

The Validity of an Inheritance Tax on Gifts Inter Vivos Withing Six Years of Death

Edmund B. Shea

Follow this and additional works at: <http://scholarship.law.marquette.edu/mulr>



Part of the [Law Commons](#)

Repository Citation

Edmund B. Shea, *The Validity of an Inheritance Tax on Gifts Inter Vivos Withing Six Years of Death*, 9 Marq. L. Rev. 1 (1924).
Available at: <http://scholarship.law.marquette.edu/mulr/vol9/iss1/1>

This Article is brought to you for free and open access by the Journals at Marquette Law Scholarly Commons. It has been accepted for inclusion in Marquette Law Review by an authorized administrator of Marquette Law Scholarly Commons. For more information, please contact megan.obrien@marquette.edu.

Marquette Law Review

VOL. 9

DECEMBER, 1924

No. 1

THE VALIDITY OF AN INHERITANCE TAX ON GIFTS INTER VIVOS WITHIN SIX YEARS OF DEATH

BY EDMUND B. SHEA

THE provision of the Wisconsin Inheritance Tax Law that every gift of a material part of the donor's estate made within six years prior to the donor's death shall be construed to have been made in contemplation of death, was added to the statute in 1913.¹ Previous to the adoption of that amendment a voluntary transfer *inter vivos* was not subject to the Wisconsin inheritance tax unless the state could prove affirmatively that (1) the transfer was intended to take effect in possession or enjoyment at or after death; or that (2) the gift was actually made in contemplation of death.² The proof of such an issue, necessarily involving the state of mind of a deceased person, was a matter of difficulty and the belief arose among those having experience with the statute that many transfers actually made in contemplation of death were escaping inheritance tax merely because of inability on the part of the state to procure sufficient evidence to establish the donor's motive.

For the purpose of overcoming the difficulty the Wisconsin Tax Commission in 1912 recommended an amendment to the statute:

providing more definitely for the taxation of transfers made in the form of gifts, grants and donations when such transfers are in the nature of a final disposition or distribution of the estate of the donor or of a material part thereof. The general purpose of the law is to impose a tax upon the passing of estates from the ancestor to his successors. It appears large estates or large portions of an estate may be and frequently are conveyed during the later years of the owner's life

¹ The amendment is as follows: "Every transfer by deed, grant, bargain, sale or gift, made within six years prior to the death of the grantor, vendor or donor, of a material part of his estate, or in the nature of a final disposition or distribution thereof, and without an adequate valuable consideration, shall be construed to have been made in contemplation of death within the meaning of this section." Chap. 643 Laws of 1913.

² This is the rule at present prevailing in Idaho, Illinois, Iowa, Kansas, Minnesota and New York.

to his children in a manner that is clearly testamentary in its nature, yet they cannot readily be proved to have been made either in contemplation of death nor to evade the tax. The law should be made as broad in its language as it is in its purpose.

Report 1912, Chap. 5 pp. 60, 61.

The amendment adopted the following year presumably was in response to the Tax Commission's recommendation.³ It is apparent, however, that the legislation thus adopted went beyond the necessities which prompted it. The purpose in view might have been accomplished by establishing a presumption that transfers without consideration during a limited period before death, *prima facie and unless the contrary be shown*, are made in contemplation of death. Such a rule of evidence would have relieved the state of the burden of proof in such cases and would have subjected to tax all *ante mortem* gifts within a given period which could not be proved to have been made otherwise than in contemplation of death. This would have fulfilled the policy of the statute as regards gifts. But instead of creating merely a rebuttable presumption legislature declared a conclusive presumption thereby making the intent or motive of the donor of the gift wholly immaterial. In effect the legislature said: "Every gift of a material part of the giver's estate within six years before his death shall be subject to inheritance tax."

