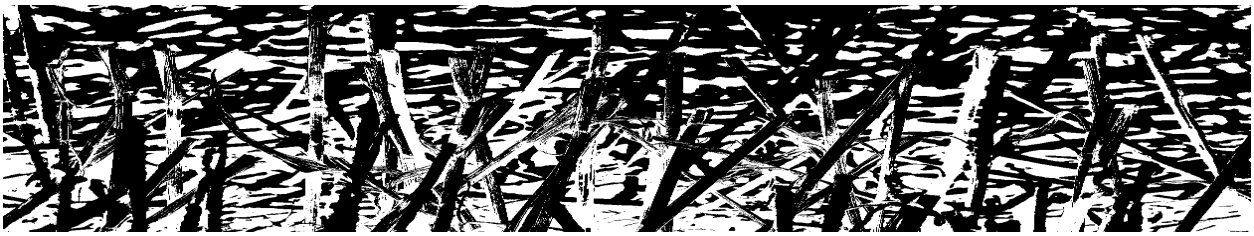

Jack Straw Fortnightly*

making shift

On November 09, the Supreme Court denied without comment an executrix' petition for *certiorari* from the decision of the Massachusetts supreme court in *Shaffer v. Commissioner*, affirming the state appellate tax board in its determination that the remainder of a QTIP trust is includible in the estate of a resident decedent income beneficiary, even though

(a) the predeceased spouse under whose will the trust had been created had been a resident of New York, not Massachusetts, when he died, and even though

(b) the decedent did not have even a limited power to appoint the QTIP remainder.

The executrix' theory was that there was no "transfer" at the death of the surviving spouse on which the state could impose an excise tax, consistent with principles of due process.

Jack does not expect even the most attentive reader to remember, but we went into this question at some length in Jack Straw one comma twelve, a little over two years ago, in a sort of freeform extrapolation from a discussion of *In re Seiden (Hogan)*, a then recent decision of the surrogate's court in New York County.

Somewhat surprisingly, the *Seiden (Hogan)* court determined that a QTIP remainder was not includible in the estate of the resident surviving spouse, despite the fact that the executor for the first decedent spouse, also a resident, had made a state level QTIP election. Right there in New York.

But as it turned out, this was something of an anomaly, arising from an oversight in legislative drafting.

The state statute that might have triggered inclusion referred only to a federal QTIP election, not to an election on a New York estate tax return, an omission that has since been corrected.[1]

In the particular case, the first decedent spouse had died in 2010 while the federal estate tax was temporarily repealed. A state level only election had been made on a pro forma 706 attached to the state return, but the executor had opted out of filing a federal return.

In the course of a broader discussion of whether or how something like a "duty of consistency" might require inclusion of a QTIP remainder in the estate of a surviving spouse -- again, for purposes of a state level tax --, we noted that a similar glitch in the statute explained the result in *Comptroller v. Taylor*, a decision of the Maryland court of special appeals from 2018.

not what you think it means

What you need, in other words, is a statute that covers both situations, a QTIP election on a federal return, or an election on a state return, same state, even if no election is made on a federal return.[2]

In *Shaffer*, the statute fairly clearly would include the QTIP remainder without reference to whether the first decedent had been a resident of Massachusetts. So the question whether this comports with due process was squarely presented.

The Massachusetts court framed much of its discussion in *Shaffer* with reference to a very similar decision out of Connecticut we also discussed in issue one comma twelve.

In 2017, the Connecticut supreme court in *Estate of Brooks* ruled that the state could properly tax a QTIP remainder despite the fact that the trust had been created under a will probated in another state, in that case Florida.[3]

In *Brooks*, unlike *Shaffer*, the surviving spouse did have a limited power to appoint the remainder and in fact had exercised it. And she was herself the trustee of the QTIP trust, whereas in *Shaffer* the remainder distributees were the co-trustees during their mother's life.

But these facts were apparently not dispositive, as they were mentioned only in a footnote, as a sort of makeweight to the nexus argument. Which had something to do with her having "enjoyed the benefit" of her life interest as a resident of Connecticut.[4]

In each of these cases, the taxpayer argued that the taxable "transfer" had occurred at the death of the first spouse in another state. It was not the state to which the survivor later relocated that had extended the benefit of a deferral of tax through a state level QTIP election, for which inclusion at the death of the survivor would have been the agreed tradeoff.

In rejecting this argument, each court cited the 1954 Supreme Court decision in *Fernandez v. Weiner*, to the effect that for purposes of due process analysis, the federal estate tax should be seen not as an excise on "transfers" as such, but on "the shifting from one to another of any power or privilege incidental to the ownership or enjoyment of property."

Or as the *Shaffer* court expressed it, "the decedent's death created a change in the legal relationship among the QTIP assets, the decedent, and the beneficiaries," and this was a sufficient nexus.

To similar effect, per the *Brooks* court, "the shift in legal relationships to property occasioned by death." But what this has to do with nexus is not entirely clear, says Jack.

dying embers

In her petition for cert, the executrix in *Shaffer* argued that *Fernandez* did not expressly overrule that aspect of *Coolidge v. Long*, also discussed in Jack Straw one comma twelve, that a state inheritance tax could not be imposed "retroactively" on remainder interests in the trust there at issue which had already "vested," albeit not yet in possession and albeit still subject to defeasance, prior to enactment.

Jack says okay, technically *Fernandez* did not address that precise point, because the retroactive application of a later enacted tax was not at issue.

