HWN:lnc
483:45:OLC
Op. 56-47

April 9, 1956

Honorable Earl W. Fase
Tax Commissioner
Territory of Hawaii
Honolulu 9, Hawaii

Attention: J. M. Bell

Dear Sir:

Reference is made to yours of March 6, 1956, seeking our advice as to the inheritance tax (Chapter 103, Revised Laws of Hawaii 1945) incidence under the following factual situation:

Elsie Hart Wilcox, hereinafter called Settlor, died in 1954. Settlor executed a trust deed in 1938, whereby she conveyed to Bishop Trust Company, hereinafter called trustee, certain personal property. The trust deed provided that the net income was payable to a charitable trust during the life of the settlor, and upon her death was payable to certain named nephews and nieces of the settlor, hereinafter called beneficiaries, for their lives. Twenty years after the death of the last surviving niece or nephew the trust was to terminate and the principal and accumulated income was to be distributed to the persons entitled to the income of the trust immediately prior to its termination. If all lawful issue of said beneficiaries should die prior to said twenty year period, then upon the death of the last survivor of said lawful issue, the trust was to terminate and be distributed to those persons who would be the heirs at law of the settlor under the laws of descent in force in the Territory if she had died intestate at that time. The settlor reserved no power to revoke, amend or alter the trust deed or any provisions thereof.

Query: Is the above described transfer made by the settlor in 1938, taxable under the provisions of Chapter 104, Revised Laws of Hawaii 1945, as amended upon her death in 1954?

The solution to the above described question turns upon an interpretation of section 5552, Revised Laws of Hawaii 1945, as amended. Since the property transferred by the settlor

was not transferred by will or the intestate laws of the Territory, and since the transfer would seem dearly not to have been made in contemplation of death, the question of taxability must turn on the intrepretation of the following language contained in said section 5552:

> "All property ... which or any interest in or income from which, shall be transferred by deed, grant, sale or gift ... intended to take effect in possession or enjoyment after such death, to any person or persons, ... in trust or otherwise, or by reason whereof any person ... shall become beneficially entitled, in possession or expectancy, to any property, or to the income thereof, shall be and is subject to a tax ... ."

The above language was considered and passed upon by the Supreme Court of the Territory of Hawaii in the case of Brown v. Treasurer, 20 Haw. 41. The fact situation therein was substantially different from the problem here involved for therein the settlor retained a beneficial interest during his life as well as a power of revocation. However, the court did hold that property could be taxed upon the death of the settlor even though it did not pass by will or descent or by transfer from one dying seized or possessed of it.

This office has also had occasion to interpret the above language. In opinions No. 1365 (1925-1926), 1406 (1927-1928) and 1858 (1946) it was held that a transfer during the decedent's lifetime, wherein he retained the income from the property transferred, but did not retain a power of revocation was taxable upon his death as a transfer intended to take effect in possession and enjoyment at or after death.

Although there has been no determination of the exact question before us in this jurisdiction, there have been numerous cases in other jurisdictions dealing with the problem under statutes such as ours. However, prior to discussing those cases mention should be made of cases decided under the federal estate tax law which law also contains a provision for the taxation of an estate when a transfer has been made so as to take effect in possession and enjoyment at or after death. It is our opinion that those cases are clearly distinguishable from the problem confronting us.

This office has previously ruled that the interpretation of section 5552 is not necessarily to be controlled by the interpretations by the federal courts of the federal estate tax law. See Op. 1858, (1946). This conclusion has also been reached by numerous state jurisdictions. See case

citations in Op. 1858 and Chase v. Commissioner of Taxation, (1948) 226 Minn. 521, 33 N.W. 2d 706; In Re Madison's Estate, (1945) 26 Cal. 2d 453, 159 P. 2d 630. The above, however, is not to indicate that there are not Federal cases which hold that such a transfer as here involved is taxable. See. Coolidge v. Nichols, (1925) 4 F.2d 112 (aff'd (1927) 274 U.S. 531).

There is an inherent distinction between an inheritance tax, with which we are confronted, and an estate tax, under which the Federal cases have been decided. That the language in both types of statutes is identical is immaterial. An estate tax is levied on the privilege of transfering one's property at death, whereas an inheritance tax is levied on the privilege of receiving property upon the death or the donor.

Under the Federal estate tax, a transfer whereby the donor presently divests himself absolutely and irrevocably of the title and control over the property is not taxable as a transfer to take effect in possession and enjoyment at or after death even though the remainder interest in the trust is not to come into effect until at or after death. The reasoning supporting the conclusion is that it is the original transfer to the trustee rather than the subsequent transfer to the beneficiary which governs the application of that statute.

Under state inheritance tax statutes where the incidence of the tax imposed is upon the recipient of the gift, rather than upon the estate of the settlor, there is a divergence of opinion as to whether a transfer such as this is subject to the tax as one intended to take effect in possession or enjoyment at or after the death of the settlor. However, it is the opinion of this office that the majority of the jurisdictions and the better reasoned cases hold that such a transfer is taxable. Some of the cases holding such a transfer to be not taxable found their reasoning in the Federal type cases, which, as pointed out above, we do not believe to be sound when applied to an inheritance tax. See Highfield v. Equitable Trust Co., (1931) 34 Del. 509, 155 A. 724.