Several other states have adopted similar legislation.⁴ The language used to express the rule in the various statutes on the subject generally conforms in substance to that of the Wisconsin law. Such statutes

³ Another circumstance leading to the adoption of this amendment is thus recounted in the opinion in *Estate of Ebeling*, 169 Wis. 434: "In the case of *State v. Thompson*, 154 Wis. 320, 142 N. W. 647, this court had under consideration the question of inheritance taxes due from the estate of one Joseph Dessert, who died at the age of ninety-two. Practically his entire estate was devised to his only daughter and sole heir, Stella D. Thompson. She took by the will about \$200,000. During the last six years of his life he gave her approximately a half million dollars, mainly in two gifts, one made three years and the other four and one-half years prior to his death. This court held that the gifts were not subject to inheritance taxes. The circumstances of that case forcibly brought to the attention of the Legislature the fact that after a person had attained the age of eighty-nine years, an age when he could not expect to live many more years, when his thoughts, naturally, were consumed rather with the disposition of property already accumulated than with the accumulation of more, he could bestow his property upon the objects of his bounty and thus evade the inheritance tax. This decision was rendered May 31, 1913. The Legislature was then in session. Ten days thereafter Senate Bill No. 575 was introduced by the Joint Committee on Finance. This bill, without amendment, was approved July 21st and became ch. 643, Laws 1913."

⁴ Arizona, Arkansas, Colorado, Kentucky, Mississippi, Missouri, North Dakota, South Carolina, Tennessee and West Virginia.

frequently declare that transfers of the kind in question shall be "considered," "deemed," "held," or "construed" to have been made in contemplation of death. In no state has the conclusive presumption been applied to transfers made more than six years before the donor's death; and in only two states is the period of that length.⁵ The length of time during which the conclusive presumption is applied in only a few jurisdictions exceeds three years.

As distinguished from the conclusive presumption on the subject of *ante mortem* gifts, the effect of which is to make the giver's state of mind immaterial, numerous states have adopted a *prima facie* presumption with reference to such transfers.⁶ An example of this type of statute is furnished by the law of Delaware which declares that "any transfer of a material part of the property of the decedent in the nature of a final disposition or distribution thereof, made by the decedent within two years prior to his death, without full consideration in money or moneys worth, shall, *unless shown to the contrary*, be deemed to have been made in contemplation of death within the meaning of this chapter." To the same effect is the Federal Estate Tax Law.⁷

The constitutionality of that part of the Wisconsin Inheritance Tax Law now under consideration was first questioned in *Estate of Ebeling*, 169 Wis. 432 (1919). In sustaining the validity of the tax the court in that case remarked that whether the gifts were held to be gifts in contemplation of death or gifts *inter vivos*, in either case they were not beyond the taxing power of the Legislature, and continued:

If they be considered gifts *inter vivos* there is abundant justification for the classification here made in segregating them from other gifts *inter vivos* as objects of taxation, the basis for such classification being the purpose to make the law taxing gifts made in contemplation of death effective. It is recognized that in enacting a police regulation it may be found necessary to include within the purview of the statute certain acts innocent and not in themselves a subject of police regulation where the inclusion of such acts is necessary, in the opinion of the Legislature, to make the police regulation effective. *Pennell v. State*, 141 Wis. 35, 123 N. W. 115. While a principle relating to police

⁵ Arizona and North Dakota.

⁶ The Massachusetts statute provides: "Any deed, grant or gift completed *inter vivos*, except in cases of bona fide purchase for full consideration in money or moneys worth, made not more than six months prior to the death of the grantor or donor, shall, *prima facie*, be deemed to have been made in contemplation of death of the grantor or donor."

⁷ "Any transfer of a material part of his property in the nature of a final disposition or distribution thereof, made by the decedent within two years prior to his death without such a consideration (fair consideration in money or moneys worth) shall, unless shown to the contrary, be deemed to have been made in contemplation of death within the meaning of Part I of this Title."

regulation does not necessarily apply to the power of taxation, no reason is perceived why the Legislature may not, as here, make a classification of gifts *inter vivos* and subject them to taxation for the purpose of making effective taxation of gifts *causa mortis*. That it will occasionally result in the taxation of gifts not in fact made in contemplation of death, which may be conceded, should not condemn the classification if the classification be reasonably necessary to carry out the legislative scheme for the taxation of gifts *causa mortis*.

