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The Applicability of State Inheritance Tax Statutes to United States Savings Bonds

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THE APPLICABILITY OF STATE INHERITANCE TAX STATUTES TO UNITED STATES SAVINGS BONDS

United States Savings Bonds when issued to individuals may be registered in three forms: (1) in the name of one person; (2) in the names of two persons in the alternative as co-owners; and (3) in the name of one person payable on death to one other person. States may impose inheritance taxes upon these bonds.

The federal regulations provide that a bond registered in the names of two persons as co-owners will be reissued or paid as follows:

(1) "During the lives of both co-owners the bonds will be paid to either co-owner upon his separate request without requiring the signature of the other co-owner; and upon payment to either co-owner the other person shall cease to have any interest in the bond"; and (2) "If either co-owner dies without having presented and surrendered the bonds for payment or authorized reissue, the surviving co-owner will be recognized as the sole and absolute owner of the bond and payment or reissue will be made only to such survivor, as though the bonds were registered in his name alone."

1 31 C.F.R. §§ 315.4, 315.5, 315.6 (Supp. 1956).
3 31 C.F.R. § 315.45 (Supp. 1956); In re Kaspari's Estate, 71 N.W.2d 558 (N.D. 1955).
A savings bond registered in the name of one person payable on
death to another "will be paid to the registered owner during his
lifetime . . . as though no beneficiary had been named. . . . The
bond will be reissued, on the . . . request of the registered owner,
to name the beneficiary designated on the bond as co-owner. The
bond will also be reissued upon the . . . request of the registered
owner together with the . . . consent of the designated beneficiary,
to eliminate such beneficiary. . . . If the beneficiary should pre-
decease the registered owner . . . the bond may be reissued as though
it were registered in his name alone."4 These regulations have been
held to be part of the provisions of the bonds.5

Although the federal regulations6 clearly establish the power of
a state to impose an inheritance tax on savings bonds, the question
remains as to whether or not the statutory language covers the
particular form of registration. This is to be determined by the
state court.7

The pertinent parts of the West Virginia inheritance tax statute8
are as follows:

A tax is to be imposed on the transfer of property, if such trans-
fer be: "(c) . . . intended to take effect in possession or enjoyment
at or after such death; (d) by any person who shall transfer any
property which he owns, or shall cause any property to which he is
absolutely entitled to be transferred to or vested in himself and any
other person jointly, with the right of survivorship, . . . in such other
person, a transfer shall be deemed to occur and to be taxable . . .
upon the vesting of such title in the survivor. . . ."

Sole Form

The sole form of registration is plainly subject to the general
state inheritance tax statute.9

Beneficiary Form

When the beneficiary form "A, payable on death to B," is used,
there ordinarily should be no difficulty in imposing an inheritance

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4 31 C.F.R. § 315.46 (Supp. 1956).
6 Supra note 2.
7 In re Brown's Estate, 122 Mont. 451, 206 P.2d 816, 823 (1949) (dissent).
8 W. Va. Code c. 11, art. 11, § 1 (Michie 1955).
9 Supra note 2.
tax on the bond on A's death. The majority rule concerning the beneficiary form is that when the co-owner dies the regulations confer absolute title on the survivor and do not merely designate persons to receive payments. Although it is a question of statutory construction, a transfer is so clearly taking place on A's death that there should be no doubt as to the applicability of the general inheritance tax statute. In Mitchell v. Carson the Tennessee court held the beneficiary form taxable. There, A retained possession of the bonds. The court decided that due to this retention, B's ownership took effect in possession and enjoyment upon A's death. A had an interest that ended only by his death. Section (c) of the West Virginia inheritance tax statute would be applicable to impose a tax in this situation.

A few courts have used the theory that the beneficiary acquires a presently vested, though defeasible interest, when the bonds are purchased and that the decedent's death ended his rights, thereby leaving the beneficiary with an indefeasible right. However, the more accurate rationale appears to be that no present full interest is created in the beneficiary, but that the only present interest created is "that the beneficiary could not be changed while the bond remained outstanding and upon the death of the donor the outstanding bond belonged absolutely to the surviving beneficiary."

