessment is proper. Thus it is obvious that there should be carefully planned inter vivos dispositions of at least a portion of the separate property of the person forcing the election.

With respect to the remaining beneficiaries of a will, a surviving spouse's election to take under that will requires a consideration of whether only the decedent's one-half share or the entire community estate is to be taxed as passing under the will of the decedent. In Calvert v. Fort Worth Nat'l Bank,101 the Texas Supreme Court ruled that the inheritance tax could be assessed only upon the decedent's one-half of the community estate.

In that case the husband established a testamentary trust disposing of his separate property and all of the community estate. Upon the widow's election to take under the will, the state contended that the whole community interest was subject to the inheritance tax assessment on the theory that it passed from the decedent.

The supreme court rejected the state's contention for two reasons. First was the fact that the legislature had in other instances been explicit when property of persons other than the decedent was to be

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99 The doctrine of election has been defined to mean that a legatee or devisee under a will is put to the choice of accepting the beneficial interest offered by the donor in lieu of some estate which he is entitled to, but which is being taken from him by the terms of the will. When by the express terms of the will the party is put to an election, he must make a choice regardless of the relative value of the two inconsistent rights. To uphold an election the compensating thing need not be of value equal to that taken away. Dakan v. Dakan, 125 Tex. 305, 315, 32 S.W. 620, 626 (1935).

100 See Wright v. Wright, 154 Tex. 118, 274 S.W. 670 (1955); Smith v. Butler, 85 Tex. 126, 19 S.W. 1083 (1892).

101 For purposes of simplicity, this section of the Article is worded in terms of a "widow's election." However, the concepts discussed are equally applicable to a husband who is put to an election under the will of his wife.

For detailed treatment of the widow's election with emphasis on the federal tax aspects, see Westfall, Estate Planning and the Widow's Election, 71 Harv. L. Rev. 1269 (1958); Comment, The Widow's Election: A Study in Three Parts, 15 Sw. L.J. 85 (1961).

100 Jones v. State, 5 S.W. 2d 973 (Tex. Com. App. 1928).
101 Jones v. State, 5 S.W. 2d 918 (1962).
considered as passing by will, and hence subject to the inheritance tax.\textsuperscript{103}

The second ground for not taxing the full community estate was based upon the fact that the wife's one-half share of community property did not pass by the decedent's will but passed because of the election by the widow. The court stated:

It is manifest that no tax liability with respect to Mrs. Taylor's community interest accrued at the death of her husband or upon the probate of his will, because her interest did not and could not pass solely by virtue of such will. Before it could be said that Mrs. Taylor's interest had passed by any means, a further voluntary and affirmative action on her part was required. It was not until she elected to take under and in accordance with the provisions of the will that the trustee became entitled to her interest in the community property. Although the election when made might be held for some purposes to relate back to Mr. Taylor's death, the effective legal act was the voluntary election of the living wife and not the testamentary disposition of the deceased husband. It seems clear to us then that Mrs. Taylor's community interest did not pass to the trustee by her husband's will within the meaning of Article 14.01.\textsuperscript{103}

The court distinguished those cases\textsuperscript{104} holding that where the widow takes under the will, the entire community interest passes under the will as if the entire estate had always belonged to the testator. The distinction was based upon the fact that those controversies involved title questions between the widow and heirs while this case involved an inheritance tax problem controlled by statute.

The case, therefore, seems clearly to settle the rule that in those situations where the widow elects to take under the will, only one-half of the community estate will be subject to the inheritance tax. However, this does not mean that the widow's share of the community property will escape the inheritance tax upon her death. At that time her one-half share may be subject to the inheritance tax as a transfer made or intended to take effect in possession or enjoyment after death under the doctrine of Bethea v. Sheppard.\textsuperscript{105}

\textsuperscript{103} The court pointed out that article 14.01 expressly includes: (1) property passing under a general power of appointment exercised by the decedent by will; (2) certain life insurance proceeds; (3) transfers made or intended to take effect in possession or enjoyment after death of the grantor or donor; and (4) transfers in contemplation of death.

\textsuperscript{104} See Graser v. Graser, 147 Tex. 404, 215 S.W.2d 867 (1949); Dakan v. Dakan, 125 Tex. 305, 83 S.W.2d 620 (1935); Kelly v. Kelly, 294 S.W. 518 (Tex. Comm. App. 1927).