Answering the objection that the classification of the statute was unreasonable in singling out for taxation only those *inter vivos* transfers made within six years of the donor's death, the court said:

Nor should it be condemned because there is no material distinction between those who fall immediately upon one side of the line and those who fall immediately upon the other, as illustrated by the fact that a gift one day less than six years prior to death is taxable, while a gift made one day more than six years prior to death is not taxable. That is always the case where the classification is of necessity fixed by an arbitrary line of demarcation.

After the decision in the *Ebeling* case the validity of the six year provision was not directly challenged until recently in *Schlesinger's Estate*, 199 N. W. 953, in which case the constitutionality of the provision in question has again been upheld. As the outcome of this case, which now is pending in the Supreme Court of the United States, is likely to influence the trend of transfer tax legislation in other states, as well as the attitude of courts in regard to the taxation of transfers *inter vivos*, it is interesting to observe some of the particular problems involved.

In the *Schlesinger* case the testator made several substantial gifts within the last six years of his life to members of his immediate family. It was found as a fact by the County Court before which the inheritance tax was settled that none of the gifts were made in actual contemplation of death.⁸ This finding was supported by undisputed evidence. Nevertheless the County Court held the gifts taxable under the statute. The facts of the case go a step beyond the facts of the *Ebeling* case in that here it affirmatively appeared that the gifts were not made in contemplation of death and the appeal, therefore, raised sharply the

⁸The finding of the County Court was as follows: "That none of the gifts made by the decedent within six years next prior to his death were in fact made in view, or in anticipation, expectation, or apprehension of death, or in the actual contemplation of death as said term 'contemplation of death' was used in the statute, and had been defined and interpreted by the Supreme Court of Wisconsin prior to the enactment of chapter 643 of the Laws of 1913, or intended to take effect in possession or enjoyment at or after the death of the decedent."

question of the right of the Legislature to impose on such transfers an inheritance tax.

Other constitutional questions besides the validity of the statutory classification are raised by the case but the discussion in the present paper will be confined to the question whether or not the tax is based on a valid classification within the requirements of the Fourteenth Amendment to the Constitution of the United States.⁹ The issue in brief is whether the classification defined by the statute is justifiable on any ground, or whether it is so discriminatory as to involve a taking of property without due process of law or a deprivation of the equal protection of the laws in violation of the Fourteenth Amendment to the Federal Constitution.

The power of the state levy an excise tax in the form of a graduated tax on inheritances is not open to question.¹⁰ But this power is subject to the constitutional limitation which prohibits a state denying to any person the equal protection of the laws. What is equality under tax laws? It requires the same means and methods to be applied impartially to all the constituents of a class so that the law shall operate equally and uniformly upon all persons in similar circumstances.¹¹ It requires that all persons subjected to such legislation shall be treated alike under like circumstances and conditions, both in the privilege conferred and the liabilities imposed. In the words of Mr. Justice McKenna in *McGoun v. Illinois, Trust & Savings Bank*, *supra*, "the state may distinguish, select and classify objects of legislation, and necessarily this power must have a wide range of discretion. It is not without limitation, of course. 'Clear and hostile discriminations against particular persons and classes, . . . might be obnoxious to the Constitutional prohibition.'" In the case last cited, the scheme of classification prescribed by the Illinois inheritance tax law was held valid because as the court said: "The first two classes, (lineal and collateral relatives) therefore depend on substantial differences, differences which may distinguish them from each other and them or either of them from the other class (strangers to the blood of the decedent)—differences, there-

⁹ The contention was urged on the hearing in the State Supreme Court that the tax with respect to transfers before death and not made in contemplation of death is not an excise tax on the *transfer* but a *direct tax on the property* transferred. Admittedly a *direct tax* on property is not valid if graduated as to rates. A similar objection has been raised as to the provisions of the Federal Estate Tax regarding insurance on the life of the decedent, payable to third parties as beneficiaries. *Frick v. Lewellyn* 298 Fed. 803. In this case the U. S. Supreme Court has granted *certiorari*.

