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deduction of 8,000 dollars.[54] Furthermore, since this contribution is one of appreciated property, it would appear that all of the rules applicable to such contributions must be considered.[55]

An overall view of the provisions of the 1969 Act relating to charitable deductions seems to indicate that the new law will have little economic effect on the individual taxpayer. It is doubtful that the increase in the maximum limitation will be a greater incentive for charitable contributions since very few individuals contribute the maximum deductible amount to charity each year. Furthermore, because of the five-year carryover provisions, which also applied under the old law, most taxpayers could deduct the entire amount of their charitable contributions anyway. While the new provisions eliminate most of the tax advantages previously available for taxpayers making charitable contributions of "ordinary income property," many of the double tax savings still remain for gifts of "capital gain property." Thus, even though many of the rules governing charitable deductions have been tightened, the individual taxpayer, by carefully following the new rules discussed in this note, can still enjoy significant tax benefits through the use of charitable contributions.

TURNER VANN ADAMS

Income Tax—Problems of a Corporate Executor in the Administration of Successive Estates

The gain or loss from the sale or exchange of property is determined, for tax purposes, by the relation of the "amount realized" to the adjusted basis of the property.[1] The method used to compute the basis for the capital gains of property acquired from a decedent is defined by section 1014 of the Internal Revenue Code of 1954 to be "the fair market value of the property at the date of the decedent's death . . . ."[2] In *Manufacturers Hanover Trust Co. v. United States*[3] the United States Court of Claims applied section 1014 in a case involving successive deaths.

The plaintiff, a corporate executor, brought an action for refund of federal income taxes paid by the estate. The plaintiff was the executor of

[54] *Id.*
[55] P.H. 1970 FED. TAXES ¶ 115 (Rep. Bull. 1, 1970).

[1] INT. REV. CODE of 1954, § 1001.
[2] *Id.* § 1014(a).
[3] 410 F.2d 767 (Ct. Cl. 1969).

the estate of a woman who had died testate in 1957 and who had left her husband as her sole residuary legatee. Her estate included securities having at her death a fair market value of approximately 65,000 dollars. The executor had not distributed the estate prior to the husband's death in 1964, and at his death the fair market value of these securities was almost 160,000 dollars. The plaintiff was also appointed executor of the husband's estate. Shortly after the death of the husband, the executor sold the securities for 160,700 dollars and with that money purchased United States Treasury notes. In July, 1965, the executor sold the notes and distributed the proceeds to the beneficiaries of the husband's estate.

As executor of the wife's estate, the plaintiff filed a fiduciary tax return for the year 1964 reporting that the wife's estate had realized a long-term capital gain from the sale of the securities. This gain was based on the difference between the sale price in 1964 and the fair market value of the securities at the wife's death in 1957, which resulted in a taxable capital gain of almost 95,000 dollars. In December, 1964, the plaintiff filed an amended tax return for the wife's estate claiming that, instead of the long-term capital gain, the estate had realized only a short-term capital gain representing the difference between the sale price in 1964 and the fair market value of the securities at the husband's death in 1964: a gain of approximately one thousand dollars. The plaintiff's claim for refund was disallowed and his suit followed.

The Court of Claims granted the government's motion for summary judgment.[4] The majority reasoned as follows: the plaintiff was acting solely in the capacity as executor of the wife's estate when he sold the securities in 1964 even though his action was taken after the husband's death. Each estate was a separate entity for tax purposes, and no merger of the two estates was accomplished although the plaintiff was acting at the time as executor of both estates. Since the plaintiff failed to show anything in New York law requiring a different result, the wife's estate had realized a long-term taxable capital gain on the difference between the sale price and the fair market value at the wife's death.[5]

The dissent relied on *Brewster v. Gage*,[6] a decision by the Supreme Court in 1930. The plaintiff in *Brewster* was one of the residuary legatees of the estate of his father, who had died in 1918. The father's stocks, the personal property in question, had been distributed in 1920, and the plain-

[4] *Id.* at 770.
[5] *Id.* at 768-70.
[6] 280 U.S. 327 (1930).