Typical of cases upholding taxability of such transfers is the case of In re Hollander's Estate, (1938) 123 N.J.hq. 52, 195 A. 805, wherein the trust instrument provided that the income would be paid to the wife of the settlor for the life of the settlor and upon the settlor's death the corpus was to be conveyed to the wife, her heirs or assigns. In holding the remainder taxable under an inheritance statute the court said:

"... a presently effective transfer by a donor inter vivos, of a separately and specifically expressed remainder interest, where such remainder interest is expressed to commence at a time at or after the death of the donor, is taxable under our statute; notwithstanding that by the very same act or instrument of transfer the donor simultaneously transfers all other interests in the same property and thereby completely and presently divests himself of all interest or possibility of interest in the property as a whole.

...

The test of taxability is not the time of the complete divesting of the transferor's interest or owership; it is the time of the complete succession by the transferee. Where there is a transfer of a specific interest in property and the succession of the transferee does not become, and under the terms of the transfer is not to become, complete until a time at or after the death of the transferor, that transfer is taxable. 'The distinction ... rests on ... whether the donee is deprived of an interest of some kind ... until the donor's death,'..."

In the case of In re Madison's Estate, (l945) 26 Cal. 2d 553, 159 P. 2d 630, wherein by a trust instrument the settlor had divested himself of all interest in certain property, with the income payable to his children during his life with the remainder to said children or their heirs upon his demise, the court held that the gifts were intended to take effect in possession or enjoyment at or after the death of the settlor and said:

"The issue is not whether the donor retained some power or interest until his death, but rather whether he tied up the property with so many strings, which could not be loosened until his death, that the transfer may be regarded as having been intended to take effect in possession or enjoyment at his death within the meaning of the statute. It should be noted at the outset that the statute speaks, not of title, but of possession and enjoyment."

It was said in In re Dunlap's Estate, 199 N.Y.S. 147 that:

"There was no transfer of possession and enjoyment of the remainders to the beneficiaries until the death

of ... the grantor. The trust deed smacks of an intent to withhold a vesting or possession and enjoyment in the three beneficiaries in the corpus of their respective shares in the remainder until the termination of the life of the grantor. The estate to the daughters during her life granted income only. The transfer upon her death was of the corpus of the three-fourths of the trust estate to the surviving beneficiaries or their issue. There was therefore a transfer here of an estate to the daughters or their issue or survivors, intended to take effect in possession or enjoyment at and after the death of the grantor, and the transfer is taxable ..."

In Chase v. Commissioner of Taxation, 226 Minn. 521, 33 N.W. 2d 706, the taxpayer argued that the donor having reserved nothing to herself and having completely divested herself of all right to and control over both income and principal of the trust, the transfer constituted a gift inter vivos and was not a transfer intended to take effect in possession or enjoyment at or after such death. Discussing the Madison and the Hollander cases, supra, the court said:

"It is apparent from these cases that the state courts above referred to, in upholding taxation of transfers of this kind, place their reliance upon the statutory expression 'intended to take effect in possession or enjoyment' as having reference to the donee's acquisition of final and complete title, rather than to the action of the donor in divesting himself of power and control at the time the transfer is made."

The court took the position that the acquisition of possession or enjoyment by the donee should govern and repudiated the theory of the Federal cases that divestiture of title and control by the doner should be determiniative, using the following language:

"... the tax is imposed not because of what occurs at the time of the original transfer, nor because the donor may have reserved some interest in the income or principal of the trust, but rather because 'The thing burdened' was 'the right to receive' and because upon the death of the donor there was 'a succession, a coming into or increasing of enjoyment and dominion an enlargement of property rights' ... a completion of title."

...

"... we are committed to the reasoning followed by the

> other state courts, to the effect that the tax should be imposed when the ultimate complete possession and enjoyment and the final vesting of the title of the principal in the beneficiaries is made contingent upon, or takes effect at or after, the death of the donor."

Other cases following this line of reasoning are Bryant v. Hackett, (1934) 118 Conn. 233, 171 A. 664; Coolidge v. Commissioner of Taxation, (1929) 268 Mass. 443, 167 N.E. 757; In re Patterson's Estate, (1910) 127 N.Y.S. 284. For cases to the contrary see In re Townsend's Estate, (1944) 349 Pa. 162, 36 A.2d 438; People v. Northern Trust Co., (1928) 330 Ill. 238, 161 N.E. 525; and dictum In re Brockett's Estate, (1932) 111 N.J. Eq. 183, 162 A. 150.

In the light of the above authorities, it is our opinion that the transfer by the settlor, Elsie Wilcox, was intended to take effect in possession and enjoyment at or after death within the meaning of section 5552 and therefore is taxable.

Respectfully yours,

HAROLD K. NICKELSEN
Deputy Attorney General

APPROVED:

EDWARD N. SYLVA
Attorney General