¹⁰ *Magoun v. Illinois Trust & Savings Bank*, 170 U. S. 283.

¹¹ *Kentucky Railroad Tax Cases*, 115 U. S. 321, 337.

fore, which 'bear a just and proper relation to the attempted classification' . . . And if the constituents of each class are affected alike, the rule of equality prescribed by the cases is satisfied."

If the provision of the Wisconsin statute now under discussion be considered as a tax on transfers *inter vivos*, it is vulnerable to the objection that it classifies those transfers on which the tax is imposed and segregates them from other similar transactions on which the tax is not imposed, by a test which is arbitrary, capricious and irrational. As was well said on this point by the Wisconsin Court in the *Schlesinger* case, "we observe no more reason why such gifts *inter vivos* should be taxed than gifts made within six years of marriage or any other event."¹²

In other words, if the provision be detached from its statutory context and be viewed as imposing a *gift tax* on certain specified transactions, the act violates the Fourteenth Amendment not necessarily because the state lacks power to tax gifts *inter vivos* but because in the exercise of that power it must proceed upon a rational basis of classification; it must treat things that are equal alike, and must not treat things as unequal which are not distinguished by real differences. A classification of gifts *inter vivos* for purposes of taxation is laid down in the federal gift tax law contained in the Revenue Act of 1924.¹³ It is difficult to conceive of any ground on which the Wisconsin statute could be defended under the Fourteenth Amendment as a tax on *inter vivos* transactions, even if it had been held valid on that ground by the state court.

The next question is whether the classification is based on rational and substantial differences, when the provision is considered in its context, as a part of a comprehensive program for the taxation of transfers caused by death. Does the statute attempt to treat as though they were equal or alike, things in fact dissimilar? The purpose and effect of the amendment is to class the transfers covered by its terms with transfers in fact made in contemplation of death, and the tax then is imposed by the substantive provisions of the statute on both groups as a single class. That the Legislature has no power by its fiat to force dissimilar things into the same group for the purposes of taxation is not open to dispute. There is no doubt that the mere legislative enactment that

¹² This statement corrects what the court had previously said in *Ebeling's Estate*, ante, to the effect that the law may be sustained as a tax on transfers *inter vivos*.

¹³ The federal statute applies to every gift in any year exceeding, in the case of residents, \$50,000; the rate begins at one per cent and increases progressively to forty per cent, the blocks being identical with those defined in the Federal Estate Tax Law. There are definite exemptions and deductions.

gifts within six years of death must be regarded as gifts in contemplation of death for the purposes of inheritance taxation, cannot settle the question of the propriety of such a classification. The latter question is one of fact to be determined by a comparison of the essential characteristics of transfers within six years of death on the one hand, and transfers in contemplation of death on the other hand. Is there such a relation or connection between these two groups of transactions as to warrant their being lumped together for inheritance tax purposes?

The legislative extension of the class of transfers actually* made in contemplation of death so as to include therein all transfers within six years of the donor's death, has been defended upon the assumption of fact that virtually all transfers within six years of death are actually made in contemplation of death.¹⁴

This broad assumption invites analysis. What is a gift in contemplation of death? The term is in current use by legislatures and courts and has acquired a definite and settled meaning. It is a gift impelled by an apprehension of death arising from some existing bodily infirmity or impending peril and not the general expectancy of eventful decease commonly entertained by all persons. The sense of imminent and approaching dissolution is an essential characteristic of such a gift.¹⁵

