Taxation -- Gift and Estate Taxes -- Tenancy by the Entirety

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Taxation—Gift and Estate Taxes—Tenancy by the Entirety.

A husband purchased a residence in Indiana with his own funds but had the title placed in his wife and himself as tenants by the entirety. The Commissioner of Internal Revenue ruled that so much of the property as passed to the wife was a gift, and a tax measured by the interest of the wife\(^1\) was collected under the Gift Tax Act\(^2\) from the donor.\(^8\) In an action for refund of the tax, which had been paid under protest, the court held the acquisition of property rights by the wife without consideration from her was a gift within the terms of the Act.\(^4\)

One of the fundamental characteristics of the estate by the entirety is unity of person. This unity rests upon the common law fiction that husband and wife are one legal personality, with title to the whole of the property held by the entirety vested in each from the inception of the estate. The husband, in creating this estate in Indiana, vested in his wife a fee simple title to the whole property, subject to these restrictions:

1. neither spouse could transfer any interest in the estate without the consent of the other;\(^5\)
2. each was entitled to the use of the whole estate with the surviving spouse taking no new estate upon the death of the other;\(^6\)
3. income and profits from the land belonged to both and were not subject to execution under a judgment against either;\(^7\) and
4. upon the sale of the property proceeds therefrom were to be equally shared.\(^8\)

In the principal case it is easily discernible that, upon the creation of this estate, the wife secured definite property rights for which she gave no consideration. The husband claimed there was no intent to pass anything of present value, the wife's "use interest" being

\(^1\) U. S. Treas. Reg. 79, Art. 19(8) (This section provides for a measurement of the value of the wife's interest based on the present worth of her right to the use of one-half the estate during the joint lives of her husband and herself and the present worth of her expectancy of survivorship, the value thereof to be computed from mortality tables.)

\(^2\) 47 STAT. 245 (1932), 26 U. S. C. A. §550 (1934) (The Statute providing for a tax upon "the transfer . . . of property by gift" is interpreted to include within its meaning the creation of a tenancy by the entirety, where the husband furnishes all the consideration for the purchase of the property, by U. S. Treas. Reg. 79, Art. 2(7), 19(8).)

\(^3\) 47 STAT. 249 (1932), 26 U. S. C. A. §558 (1934).


\(^5\) See Baker v. Cailor, 206 Ind. 440, 444, 186 N. E. 769, 770 (1933).


\(^7\) Patton v. Rankin, 68 Ind. 245 (1879); Nobile v. Bartletta, 109 N. J. Eq. 119, 156 Atl. 483 (1931). Contra: Raptes v. Papas, 259 Mass. 37, 155 N. E. 787 (1927); Lewis v. Pate, 212 N. C. 253, 193 S. E. 20 (1937). The present day status of the wife's right to share in the usufruct was indicated by Tiffany, who, while speaking of the husband's right to the usufruct, said, "... it has, as being, not an incident of the tenancy by entireties, but merely one of the husband's common law marital rights, been regarded as taken away by the married woman's property acts, so that the husband can no longer assert an exclusive right to rents and profits. . . ." 1 TIFFANY, REAL PROPERTY (2d ed. 1920) §194.

\(^8\) Fogleman v. Shively, 4 Ind. App. 197, 30 N. E. 909 (1892).
merely the fulfillment of his marital obligation to provide a home. Therefore, since the wife's "future interest", her expectancy of survivorship, was questionable as a taxable acquisition, the designation of her accession to such interest as a gift was an unreasonable and invalid construction of the Gift Tax Act.

There is an obvious inconsistency in the Government's position as to the taxable qualities of a tenancy by the entirety. Under the Estate Tax Act, the full value of a tenancy by the entirety, for which a husband provided all the consideration, is included in the gross estate of the husband at the time of his death. In this situation, the wife's acquisition of the property is taxed upon the death of her husband. In the same factual situation after the advent of the Gift Tax Act, the transfer of property interests to the wife is treated as occurring at the time of the creation of the estate by the entirety. Thus the Government vacillates between inconsistent interpretations of the tenancy by the entirety as to the point of time at which taxable transfers occur in such estates. However, it should be pointed out that this inconsistent reasoning works little hardship upon the taxpayer, for the possibility of double taxation is guarded against.