\textsuperscript{105} See Graser v. Graser, 147 Tex. 404, 215 S.W.2d 867 (1949); Dakan v. Dakan, 125 Tex. 305, 83 S.W.2d 620 (1935); Kelly v. Kelly, 294 S.W. 518 (Tex. Comm. App. 1927).

"Whether the right of succession to such interest [the widow's one-half share of the community property] is taxable as a transfer made by her in contemplation of death or to take effect in possession or enjoyment after death is a question which must be determined later." — Tex. at —, 356 S.W.2d at 927.
II. Exemptions

A. Personal Exemptions

An estate tax is levied against the entire estate as a unit, while an inheritance tax is levied against the distributive share of each beneficiary of the estate. In harmony with the virtually uniform rule, the Texas inheritance tax rates and exemptions are determined by the relationship of the beneficiary to the decedent. The relationship of the beneficiary will cause the inheritance tax rate to vary, as well as the amount exempt from tax. In the normal situation these variations will have no effect on the testamentary disposition of the decedent's property. However, in certain circumstances a consideration of the rates and exemptions will favor transferring property to one beneficiary by inter vivos gift and to other beneficiaries by testamentary disposition.

B. Charitable Exemption

In most circumstances an estate plan will have a charitable disposition of a part of the property in the estate. Such disposition is advantageous under the federal income, gift, and estate taxes; thus, the donor of such a charitable disposition will receive federal tax advantages in either an inter vivos or testamentary transfer to a qualified charity. However, there are extreme limitations upon the advantages of a charitable devise with respect to minimizing the Texas inheritance tax.

The very nature of the inheritance tax prevents the other beneficiaries of the estate from realizing any tax advantage on a charitable devise of property. Since the inheritance tax is imposed on the privilege of succession to property, not the property, only the charity receives any benefit from the exemption. Furthermore, the territorial restriction of the Texas charitable exemption prescribes a careful study of any such bequest if the donor desires a tax-exempt transfer.

106 Mahany, Texas Taxes 836 (1946).
107 See Kidder, State Inheritance Tax and Taxability of Trusts 398 (1934).
113 Cahn v. Calvert, 159 Tex. 385, 321 S.W.2d 869 (1959); State v. Hogg, 123 Tex.
568, 72 S.W.2d 593 (1934).
114 See Tex. Tax—Gen. Ann. art. 14.06 (1959): Provided, however, that this Article shall not apply on property passing to or for the use of the United States, or to or for the use of any religious,
Prior to 1933, to qualify for the exemption a charity had to be located in Texas, and the devise had to be used within the state. The mandatory location requirement was deleted by statutory amendment in 1933, and only the restriction on using the property within the state was retained. The evolution of the exemption was continued in 1959 when certain regional charities were permitted tax-exempt status. Though these statutory amendments indicate a relaxation of the territorial restriction, the estate planner should be cautious in making any testamentary disposition of property to a charity, since tax exemptions are construed against the taxpayers claiming the exemption.

The narrow exemption permitted charities under the Texas statute, together with the sharp acceleration of tax rates to be applied to property without tax-exempt status, presents strong reasons for an inter vivos transfer of the property when the charity cannot qualify for the exemption. Subject to certain exceptions, an inter vivos transfer of the property will be desired for federal tax reasons. Admittedly the impact of the Texas provision is sometimes reduced by the deduction for state taxes permitted in the computation of the

educational, or charitable organization, incorporated, unincorporated, or in the form of a trust, when such bequest, devise, or gift is to be used within this state. The exemption from tax under the preceding provisions of this Article shall without limiting its application under other appropriate circumstances, apply to all or so much of any bequest, devise, or gift to or for the use of the United States, or a religious, educational, or charitable organization, which is, in writing and prior to the payment of the tax, irrevocably committed for use exclusively within the State of Texas or transferred to a religious, educational or charitable organization for use exclusively within this state.

Provided, further, that if property so passing is to or for the use of a religious, educational, or charitable organization which conducts its operations on a regional basis, one such region of which includes the State of Texas, or any part thereof, then a bequest, devise, or gift to be used within such region shall be deemed to be used within this state.

For purposes of this paragraph a region shall comprise not more than five contiguous states, either in whole or in part, one of which is the State of Texas.

...See Texas Acts 1931, 42d Leg., ch. 72, at 109. In San Jacinto Nat'l Bank v. Sheppard, 125 S.W.2d 715 (Tex. Civ. App. 1939—Austin) no error bit., the court held that the term "located" as used in the statute was used in the sense of domicile or residence of a corporation and not merely to distinguish, generally, a foreign from a domestic corporation. However, in order to obtain the exemption, the corporation must use the devise or gift within the state.


