DEPARTMENT OF REVENUE: INCOME TAX REGULATION: Federal estate taxes are deductible on the State income tax return of the Estate paying said taxes. Gift taxes are deductible on a State income tax return by the taxpayer who pays such tax.

October 13, 1950

FILED

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Mr. T. R. Allen
Supervisor, Income Tax
Department of Revenue
Jefferson City, Missouri

Dear Mr. Allen:

This will acknowledge receiving the following request for an official opinion, which request is as follows:

> "A ruling is desired from your office regarding the interpretation of the State Income Tax Statutes, Section 11349, R.S.A. 1939, in regard to the Subdivision under this Section captioned Taxes, which reads as follows:
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> 'All taxes paid within the year imposed by the authority of the United States or its territories or possessions, or foreign country or under authority of any state, county, school district or municipality or other taxing subdivision of any state or country, not including those assessed against local benefits and inheritance taxes and taxes based on income, except those imposed by the United States on incomes.'
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> "In connection with this paragraph, I also wish to quote herewith a ruling with regard to deductions in connection with administration of the State Income Tax Law as promulgated by the Department of Revenue which was filed with the Secretary of State under date of January 5, 1950, which in part read as follows:
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> ' * * * not including those assessed against local benefits and inheritance, estate or gift taxes * * *'
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> "The ruling referred to above has been questioned with respect to federal estate taxes. The inclusion in

> this ruling of gift and estate taxes is made by this department having been added on the basis that estate and gift taxes and inheritance taxes are of a like nature, properties received through inheritance, estate or by gift represents something of value received by endowment or gift without being actually purchased.
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> "It is the contention of this department that inasmuch as the statutes disallow the deduction of inheritance taxes in arriving at taxable income, that likewise estate and gift taxes should also be disallowed as a proper deduction. Properties received under any of the three classifications are primarily not the result of income and it is the firm conviction of this department that there was no intent on the part of our legislature in the passage of this section of the income tax law to allow such deduction for income tax purposes.
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> "I might refer to the fact with respect to federal estate taxes that they were at one time classified as inheritance tax and in later years the classification was changed to estate taxes. Under the circumstances it is felt that this department was justified in the promulgation of the ruling which is now being contested."

Section 11349, R. S. Mo. 1939, as amended by Laws 1947, Volume 1, pages 531 and 532, provides, in part, as follows:

> "All taxes paid within the year imposed by the authority of the United States or its territories or possessions, or foreign country or under authority of any state, county, school district or municipality or other taxing subdivision of any state or country, not including those assessed against local benefits and inheritance taxes and taxes based on income, except those imposed by the United States on incomes.
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> "Income on which tax is paid in another state or country: Such part of the income in any taxable year on which a tax is imposed by any other state or country and paid to such state or country shall be deducted where such income is included in the taxpayer's return, but such credit shall not exceed such proportion of the tax payable under this Act as the income subject to tax in such other state or country bears to the taxpayer's

net income upon which the tax is imposed by this Act.

The beginning of this section says "In ascertaining net income there may be deducted from gross income derived during the same period the following:" This section does not include estate or gift taxes as the taxes that are excluded from the right to be deducted from gross income by the taxpayer. Your regulation inserts the words estate or gift taxes to supply the omission on the part of the Legislature to use such taxes in the exclusionary clause.

Cooley on Taxation, Vol. 4, Section 1721 defines inheritance tax as follows:

> "An inheritance tax is a tax on the privilege of transmitting or receiving property after death as distinguished from a tax on the property affected. It is a tax on the privilege of succeeding to the inheritance or of becoming a beneficiary under the will. The subject of the tax is the transmission from the dead to the living, not the thing transmitted. It is a bonus exacted from the kindred and others 'as the condition on which they may be admitted to take the estate left by a deceased relative or testator.' The term 'inheritance tax,' as generally employed, applies to all transmissions of property occasioned by the death of the owner, whether transmissions by operation of law where one dies intestate, by will, by gifts causa mortis, or by disposition inter vivos in contemplation of death. While the generic term 'Inheritance taxation' is used for convenience it is strictly speaking inaccurate, it has been said by the latest work on this subject which further says: 'For example the federal estate tax is not a tax on inheritances but an impost upon estates, levied before anything reaches the beneficiary. Theoretically this tax is on the transfer from the dead to the living imposed upon the right of the decedent to transmit his property and not upon the right of the beneficiary to receive it. As the tax is on the transfer the term used in the New York statute "Transfer Tax" would seem to be more apt. "A tax levied upon any

> form of donative transfer from the dead to the living in contemplation of or effective at death" would seem to cover the various taxes imposed by the states of the union and the federal government under the general subject of inheritance taxation.'"

Section 1722 of this same work defines estate tax as follows:

> "These taxes are sometimes divided into (1) inheritance taxes and (2) estate taxes according to whether the tax is based on the estate or interest of the deceased or the estate or interest of the living, i.e., the heirs or devisees. An 'estate tax' taxes not the interest to which some person succeeds on a death, but the interest which ceased by reason of the death; while an 'inheritance tax' is based on the interest to which the living succeeds. The tax on the right to receive property under a will is to be distinguished from the tax on the right to transmit it. In most states the tax is based on the right to receive property; but in some states the tax is on the right to transmit; and the federal statute is of the latter kind."