This inconsistency is mirrored in two distinctly different approaches used by the Supreme Court in considering this type of estate for purposes of taxation. In Lang v. Commissioner, an income tax case, in the computation of the profit on a wife's property secured as an estate by the entirety and sold after the husband's death, the question arose as to when she acquired it. The Court ruled that the value at the time of the creation of the estate provided the proper basis for computation, i.e., that she is to be treated as having acquired it at that time. In reaching this decision primary importance was given the legal aspects of the estate's creation by a strict adherence to the technicality that title passes to both spouses per tout et non per my at the time of the estate's creation. Using this approach in examining the transfer of a full fee simple title to the "marital unit", one would consider the wife's acquisition a legal interest in land secured at the inception of the estate. At that time, her interest, which would be technically complete and protected by law, would be equal in all respects to her husband's and,

11 44 Stat. 71 (1926), 26 U. S. C. A. §411(e) (1934); 47 Stat. 278 (1932), 26 U. S. C. A. §413(2) (a) (1934) (These two statutory provisions prevent the husband's having to pay a tax upon an estate by the entirety at the death of his wife if he has furnished all the consideration in the purchase thereof, and avoid the danger of double taxation by deducting from the estate tax the amount paid as a gift tax where overlapping in the imposition of the two taxes occurs.)
as such, would be a fit subject for a gift tax, despite the possibility of her accession to greater economic rights at her husband's death. This legalistic reasoning was substantially that underlying the holding in the principal case.

The other method of approach crystallizes its attention upon the economic interest transferred to the wife in such an estate by the death of her husband. The Supreme Court, in *Tyler v. United States*, 13 used such an approach in upholding Congress' right to apply an estate tax to an estate by the entirety. The Court, on another occasion, said with reference to that decision, "Congress was aware that what was of the essence of a transfer had come to be identified more nearly with a change of economic benefits than with technicalities of title." 14 Thus, the legislative approach to the problem of transfers where the passage of legal title and economic advantages do not coincide in point of time appears to be the economic one. The principal case does not afford a fair test of such a treatment, for the wife's "use interest" constitutes a present economic advantage from the time of the estate's creation; this is true despite its economic insignificance when compared to her rights accruing at her husband's death. It is, also, immaterial that this economic advantage is financially negligible because the property is used as a home place; for, in the event of a change of residence, it would be a source of income, a right to a share of which would by law vest in the wife. Thus, a choice between the two approaches is unnecessary as the same result would probably have been reached had either been used.

A true test of the latter approach would have been presented had this case arisen in North Carolina or Massachusetts. These states, unlike other states which retain the tenancy by the entirety, give exclusive control of the income and profits to the husband. 15 The wife's interest in land in such an estate is truly based on "refinements in title", as it is economically "frozen" until the death of her spouse. Thus, if a husband in these states pays a gift tax and outlives his wife, he will have paid a tax upon a transfer which never occurred in a real and practical sense. A gift tax is a tax upon the transfer of property and not directly upon the property itself; 16 to tax in such a case would be to exalt form over substance. A case arising in one of these states would

13 281 U. S. 497, 50 Sup. Ct. 356, 74 L. ed. 991 (1930) (The Court, speaking of the common law fiction of the "marital unit", said: "This view, when applied to a taxing act, seems quite unsubstantial. The power of taxation ... is not to be restricted by mere legal fictions. Taxation ... is eminently practical, and a practical mind ... would have some difficulty in accepting the conclusion that the death of one of the tenants ... did not have the effect of passing to the survivor substantial rights.")


15 See note 7, *supra*.

16 See note 7, *supra*.

force a choice between the legalistic and economic approaches as the
conflict between the views would be irreconcilable.

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Trade Regulation—Right of Patentee to Control Patented
Article after It Has Passed into the Hands of a Purchaser.

Plaintiff granted a license "to manufacture . . . and sell only for
radio amateur reception, radio experimental reception, and radio broad-
cast reception . . ." certain patented apparatus known as a vacuum-tube
amplifier, the patents to which were held by a patent pool to which the
plaintiff and other large electrical companies belonged. Pursuant to
the license agreement, the licensee attached to each amplifier it sold a
plate bearing the legend: "Licensed only for Radio Amateur, Experi-
mental and Broadcast Reception. . . ."¹

Defendant purchased many amplifiers from the licensee with this
license notice attached and used them in talking motion picture equip-
ment. At the time of the sales the defendant knew that the license did
not contemplate his intended use, and the licensee knew that defendant's
intended use was not authorized by the patentee. The present suit was in-
istituted against the defendant charging infringement of the patents under
which the amplifiers were manufactured and sold by the licensee. The
lower courts held the patents valid and infringed by defendant,² and the
Supreme Court of the United States affirmed³ their decree, Mr. Justice
Black dissenting.

An analysis of the nature of the right conferred by the Patent
Statute⁴ shows that the patentee does not, by virtue of the Act, acquire
the right to make, use, or vend the patented article, these being merely
common law rights existing in any owner of chattels. The only addition
afforded to these rights by the patent law is the power to exclude all
other persons from making, using, or vending the invention or dis-
covery.⁵ The grant of this exclusive right does not mean that it must
be exercised; the article may be wholly withdrawn from the market,⁶

decision, U. S. Sup. Ct., Nov. 21, 1938, Justices Black and Reed dissenting.
invention or discovery.
⁵ See Bloomer v. McQuewan, 14 How. 539, 549, 14 L. ed. 532, 537 (U. S. 1852).