...See Texas Unemployment Compensation Comm'n v. Bass, 117 Tex. 1, 151 S.W.2d 567 (1941); accord, Hedgecroft v. City of Houston, 150 Tex. 654, 244 S.W.2d 632 (1951).


...For example, by keeping property in the estate for a testamentary disposition to a charity the marital deduction is increased. 2 Casner, Estate Planning 896 (3d ed. 1961).

federal estate tax. However, that deduction does not resolve the problem in most instances, and careful consideration should be given any charitable disposition of property.

III. SPECIAL PROBLEMS

A. Marital Deduction

The Texas inheritance tax has no special exemption for property passing to a surviving spouse. The absence of such an exemption is an important distinction from the federal estate tax, which permits a deduction of fifty per cent of the adjusted gross estate upon the passing of that amount of property to the surviving spouse. However, since one-half of the community property is excluded from the adjusted gross estate, only when an estate consists of separate property will the federal marital deduction be a factor in an estate plan. Admittedly, this deduction is important in the formulation of an estate plan; however, in some circumstances the Texas inheritance tax will lessen the effectiveness of the marital deduction.

In many instances an estate plan will require an inter vivos disposition of a portion of an estate to third persons. Where the estate consists of both community and separate property the careful selection of the property to be transferred may result in an effective reduction in Texas inheritance tax liability. Although it may not affect the federal gift and estate tax liabilities, in most instances an inter vivos transfer of separate property will produce the most favorable inheritance tax results. In making that choice it is important to note the lack of a special exemption on property passing to a surviving spouse in the Texas statute. Because of the absence of

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126 Ibid.
129 For example, a husband (H) and wife (W) have a community estate of $400,000 and H has separate property valued at $100,000. H and W desired to make an inter vivos gift of $100,000 to their two children; further, it is desired that only the surviving spouse and the children receive the property interests of the first spouse to die. Upon the death of H, by qualifying for the federal estate tax marital deduction, the federal estate tax liability will not be affected by the selection of the property for inter vivos transfer. However, an inter vivos transfer of the separate property will permit a Texas inheritance tax assessment of $3,650, while the retention of the separate property in the estate will result in $5,450 inheritance tax liability. The inheritance tax liability is based on the property passing to W in fee. Although a division of the estate by using future interests will reduce the margin of difference in the inheritance tax, the decrease in the Texas inheritance tax is established. Tex. Tax—Gen. Ann. art. 14.02 (1959).
an exemption, retention of the separate property in the estate would increase the amount of property subject to the Texas inheritance tax by the amount of the possible federal estate tax marital deduction.\textsuperscript{120} Equally important in deciding to transfer the separate property is the increase which occurs in the surviving spouse's federal income tax basis in the community property without the necessity of including the community interest in the estate of the decedent.\textsuperscript{121}

There are many situations when the separate property will not be selected for inter vivos disposition. In such circumstances, an estate planner must examine the avenues available to reduce the Texas inheritance tax in conjunction with qualifying for the federal estate tax marital deduction.\textsuperscript{122} Unlike the gift tax,\textsuperscript{123} in qualifying for the federal estate tax marital deduction it should be remembered that it is immaterial whether the decedent bequeathes his interest in community or separate property to the surviving spouse.\textsuperscript{124} It is only necessary for the decedent to own separate property which is includible in his gross estate.\textsuperscript{125}

The Texas inheritance tax may still be reduced without sacrificing the federal estate tax marital deduction. Through the proper use of a general power of appointment\textsuperscript{126} or a power of invasion\textsuperscript{127} an estate can qualify for the federal estate tax marital deduction and yet reduce the Texas inheritance tax.\textsuperscript{128} For example, a bequest of property to the surviving spouse for life with a general power of appointment will not only qualify for the marital deduction but will also reduce the inheritance tax assessment.\textsuperscript{129} Thus, the total death tax liability is reduced effectively without impairing any plan of disposition.

\textsuperscript{120} To the extent the property would be community property, the Texas inheritance tax would be assessed in any event. Only the fifty per cent available for the federal estate tax marital deduction will be the increase in the property subject to the Texas inheritance tax. See Int. Rev. Code of 1954, § 2056.

\textsuperscript{121} Int. Rev. Code of 1954, §§ 1014(b) (6), - (7).

\textsuperscript{122} Int. Rev. Code of 1954, § 2056.