Cooley on Taxation, Vol. 4, Sec. 1759, says:

> "Income tax statutes, whether a federal statute or a state, are subject to the rule of strict construction the same as other tax statutes; but it is the duty of the courts to observe the fundamental rule to ascertain and give effect to the intention of the legislature. The statute should receive a practical interpretation. 'Persons' is construed as including corporations."

The Taxing Power, State Income Taxation by Tuller, page 362, considers the difference between deductions and exemptions and says:

> "The legislative assumption above referred to has probably arisen out of a failure to differentiate between deductions on the one hand and exemptions on the other. They are inherently different things.

Deductions may be defined as expenses properly incurred and losses actually suffered. These must be substracted from the gross income of the taxpayer, in order to determine what is, in fact, his net income. This is a matter of fact, not a matter of legislative discretion or grace. Exemptions, on the other hand, are subtractions made from net income. Whether any exemptions shall be allowed is in all probability entirely a matter of legislative discretion and grace. But because the Legislature may tax the entire net income, and so may refuse to allow exemptions to be subtracted from net income in arriving at the base on which the tax shall be computed, it does not at all follow that it may prescribe what deductions shall be made from gross receipts in order to arrive at the net income which shall be taxed. They are two entirely different things and are governed by different principles. The former is a matter of law. But whether the income taxed is actually net is a matter of fact.

"It seems inescapable that if the Legislature refuses to allow any necessary and proper element of expense to be deducted from gross income, the tax is, to that extent, not a tax on net income, but a tax on gross receipts. Insofar as existing state statutes attempt to tax gross income, they are believed to be unconstitutional and void. * * *"

The rule concerning the construction of tax statutes is also considered in 51 Am. Jur., Sec. 310, page 361, in which we find the following statement:

"The intention of the legislature with respect to tax statutes must, as in the case of statutes generally, be ascertained from the language of the act. As has been frequently pointed out, a tax cannot be imposed without clear and express language for that purpose. Unless the context shows that they are differently used, the words employed are to be given their ordinary meaning, and the effect of the statute is not to be extended by implication or forced construction beyond the clear meaning or import of the language used; nor is its operation to be enlarged to embrace matters not specifically point out.

* * * * * * *

"The literal meaning of the words employed in tax statutes is most important, and the general rule requiring adherence to the letter in construing statutes applies with peculiar strictness to tax laws. The rule may not, however, be carried so far as to reduce a taxing statute to empty declarations, to require that to be done which the law does not authorize, or to violate a fundamental principle upon which the government is founded and operated."

A further statement of the rule of construction is found in 51 Am. Jur. Section 316, page 366:

"Although it is sometimes broadly stated either that tax laws are to be strictly construed or, on the other hand, that such enactment are to be liberally construed, this apparent conflict of opinions can be reconciled if it is borne in mind that the correct rule appears to be that where the intent or meaning of tax statutes, or statutes levying taxes, is doubtful, they are, unless a contrary legislative intention appears, to be construed most strongly against the government and in favor of the taxpayer or citizen. Any doubts as to their meaning are to be resolved against the taxing authority and in favor of the taxpayer, or, as it is sometimes put, the person upon whom it is sought to impose the burden. * * *"

The rule of construction is also stated in 47 C.J.S., Sec. 53, page 173, as follows:

"As a general rule internal revenue laws are to be construed liberally in favor of the taxpayer, and strictly or most strongly against the government; and doubts concerning their interpretation or application must be resolved most strongly against the government and in favor of the taxpayer. Before the property of a citizen can be taken under the exercise of the taxing power it is necessary that the statute be clear and unambiguous. The rule applies to statutes laying a tax, to limitation provisions, to words of exception confining the operation of the duty, and to remedial statutes intended to grant relief to

> taxpayers, although it has been held that a statute relative to the recovery of taxes paid must be strictly construed, as it is in derogation of the sovereign immunity from suit. Also laws for the redemption of property from sales for taxes have been construed favorably to the owner of the land.
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> "The rule of liberal construction in favor of the taxpayer does not, however, require the court to reject the plain and reasonable meaning of a statute, or change the rule considered supra Sec. 51, that the language used must be given its usual and ordinary meaning. The revenue acts should receive a fair, reasonable, and, according to some authorities, liberal construction such as will not endanger public interests, and so as effectually to accomplish their purpose, and not permit evasions on merely fanciful and unsubstantial distinctions or make the statute a practical nullity on account of the ease of its evasions."

Gift taxes are defined in 47 C.J.S., Sec. 504, page 732, as follows:

> "The Internal Revenue Code, 26 U.S.C.A. Sec. 1000, and similar statutes, impose a tax on the transfer by any individual of property by gift. This tax is not a direct tax on property as such, and its imposition does not rest on general ownership; but it is an excise on the use made of property, on the exertion of the privilege of transmitting title by gift. The gift and estate tax laws, as discussed supra Sec. 478 are closely related and the gift tax serves to supplement the estate tax. The gift tax, however, was passed not only to prevent estate tax avoidance, but also to prevent income tax avoidance by reducing yearly income and thereby escaping the effect of progressive surtax rates."