But it did clearly say that a state could impose a "transfer" tax on "the shifting at death of particular incidents of property," even if those arrangements were already in place.

And Jack would also say, apropos *Coolidge*, that there is no substantive difference between a contingent remainder and a vested remainder subject to defeasance. The distinction depends entirely upon whether the condition is framed as "precedent" or "subsequent," which is a species of magical thinking.[5]

Perhaps anticipating that the executrix would find no traction, the state commissioner of revenue waived a reply to the cert petition.

under submission

Closing arguments in *Fairbairn v. Fidelity Charitable* on December 04 concluded a six-day virtual bench trial.

We discussed this case very briefly a few months back in issue three comma three, suggesting at the time that the trial court might have an imperfect understanding of what remedies are actually available to the plaintiffs here.

Copies of trial and post-trial briefs are posted to the Jack Straw landing page, together with briefs supporting and opposing Fidelity's motion in limine to preclude the Fairbairns from pursuing a damages claim on behalf of the DAF itself, as they had no ownership interest in the fund.

Your correspondent is out of pocket something like twenty dollars on just these documents, because the "public access to court electronic records" system, or PACER, puts all this stuff behind a paywall at ten cents a page.

HR 8235, which cleared the House on a voice vote on Tuesday, December 08 and was received in the Senate the following day, would make these records free to the public. Jack suggests that his readers might contact their Senators to urge them to support this measure.

under confusion

It appears IRS might not be appealing the decision of the Tax Court in *Dickinson*, which was the focus of our previous issue.

A notice of appeal would have been due December 08. However, the online docket is not updating while the court changes over to some other system, and anything filed after November 20 would have been on paper. The clerk's office tells your

correspondent these filings are simply accumulating "in buckets" until the new system comes online, so they cannot confirm whether anything was filed.

Meanwhile, we are not yet seeing any filings in the 11th Circuit federal appeals court, where an appeal would lie. But this could be simply a matter of delayed postings.

The lawyer from the chief counsel's office who handled the case will not comment, and the IRS media office claims that even to answer the question whether a notice of appeal has been filed would be to disclose "return information," in violation of section 6103.

Which is not only absurd, but also entirely contrary to the position the government is asserting in the case down in Georgia we mentioned briefly almost two years ago in issue two comma five in responding to a counterclaim by one of the defendants that a DOJ news release issued at the time the lawsuit was filed damaged his reputation.

under the net

The IRS Statistics of Income Division has released data on individual returns for 2018, the first year following enactment of the 2017 tax bill.

One spreadsheet shows selected components of adjusted gross income and selected deduction and credit items reported by taxpayers in the top half of adjusted gross incomes, ranked in declining percentiles from the top 0.001 pct. on down.

There were about 144.3 million returns filed for tax year 2018. The average income for those fourteen hundred people at the very top was $68.9 million.

Of just over $196.9 billion in charitable contribution deductions reported, more than half was claimed by two-thirds of one pct. of filers, all within the top one pct. of incomes, for which the adjusted gross income floor was $540k.

Within that range, charitable contributions were by far the largest single category of itemized deduction, by dollar value, whereas across all income ranges somewhat more was claimed for home mortgage interest.

State and local taxes were a distant third, this being the first year these were capped at $10k.

From a slightly different data set, we learn that about 17.4 pct. of all contributions deductions claimed, $33.2 billion, were for noncash contributions made by not quite 11k taxpayers with adjusted gross incomes of $10 million or more.

and finally

The 7520 rate recovered slightly in December to 0.6 pct. from the record low 0.4 pct. where it had sat for four months. And the rate is holding at .06 pct. for January. On the other hand, mid-term Treasury yields have fallen slightly since the January rate was set.

endnotes

[1]

Indeed, the revised New York statute no longer permits inconsistent elections as to QTIP as between the federal and state returns.

[2]

Which does often happen where the estate is below the federal exclusion amount but above the state threshold.

We are not (yet, or probably ever) looking at cases in which a state level only election was made in another state, no federal election, or in which an election was made on the federal return but not on the state return --

-- which latter scenario would be quite unusual except in a state that does not have an estate tax.

And of course immediately after writing the preceding sentence, your correspondent stumbled across *Estate of Evans*, a recent unpublished decision of the Oregon tax court, now pending appeal to the state supreme court, in which a QTIP remainder was taxed in the estate of an Oregon resident on the strength of a federal election, but the predeceased spouse had been a resident of Montana, which has no estate or inheritance tax.

Your correspondent has not yet been able to retrieve briefs to the state tax court, and apparently briefing has just begun in the state supreme court. Oral argument is set for May 06. Watch this space.

[3]

Something we did not note in our earlier discussion is that the Supreme Court had denied cert in *Brooks*.

[4]

The attentive reader will recall that this was not enough in *Kaestner* to support due process nexus. See yet again Jack Straw two comma nine. Not surprisingly, the taxpayer in *Shaffer* cited *Kaestner* in her reply brief to the Massachusetts court, and in her petition for cert, but to no avail.

[5]

On this point, Jack is in good company, with at least Prof. Lawrence W. Waggoner, the Lewis M. Simes Emeritus Professor of Law at the University of Michigan.

The remainder in *Shaffer* was to a trust for the benefit of descendants *per stirpes*, with outright distribution to each daughter as she attained age fifty. Analytically, this would in fact be vested subject to defeasance by a daughter not surviving to distribution, with shifting executory interests in the more remote beneficiaries.

Jack says, everything merges with the night