\textsuperscript{123} For gift tax purposes the marital deduction is inapplicable to a gift of property which is community property at the time of the gift. Int. Rev. Code of 1954, § 2523 (f).

\textsuperscript{124} 4 Mertens, op. cit. supra note 124.

\textsuperscript{125} Suppose H's community property interest is $200,000 and he also has $100,000 in separate property. The maximum marital deduction available is $50,000. If H devises his $200,000 interest to his surviving spouse in fee and the separate property to a third person, the $50,000 federal estate tax marital deduction would be available, even though the separate property passed to a third person.

\textsuperscript{126} Int. Rev. Code of 1954, § 2056(b) (5).

\textsuperscript{127} Care must be taken to bring the gift within the terms of the statute. A power to invade the corpus for the widow's needs or for her support will not achieve the desired result since her rights are limited by objective standards. A power to sell or consume may not include a power to give. Difficult questions of construction will arise whenever language used creates any uncertainty. 1 Bowe, Estate Planning and Taxation 74 (1957).

\textsuperscript{128} See note 8 supra and accompanying text.

\textsuperscript{129} Suppose H dies with $200,000 in community property interest and $200,000 in
B. Wills

A will generally places the burden of paying death taxes. The consideration of the responsibility for such payments is important to any estate plan.\textsuperscript{140} Since the Texas inheritance tax is neither an expense of administration nor a charge upon the general estate of the decedent,\textsuperscript{141} a provision in the will assessing the burden of the normal expenses will not adequately place the death tax burden. The successive nature of an inheritance tax requires a charge against each share or interest according to its value, and each beneficiary receives an interest burdened with the inheritance tax imposed on the right to receive the property.\textsuperscript{142} However, a specific provision in the will may relieve the property passing to a beneficiary of the tax burden, provided the testamentary provision to such effect is clear and unequivocal.\textsuperscript{43}

The Texas courts have given these provisions strict interpretation.\textsuperscript{144} For example, when a will directed the executors "to pay such legacies, all taxes, State, National, all debts, just and provable, against my estate," a Texas court rejected a contention that the Texas inheritance taxes should be paid pursuant to the provision.\textsuperscript{145} Therefore, in drafting a will provision placing the burden of death taxes, the provision should specifically mention inheritance taxes.

It is equally important to include a provision for payment of the estate tax in the will. Though the Texas estate tax provides for apportionment when there is an inheritance tax assessed against the estate,\textsuperscript{146} there is no apportionment of the Texas estate tax when no

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\textsuperscript{140} Casner, op. cit. supra note 120, at 1132-16.


\textsuperscript{142} Sinnott v. Gidney, 159 Tex. 366, 322 S.W.2d 507 (1959); Norton v. Jones, supra note 114.

\textsuperscript{143} It is competent for a testator to specify what property or class of property shall assume the burden of the tax on the transfer or the right of succession of his estate, as for example, to provide that inheritance and estate taxes shall be paid out of a general or residuary estate, or out of a particular fund. Since the practical effect of such a provision is to increase the gift, the intent of the testator to make such a gift will not be drawn from uncertain language. Norton v. Jones, 210 S.W.2d 820, 821 (Tex. Civ. App. 1948—Dallas) error ref.

\textsuperscript{144} See cases cited note 142 supra.

\textsuperscript{145} In Norton v. Jones, 210 S.W.2d 820 (Tex. Civ. App. 1948—Dallas) error ref., the court gave special emphasis to the use of "my estate" in the clause placing the burden of the death taxes. The court reasoned that since the estate did not owe an inheritance tax, the use of the words "my estate" served expressly to exclude from consideration all taxes due and owing by everyone else.

\textsuperscript{146} See Tex. Tax—Gen. Ann. arts. 15.01-.03 (1959).
inheritance tax is imposed on an estate. Moreover, Texas has no general apportionment statute, and where the taxable estate includes only testamentary assets, the Texas Supreme Court does not recognize the apportionment rule. Thus, in absence of a provision in the will directing otherwise, the estate tax attributable to testamentary assets is not apportionable and the burden of the tax is determined by the rules of law applicable to debts and expenses of administration.

In those instances when the federal estate tax marital deduction is desired, the devise to a surviving spouse should pass free from tax. Although an assessment of the inheritance tax does not disqualify the devise for the marital deduction, the deduction will be diminished by the amount of the inheritance tax liability. Thus, the portion of the estate to be used to satisfy the death tax liability should be clearly identified in the will.