Estate taxes are not deductible now on federal income tax returns but under prior statutes federal estate taxes were deductible in computing the net income of an estate because the federal statute allowing the deduction of all taxes paid by the taxpayer did not exclude estate taxes. Such taxes are deductible only by the personal representative of the decedent, and not by a beneficiary or legatee of the estate (see cases cited in 47 C.J.S., Sec. 349, page 510, footnote 95).

27 Am. Jur. Sec. 11, page 369, says:

> "The amount paid or payable as inheritance, estate or successive taxes was formerly deductible in computing the Federal income tax of a decedent's estate, and in some instances, in computing the tax of individual beneficiaries. But such deductions are now denied by an express statutory provision.
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> "In the absence of statutory provisions expressly denying a deduction on account of inheritance, estate or succession taxes, the amount paid or payable in respect of such taxes has been held deductible in computing the state income tax of a decedent's estate."

The leading case on the question whether or not an estate tax could be deducted on an income tax return of the estate prior to the enactment of the federal revenue laws excluding the deduction of estate taxes on income tax returns was the case of U.S. v. Woodward, 41 S.C. 615, 256 U.S. 632, 65 L. Ed. 1131, in which the Supreme Court of the United States said:

> "The solution of the question turns entirely upon the statutory provisions under which the two taxes were severally collected. The Act of 1918, by Secs. 210, 211, and 219, subjects the net income 'received by estates of deceased persons during the period of administration or settlement' to an income tax measured by fixed percentages thereof; by Secs. 212 and 219 requires that the net income, as defined in Sec. 213, and making the deductions named in Sec. 214, and by Sec. 214 makes express provision for the deduction of 'taxes paid or accrued within the taxable year, imposed (a) by the authority of the United States, except income, war-profits and excess-profits taxes.' This last provision is the important one here. It is not ambiguous but explicit, and leaves little room for construction.

The words of its major clause are comprehensive and include every tax which is charged against the estate by the authority of the United States. The excepting clause specifically enumerates what is to be excepted. The implication from the latter is that the taxes which it enumerates would be within the major clause were they not expressly excepted, and also that there was no purpose to except any others. Estate taxes were as well known at the time the provision was framed as the ones particularly excepted. Indeed, the same act, by Secs. 400-410, expressly provides for their continued imposition and enforcement. Thus, their omission from the excepting clause means that Congress did not intend to except them.

"The Act of 1916 calls the estate tax a 'tax,' and particuarly denominates it an 'estate tax.' This court recently has recognized that it is a duty or excise, and is imposed in the exertion of the taxing power of the United States. New York Trust Co. v. Eisner, 256 U.S. 345, ante, 963, 16 A.L.R. 660, 41 Sup. Ct. Rep. 506. It is made a charge on the estate, and is to be paid out of it by the administrator or executor, substantially as other taxes and charges are paid. It becomes due not at the time of the decedent's death, as suggested by counsel for the government, but one year thereafter, as the statute plainly provides. It does not segregate any part of the estate from the rest, and keep it from passing to the administrator or executor for purposes of administration, as counsel contend, but is made a general charge on the gross estate, and is to be paid in money out of any available funds, or, if there be none, by converting other property into money for the purpose.

"Here the estate tax not only 'accrued,' which means, became due, during the taxable year of 1918, but it was paid before the income for that year was returned or required to be returned. When the return was made, the executors claimed a deduction by reason of that tax. We hold that, under the terms of the Act of 1918, the deduction should have been allowed."

This case was cited with approval in the case of Farmer's Loan and Trust Company vs. United States, 9 Fed. 688, l.c. 690, in which the court said:

> "In providing for the deduction of 'taxes paid within the taxable year,' the statute in an exempting clause enumerates what taxes are to be excepted, which implies a purpose not to except others. U.S. v. Woodward, 256 U.S. 632, 41 S. Ct. 615, 65 L. Ed. 1131. Such taxes as those here in question are not within the exception, and the courts cannot add exceptions to those specifically enumerated by Congress. The executors were required to pay the taxes as an incident in the administration and settlement of the estate. They were paid, not for the account of the devisee and legatees, but in reality for the decedent's account as a tax upon her right to transmit. * * *"

30 Am. Jur., Sec. 3, page 109, states in part as follows:

> "The words of a revenue statute are generally interpreted in their ordinary and accepted meaning; and such a statute is to be given a sensible construction. But the courts cannot supply omissions in internal revenue laws."

CONCLUSION

It is the opinion of this department that the regulation, promulgated by the Department of Revenue and filed with the Secretary of State on January 5, 1950, in which estate taxes and/or gift taxes are not allowed as a deduction in connection with a state income tax return, is invalid and beyond the power of the Department of Revenue. Federal estate taxes may be deducted on the state income tax return of the estate paying such taxes. Gift taxes may be deducted on a state income tax return by the taxpayer paying the gift taxes.

Respectfully submitted,

APPROVED:

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