¹⁴ In *Schlesinger's Estate, ante*, the Wisconsin court says: "Our reports show that after the enactment of the Inheritance Tax Law many cases appeared in which elderly men of wealth, for the purpose of evading the law, made a more or less complete distribution of their property by way of gifts. The difficulty of proving that such gifts were made in contemplation of death, coupled with the public necessity of not allowing large estates to escape the provisions of the law, induced the Legislature to make the classification it did. While it may be granted that, as to a particular gift not made in contemplation of death, the Legislature could not declare it to be one made in contemplation of death, it does not by any means follow that in establishing a general class it cannot draw into that class gifts strictly not falling within it, provided that gifts of that class are usually and ordinarily of the kind which the class calls for, and especially where a practical and efficient administration of the law demands the classification." It may be remarked parenthetically that the Wisconsin reports during the period from the enactment of the inheritance tax law to date contain only six cases in which there arose any inheritance tax question as to transfers in contemplation of death.

¹⁵ In *State v. Thompson*, 154 Wis. 320, it is said: "An act is not done in contemplation of death when the feeling that dissolution is approaching is absent and is not the cause which impels or prompts the doing of the act." In *State v. Pabst*, 139 Wis. 561, the subject is covered in the following language: "The words, ('in contemplation of death' in the inheritance tax law) are evidently intended to refer to an expectation of death which arises from such a bodily or mental condition as prompts persons to dispose of their property and bestow it on those whom they regard as entitled to their bounty." . . . "A gift is made in contemplation of an event when it is made in expectation of that event and having it in view, and a gift made when the donor is looking forward to his death as impending, and in view of that event, is within the language of the statute."

The definition does not include any of the numerous gifts actuated by motives other than an apprehension of impending death. Thus for example it is a common practice among prudent men of means who are in the prime of life and to whom death has never become an active threat, to make substantial donations to their children and grandchildren. This practice is judicially noticed in *State v. Thompson, supra*. The marriage of a child is frequently the occasion for gifts from parents and parents-in-law. Marriage settlements between the parties have been in vogue from time immemorial. Parents make gifts to set up their sons in business. Husbands transfer substantial portions of their estates to their wives to provide against many contingencies besides death. It is common knowledge that men make large gifts under the circumstances mentioned and under a great variety of other circumstances, without being impelled by the apprehension of imminent dissolution. The special and peculiar kind of transfers which fulfill the definition of gifts made in contemplation of death form but a fraction of the total number of gifts without consideration. What the fraction may be cannot be computed or estimated accurately. Scientific data on the point are not available. Any conclusion which is reached must be based on general knowledge and experience. But it is reasonable to suppose that transfers in actual contemplation of death within the legal definition of the term constitute at most an insignificant portion of the total number of gifts without consideration made within six years of the donors' death.

Having in mind the precise legal character of a gift in contemplation of death, and the variety of motives which lead men to give away their property, it is impossible to accept the conclusion "that of all the gifts coming under the statute made by residents of Wisconsin within six years of their death, by far the larger proportion thereof have actually been made in contemplation of death."

If we consider the entire group of voluntary gifts between living persons wherein material portions of the donors' estates are transferred, it is probably true that the motive of avoiding liability for inheritance taxes plays a part in many of such transactions. It is probable that no person of means makes any considerable gift at the present time without an acute consciousness of the bearing of the inheritance tax law upon the transaction in hand. Indeed, no vigilant property owner can fail to perceive the shadow cast by the long arm of the inheritance tax law upon the transactions of everyday life. Every prudent person is irresistibly led to consider how to dispose of his estate in such a way as to reduce transfer taxes to a minimum, and it is common knowledge that inheritance tax legislation has been and still is the cause of a great and growing volume of gifts between living persons which would not

have been made were it not for the inheritance tax laws. The passage of the federal gift tax is a legislative recognition of this modern trend.

