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Taxation

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TAXATION

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It was a quiet year insofar as developments judicial or legislative in the tax law of South Carolina were concerned. The Supreme Court handed down another decision dealing with the pernicious problem of placing the burden of taxation on an estate, where the will does not clearly give the answer. The South Carolina Tax Study Commission issued another excellent annual report, but suggested for this year relatively modest, albeit useful, changes in the law. Most of these changes were adopted by the legislature.

CASES

Apportionment of Death Taxes

Estates of decedents who die domiciled in South Carolina, and whose deaths occur after December 31, 1961, are subject to federal and state estate taxes, the provisions thereof being substantially identical, except for the rates, which are of course very different.[1] For decedents dying on or before that date, the Federal Estate Tax applies, as does the South Carolina inheritance tax[2] and the old Estate Tax.[3] The federal law has few provisions specifically allocating the burden of taxation between the various properties included in the gross estate,[4] and even these provisions operate only if the testator does not direct otherwise. These provisions have been incorporated into the new South Carolina Estate Tax.[5] Generally, state law is determinative as to where the ultimate tax burden will rest,[6] for both federal and state taxes. As far as estate taxes are concerned, federal or state, it has been said that "the testator may prescribe his own law on

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1. The rates in the new South Carolina Estate Tax, Act No. 382 of 1961, vary from 4% to 6% of the taxable estate; the federal rates vary from 3% to 77%.
2. CODE OF LAWS OF SOUTH CAROLINA, §§ 65-451 to 65-529 (1952).
3. CODE OF LAWS OF SOUTH CAROLINA, §§ 65-551 to 65-553 (1952); this law is preserved in the new statute, Article 3, Section 1.
4. INT. REV. CODE OF 1954, §§ 2205 (Reimbursement out of estate); 2206 (liability of life insurance beneficiaries) and 2207 (liability of recipient of property over which decedent had power of appointment).
5. Article 10, Sections 4, 5 and 6 of the new statute.
6. Riggs v. Del Drago, 317 U. S. 95 (1942).

the subject";[7] the testator may prescribe in the will or other instrument where the burden should fall. Thus in a clearly thought out estate plan, the placing of the tax burden can be settled by the dispositive instruments.

Unfortunately, this requires both lawyer and client education as to the pitfalls along the path. The most common failures in planning result from inclusion in the "gross estate" of property which passes outside the will, and augments the amount of tax that is anticipated, sometimes even wiping out the residue of the estate, if the residue must bear the tax; or change in the economic circumstances of the testator, or the valuation of his property, so that a well-laid plan is no longer adequate to meet the new situation.

The Supreme Court in two fine recent decisions tried to make a sensible scheme of taxation for the situation in which the testator does not clearly indicate where the burden of taxation will lie. In *Gaither v. U. S. Trust Co. of N. Y.*,[8] the Court held that where the will makes no mention of placing the tax burden, that burden will fall on the residuary gifts rather than on specific bequests. This decision was felt to be compelled by prior decisions of the Court, so that the interest of *stare decisis* in a rule of property must control. In *Myers v. Sinkler*,[9] the Court had a case in which substantial property had been transferred inter vivos many years before, but with a retained life estate, so that the property was included in the gross estate for federal taxation. The will provided that all taxes "imposed against my estate . . . . shall be paid out of my residuary estate. . . in order that all legacies and bequests made by my Will shall be free from the same". The Supreme Court held that since in this situation the non-probate property was brought into the gross estate by "legislative fiction," equitable apportionment should prevail, and the non-probate property must pay its fair share of the tax burden. The quoted language was found to evidence an intent only to burden the residue with the taxes attributable to the probate estate.

In *Dial v. Ridgewood Tuberculosis Sanatorium*,[10] the Supreme Court was again faced with this problem. Testatrix

7. TRACHTMAN, ESTATE PLANNING 48 (1961).
8. 230 S. C. 568, 97 S. E. 2d 24 (1957), discussed in ANNUAL SURVEY, 10 S.C.L.Q. 131-135 (1957).
9. 235 S. C. 162, 110 S. E. 2d 241 (1959), discussed in ANNUAL SURVEY, 13 S.C.L.Q. 381-383 (1961).
10. 240 S. C. 64, 124 S. E. 2d 598 (1962).