tiff had sold some of them in 1920, 1921, and 1922. The Commissioner of Internal Revenue contended that the values of the stocks at the testator's death, rather than at the date of distribution, should have been used to determine capital gains and assessed a deficiency.[7] The district court agreed with the plaintiff's contention that the proper time for determining basis for gains was the date of distribution,[8] but the Court of Appeals for the Second Circuit reversed[9] and held that the date of death was determinative. The Supreme Court affirmed this judgment.[10]

The Supreme Court in *Brewster* relied on basic principles of property law in reaching its decision. Under one of these principles, title to devised real property, both legal and equitable, passes immediately to the devisee; but the legal title to bequeathed personal property passes to the executor. The Court stated that "immediately upon the death of the owner there vests in each of [the legatees] the right to his distributive share of so much as shall remain after proper administration"[11] and that "there vests in the . . . executors, as of the date of the death, title to all personal property belonging to the estate; it is taken, not for themselves, but in the right of others . . . ."[12] The Court emphasized the significance of the date of death of the testator and relegated the date of distribution to secondary importance: "[T]he decree of distribution confers no new right; it merely identifies the property remaining, evidences right of possession in the heirs or legatees and requires the administrators or executors to deliver it to them. The legal title so given relates back to the date of death."[13] The Court concluded that at the testator's death the legatee received an economic interest in the property even though the executor held the legal title and that from the date of death the legatee would be enriched or suffer loss with every increase or decline in the value of the property.[14]

The dissenting judge applied these principles to the facts before the court in *Manufacturers Hanover Trust* and reached a result favorable to the taxpayer. His position was based on the rationale that the basis used in the determination of capital gains should relate to the beneficial

[7] *Id.* at 333.
[8] Brewster v. Gage, 25 F.2d 915 (W.D.N.Y. 1927).
[9] Brewster v. Gage, 30 F.2d 604 (2d Cir. 1929).
[10] 280 U.S. at 337.
[11] *Id.* at 334.
[12] *Id.*
[13] *Id.*
[14] *Id.*

interest in the property. Since at the wife's death the husband acquired a beneficial interest in the property, his basis should have been the fair market value at that date. At the husband's death his legatees (the children) received a stepped-up basis: the fair market value of the property at his death rather than its lesser value at the time that he acquired it. The sale by the executor could only be made for the legatees, the beneficial owners. By focusing on the beneficial interest, the dissenting judge concluded that the only gain realized was the difference between the sale price and the fair market value of the securities on the date of the husband's death.[15]

Section 1014(b)(1) of the Code, which provides that a decedent's estate shall be considered to have acquired property from the decedent for the purpose of applying the general rule[16] for determining basis, does not require a result different from the position taken by the dissent. The estate is a taxable entity, and specific provisions in the Code provide for the taxation of capital gains realized by it.[17] Section 1014(b)(1) allows the estate a stepped-up basis at the death of the decedent. This provision does not preclude the courts from looking at the beneficial interest to compute the basis for capital gains; *Brewster*, in fact, held that they must.

Moreover, courts have focused on the holder of the equitable title in other areas of tax law. An example can be found in the determination of what constitutes a depreciable interest. The basis used to determine depreciation is the same as the basis used in computing capital gains.[18] A case in which the depreciable-interest concept is illustrated is *Helvering v. F. & R. Lazarus & Co.*[19] In that case a bank held the legal title to three buildings used by the taxpayer in his business. The Commissioner disallowed a depreciation deduction on the ground that the deduction followed the legal title. The Supreme Court ruled against the Commissioner. It concluded that since the instrument conveying legal title to the bank was merely a security agreement, the taxpayer, being the equitable owner, should be allowed the depreciation deduction. The Court in *Lazarus* emphasized the "equitable nature of [tax] proceedings" and the concern of tax courts with "substance and realties" rather than formal

[15] 410 F.2d at 770-73 (dissenting opinion).
[16] INT. REV. CODE of 1954, § 1014(a).
[17] *Id.* §§ 641(b), 1202. The majority relied on the separate-entity theory in *Manufacturers Hanover Trust*. 410 F.2d at 770.
[18] *Id.* § 167(g).
[19] 308 U.S. 252 (1939).

documents.[20] In defining depreciable interest, the Court of Appeals for the Ninth Circuit has said:

> It is not the physical property itself, nor the title thereto, which alone entitles the owner to claim depreciation. The statutory allowance is available to him whose interest in the wasting asset is such that he would suffer an economic loss resulting from the deterioration and physical exhaustion . . . .[21]

Clearly equitable ownership was critical in the court's determination of the depreciable interest.