But does the fact that rich men are giving away their estates during life in order to avoid inheritance taxes and that thereby collections of inheritance taxes are falling off, warrant the legislature in picking out at random, on a chronological basis, a limited number of transfers *inter vivos* and imposing upon such transfers an excise termed an "inheritance" tax in order that more money may be realized from the so-called inheritance tax? Are gifts within six years of death in some way related to testamentary transfers or to transfers in contemplation of death so that they may be classed with the latter for taxation? No relationship between the two classes is referred to in the *Schlesinger* case opinion other than that which has already been touched upon, namely, that the collective group of transfers within six years of death are in fact transfers in contemplation of death. The latter conclusion assumes the point in issue. The connection at most appears to be remote and accidental rather than close or necessary, and it is extremely doubtful whether the two kinds of transfers can be said to overlap to any significant degree. If these two kinds of transactions are in fact essentially dissimilar no good reason can be found for including them in a single class for purposes of inheritance taxation.

It is apparent that the conclusive presumption as to *ante mortem* transfers within six years of death is in no way necessary or proper to the effective enforcement of the inheritance tax law as a whole. The policy of the statute being to reach transfers of a testamentary character as distinguished from transfers *inter vivos*, its full legitimate purpose with respect to transfers in contemplation of death can be accomplished by the enactment of a rule of evidence to the effect that every transfer within a given period before death shall be deemed *prima facie* to have been made in contemplation of death. Such a rule would insure collection of the tax on every gift in contemplation of death. And the fact that the legitimate legislative purpose can be fully carried out by the simple method referred to demonstrates that there is no necessity to resort to the conclusive presumption in order to make the law effective. This circumstance is not of controlling importance but it answers the argument that the discrimination is justified by necessity.

Is the classification discriminatory in treating things that are in fact equal as though they were different? What characteristics distinguish those *ante mortem* gifts which occur within six years of the donor's death from other similar gifts anterior in point of time? For example, suppose that in settling the estate a man dying in 1924 it appears that in 1919 he gave his son John a gift worth \$100,000 and that in 1917,

under similar circumstances, he made a gift of the same value to his son Henry. The former gift is taxed, the latter escapes. What fact requires or permits these two transfers to be treated differently? It is not a convincing answer to suggest that in any classification by division of time, by number or by weight, etc., there must be an arbitrary line drawn somewhere and if the line drawn by the legislature cannot be said to be clearly wrong it must stand.¹⁶ This overlooks the point of the objection that the time element has no relation whatever to the appropriateness of the tax on either transaction. It has been already suggested that the fact without more, that a transfer precedes death does not have any tendency to show that it was made in contemplation of death. The mere sequence of the two events is not significant. The formula *ante hoc ergo propter hoc* is bad logic. It is not as though the tax were conceded to be justified in any time dimension whatever, however limited. We are dealing not with a true classification by weight, dimension or number, but with a chronological arrangement which has no rational basis with respect either to the transfers which it includes or to those which it excludes. In other words, the present line of inquiry is based on the premise, previously considered, that there is no legitimate inference from the mere fact that a man gives away property that he does so in contemplation of death. If this be true, then it is just as true with respect to gifts made shortly before his death as in the case of gifts separated by a longer period of time from the event of death. And it follows that wherever the boundary line be placed in point of time, it will be an arbitrary and capricious barrier erected within a single group of similar things. The distinction for taxation purposes would be based on no differences in fact. This would be rank and hostile discrimination within the prohibition of the Fourteenth Amendment.

The whole question, therefore, turns largely on the first inquiry, as to whether or not transfers made within six years of death are fundamentally like, similar or equal to transfers in contemplation of death. As before stated, the question is one of fact. If the correct conclusion is that the two groups of transfers have essential common characteristics which are germane to the subject matter of inheritance taxation then the classification prescribed in the statute may be held not to offend the Fourteenth Amendment. On the other hand, if the correct answer is that transfers prior to death are not fundamentally like, similar or equal to transfers in contemplation of death, the classification attempted in the statute must be held discriminatory and a deprivation of the equal protection of the laws guaranteed by the federal constitution.

¹⁶ *In re Schlesinger's Estate, ante.*