A testamentary charitable disposition of property requires more than just an adequate identification of the charity. The territorial restriction of the Texas inheritance tax charitable exemption dictates a provision restricting the use of the property to comply with the statute. The Texas courts and the Attorney General indicate that an express limitation on the property in the will is sufficient to meet the requirements of the exemption. It is also important to assure a tax-free passing of property to the charity. Though in some instances an imposition of the inheritance tax will not affect the federal estate tax liability, there are other situations when such an assessment will increase the federal death tax liability by reducing the federal estate tax charitable deduction.

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148 In Sinnott v. Sidney, 159 Tex. 366, 322 S.W.2d 307 (1959), the Texas Supreme Court defined testamentary assets as "property passing under the will or by descent as distinguished from that which, although includible in the estate, is not part of the testamentary or intestate estate." 322 S.W.2d at 513.
149 Ibid.
150 Ibid. In Thompson v. Thompson, 149 Tex. 632, 236 S.W.2d 779 (1951), after holding the estate tax to be an expense of the administration, the Texas Supreme Court held the orders of liability for such expenses, absent a will provision directing otherwise, to be the following: (1) residuary estate, (2) personal property, and (3) real property.
152 For example, assume that the only bequest to the surviving spouse is $100,000 and the spouse is required to pay a state inheritance tax in the amount of $1,100. If no other death taxes affect the net value of the bequest, the value for the purpose of the marital deduction is $98,900. See Treas. Reg. § 20.2016(b)(4)(c) (1961).
155 Ibid. In Thompson v. Thompson, 149 Tex. 632, 236 S.W.2d 779 (1951), after holding the estate tax to be an expense of the administration, the Texas Supreme Court held the orders of liability for such expenses, absent a will provision directing otherwise, to be the following: (1) residuary estate, (2) personal property, and (3) real property.
IV. Conclusion

The preceding discussion clearly establishes that no estate plan can be properly drafted without careful consideration of the Texas death tax liability. Granted, in most instances the federal tax considerations will control the disposition of property, but under certain circumstances, the inheritance tax can be effectively diminished without impairing a possible reduction in federal estate tax liability.

In summary, in planning any estate subject to the Texas death tax assessment there are certain factors that should be considered.

The following factors are the more important:

1. In both the creation and exercise of a general power of appointment the Texas death tax assessment emphasizes the advantage of an inter vivos power; in addition, the possible passing of the property in default of appointment should be carefully examined.

2. The use of future interests should be an integral part of any plan; the case of Calvert v. Thompson appears to be a command for the use of future interests in the devolution of any Texas estate.

3. In any attempt to remove life insurance proceeds from possible taxation, payment of premiums by the insured should be avoided. Furthermore, care should be taken to secure the exemption upon the payment of proceeds to a named beneficiary.

4. The broad interpretation of the Texas inheritance tax provision regarding “transfers intended to take effect at or after death” must always be considered in any inter vivos transfers of the estate. As noted, this provision is particularly hazardous in the creation of irrevocable inter vivos trusts.

5. The selection of a testamentary charitable beneficiary should be carefully examined; the proper restriction on the bequest for sole use within the restricted area of the statute should be secured.

6. Under most circumstances the estate should first exhaust its separate property in any inter vivos transfer of property; in the event such property is unavailable for inter vivos disposition, the

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158 See note 15 supra and accompanying text.
159 See note 22 supra and accompanying text.
160 See note 34 supra and accompanying text.
162 See note 50 supra and accompanying text.
163 See note 42 supra.
164 See notes 67, 91 supra.
165 See note 89 supra and accompanying text.
166 See note 119 supra and accompanying text.
167 See note 126 supra and accompanying text.
divided estate should always be used to reduce the inheritance tax assessment.\(^8\)

(7) The will should specifically provide for the burden of the inheritance tax assessment;\(^9\) in addition the will should expressly negate the exercise of any power of appointment possessed by the estate when it is not desired to exercise the power.\(^10\) Finally, a charitable bequest should be restricted to comply with the statutory provision.\(^11\)

These general considerations of the Texas death tax assessment indicate that the tax has a twofold significance in an estate plan. It is important as one of many factors to be considered in formulating the plan. Moreover, upon formulation of the plan the avenues available to reduce the inheritance tax assessment must be examined to assure maximum tax benefit.

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\(^8\) See note 132 supra and accompanying text.
\(^9\) See note 143 supra and accompanying text.
\(^10\) See note 22 supra and accompanying text.
\(^11\) See note 153 supra and accompanying text.