The rationale of the dissent would be equally applicable in determining capital losses and would produce a result different from that which would be reached by using the rationale of the majority. If the securities in *Manufacturers Hanover Trust* had decreased in value between the wife's and the husband's death and then had further declined after the death of the husband, the basis used in determining the loss would, under the view of the dissent, still be the fair market value on the date of the husband's death. In a declining market, the difference between the two computations would be significant if the property was, as in *Manufacturers Hanover Trust*, held over a long period and then sold immediately after the second death.

The validity of the dissent's rationale can be illustrated by posing a situation in which there are multiple legatees. If, in the principal case, the husband had shared the securities with his two children, his portion that was sold by the executor after his death would have received the stepped-up basis while the basis of the children's shares would have remained the fair market value at the time of their mother's death. This difference would have occurred even if the securities had at all times been treated as an entity by the executor, had been acquired from the same decedent, and had been sold simultaneously.

The most serious objection to the view of the majority is that its focus is primarily on the date of distribution and on the status of the plaintiff as executor of the wife's estate on the date of sale. If the securities had been distributed to the husband and had not been sold or exchanged prior to his death, his estate and his legatees would have received a stepped-up basis at his death. If the securities had been distributed to his estate after his death but before sale, an identical result would have followed.

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[20] *Id.* at 255.

[21] Commissioner v. Moore, 207 F.2d 265, 268 (9th Cir. 1953).

The only difference between the latter situations and the actual facts of the case is that the date of distribution occurred both after the husband's death and the executor's sale. *Brewster* held that the decree of distribution gives no new rights and should not be considered in determining basis. By concentrating on the status of the plaintiff as executor of the wife's estate at the time of sale and on the date of distribution, the majority in *Manufacturers Hanover Trust* put form before substance.[22]

The result reached in *Manufacturers Hanover Trust* represents a trap for the unwary. A long period of administration is not unusual, and the conclusion reached by the majority would, *mutatis mutandis*, be equally applicable to a shorter period of administration. The use of a single corporate executor for sucessive estates is not an unusual practice. The likelihood of a corporate executor's serving successive estates has in fact, been greatly increased in North Carolina due to the significant and continuing expansion of the state's larger banks, which now offer trust services that were not available in the past. Executors should be aware when administering successive estates that utmost care should be taken in the choice of dates for the distribution and sale of estate property.

LANNY B. BRIDGERS

Insurance—Liability of Insurers under the Omnibus Clause to Protect Emergency Drivers—The North Carolina Situation

The general effect of an omnibus clause in an automobile liability insurance policy is that one using the automobile with the permission of the named insured becomes an additional insured under the policy.[1] Not only does coverage under the omnibus clause provide the driver with a right against the insurer for indemnification for liability arising out of his use of the vehicle,[2] but such coverage also guarantees at least minimal recovery to an innocent third party who suffers personal injury or prop-

[22] The inequitable result reached by the majority is even more apparent upon consideration of the estate-tax consequences. The fair market value of the securities at the date of the husband's death was used to compute the estate tax on his estate.

[1] 7 J. APPLEMAN, INSURANCE LAW AND PRACTICE § 4354 (1962) [hereinafter cited as APPLEMAN]; 7 D. BLASHFIELD, AUTOMOBILE LAW AND PRACTICE §§ 315.5, .8 (3d ed. 1966) [hereinafter cited as BLASHFIELD].

[2] 7 APPLEMAN § 4354; 7 BLASHFIELD § 315.5. The liability of the insurer is still controlled by the limits of coverage of the policy. 7 APPLEMAN § 4371.