Mrs. Seibels died leaving probate property of an appraised value of $294,000. She also had a general testamentary power of appointment over property in a trust estate left by the will of her husband, the value of the corpus of the trust being appraised at $207,000. Testatrix' will contained a clause directing that all death taxes be paid by her executors from her residuary estate. It was stipulated that testatrix' Columbia, South Carolina, counsel wrote to her advising that the trust property would be taxed as part of her estate. Her will exercised the power of appointment granted her in her husband's will, the language of exercise being the same dispositive language that she used in disposing of her own property. The Supreme Court, per Mr. Justice Legge, held that her intention was to charge her residuary estate with the entire burden of death taxes, including the taxes resulting from the inclusion of the non-probate property.[10a]

License Taxes — "Corporation for Profit"

In *Coble Dairy Products Co-op., Inc. v. Livingston*,[11] the taxpayer co-operative sued to recover taxes paid under protest. The Tax Commission assessed against taxpayer additional corporate license tax for the years 1956, 1957 and 1958, pursuant to Section 65-621 of the 1952 Code, which then read, "Every corporation organized under the laws of this [State] to do business for profit, . . . and every corporation organized to do business for profit under the laws of any other state, doing business in this State . . . shall . . . make a report annually . . . ."[12] Section 65-625 levied the license tax on such corporations. In 1959, the legislature amended the statute *inter alia* by deleting the words "for profit" as

10a. Respondent argued that both Myers v. Sinkler, the leading authority determining the law of the state, and I.R.C. § 2207, called for a determination that the appointed property and not the residue should bear the tax "in the absence of a clear intent to the contrary in the decedent's will." Respondent's brief, p. 2. The language in the Internal Revenue Code is, "Unless the decedent directs otherwise in his will. . . . ." In Myers v. Sinkler, the Court cited with approval Hooker v. Drayton, 69 R.I. 290, 33 A. 2d 206, 150 A.L.R. 723 (1943), which said, "In the absence of a clearly expressed intent to the contrary in the decedent donee's will, such tax is ultimately to be borne by the appointed property, and not by his residuary estate." 235 S. C., 172. However, Mr. Justice Legge's opinion in Myers does not seem elsewhere to suggest the imposition of a higher standard of conviction that that required in any question of determining the intent of the testator from the language of the will.

11. 239 S. C. 401, 123 S. E. 2d 301 (1961).

12. CODE OF LAWS OF SOUTH CAROLINA, §§ 65-621 et seq contains the directly relevant sections.

they applied to foreign corporations, but, as the Court points out, the change had no effect on the legality of the assessment in this case. The Supreme Court, in an opinion by Mr. Justice Moss, held that the taxpayer was not a corporation organized for profit as an entity, but rather for the profits of its producer members.[13] Consequently, the Court held that the Tax Commission was without authority to require the filing of annual reports of the assessment of the license tax.

LEGISLATION

The South Carolina Tax Study Commission continued to labor to improve the statutes governing taxation in the state, and issued its Third Annual Report. The Study Commission expressed sentiments that are worthy of constant consideration in formulating both national and state revenue policies:[14]

> The revenue system in South Carolina, as in most states, is one largely dependent upon self-assessment by the taxpayer. . . .
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> A self-assessment system of taxation depends upon general voluntary compliance by the public which, in turn, stems from public confidence. Public confidence comes when and to the degree that each taxpayer is convinced: (1) that the taxes levied are fair and reasonable, (2) that taxes are uniformly applied to and collected from all taxpayers, and (3) that the funds collected are spent wisely and efficiently for proper governmental functions. All of these criteria might be summarized in one word, fairness. The more widespread this feeling of fairness, then the more widespread will be public acceptance and consent to the system of self assessment, the inevitable result being increased collections.

The breadth of the work of the Study Commission is indicated in the bills that were passed this year by the legislature, three in the property tax field,[15] seven relating to in-

13. The Court quoted the North Carolina Co-operative Marketing Act, G.S. § 54-130, providing that "Associations organized hereunder shall be deemed nonprofit, inasmuch as they are not organized to make profit for themselves, as such, or for their members, as such, but only for their members as producers." The Court noted that an identical provision is included in CODE OF LAWS OF SOUTH CAROLINA, § 12-902 (1952).
14. THIRD ANNUAL REPORT, p. 7 (1962).
15. Act No. 709 of 1961, p. 1705; Act Nos. 819 and 820, id p. 1964 et seq.

come taxes[16] and six affecting other taxes.[17] In addition, the legislature passed an important piece of legislation not discussed in the Report of the Tax Study Commission, the Unincorporated Professional Association Act.[18] This statute is designed to permit an unincorporated organization to qualify as an "association" within the federal tax laws[19] and thereby meet the conditions for establishment of a qualified pension plan.[20]

16. Act Nos. 821 through 827, id p. 1967 et seq.
17. Act Nos. 870 through 875, id p. 2163 et seq.
18. Act No. 784, *id* p. 1911. See discussion in Lipton, Recent Legislation, 14 S.C.L.Q. 487 at 488-489 (1962).
19. INTERNAL REVENUE CODE OF 1954, § 7701 (a) (3).
20. *Id* §§ 401-404.