"A and B" Form

When bonds are registered in the form of "A and B" it has been held that the registrants are joint owners and upon the death of one of them, his share in the bonds would be included in his estate and

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12 186 Tenn. 228, 209 S.W.2d 20 (1948); accord, Hallett v. Bailey, 143 Me. 1, 54 A.2d 533 (1947); Succession of Raborn, 210 La. 1033, 29 So. 2d 53 (1946).

13 Supra note 8.


15 In re De Santo's Estate, 142 Ohio St. 223, 51 N.E.2d 639 (1943).
the survivor would retain the other half interest.\textsuperscript{16} Under this theory a tax could be imposed upon one-half the value of the bonds at most. But in \textit{In re Messerschmidt's Estate},\textsuperscript{17} where the purchaser retained possession, the full value of the bonds was taxed on his death. While in \textit{In re Comb's Estate}\textsuperscript{18} the court held that the amount of the bonds which was not contributed by the survivor is taxable. The theory used in the \textit{Messerschmidt} case would be applicable to impose a tax under section (c)\textsuperscript{19} of the West Virginia statute.

\textbf{"A or B" Form}

Under the general rule when bonds are registered in the form of "A or B", a federal contract is created between the purchaser and the United States Government.\textsuperscript{20} States do not have the power to modify such contracts. The terms of the contract and not state laws are used to determine the rights of the surviving co-owner.\textsuperscript{21}

The "or" form of bonds may be surrounded by numerous factual situations a few of which will be discussed. First let us consider the situation in which the decedent paid for the bonds and retained possession of them. A Tennessee court\textsuperscript{22} found on these facts that the decedent "owned an interest in these bonds which at her option was determinable only by her death." That by reason of the decedent's retention, the possession and enjoyment of the bonds by the survivor took effect only upon the decedent's death. As a result, these bonds were included in the language of the Tennessee inheritance tax statute. The court went on to say that the retention of possession by the decedent, until her death, conclusively established it to have been her intention that the beneficiary's ownership of these bonds should take effect in possession or enjoyment on her death.

\textsuperscript{16} Waltenberger v. Pearson, 81 Ohio App. 51, 77 N.E.2d 491 (1946). In this case the court found that the "A and B" form of registration was unauthorized. It should be noted that under present regulations such registration is authorized in Series E bonds. \textit{Supra} note 1.

\textsuperscript{17} 73 N.W.2d 123 (S.D. 1955).

\textsuperscript{18} 90 N.E.2d 440 (Ohio Ct. App. 1949).

\textsuperscript{19} \textit{Supra} note 8.

\textsuperscript{20} Conrad v. Conrad, 66 Cal. App. 2d 280, 152 P.2d 221 (1944). This proposition also applies to other authorized forms of registration.

\textsuperscript{21} Ervin v. Conn, 225 N.C. 267, 44 S.E.2d 402 (1945).

\textsuperscript{22} Mitchell v. Carson, 156 Tenn. 228, 209 S.W.2d 20 (1948); accord, \textit{In re Rummel's Estate}, 74 S.D. 131, 49 N.W.2d 380 (1951); State Board v. Cole, 122 Mont. 9, 185 P.2d 989 (1948).
It has been said that the test is whether or not the decedent "has irrevocably parted with all his interest, title, possession and enjoyment in his lifetime." If he has not then a taxable transfer occurs at death.\textsuperscript{23}

Although a recent opinion of the Attorney General of West Virginia\textsuperscript{24} expresses a contrary view, it is believed that the West Virginia court would have little difficulty in imposing a tax in this situation. This is due to section (c) \textsuperscript{25} of the West Virginia statute to the effect that a tax is to be imposed if a transfer is "intended to take effect in possession or enjoyment at or after such death."

A different situation arises when the beneficiary is in possession at the time of the donor's death. A North Dakota court found here that a completed inter vivos gift took place by the voluntary delivery prior to death. Therefore, from the time of delivery, the decedent had no interest in the bonds which he might legally enforce. As a result no interest passed on his death, so that the inheritance tax statute was inapplicable.\textsuperscript{26}

However, in \textit{Weeks v. Johnson}\textsuperscript{27} the court held that such an inter vivos transfer was ineffectual because there was no compliance with the pertinent federal regulations\textsuperscript{28} concerning reissue. Therefore the status of the bonds was just the same as if no transfer was attempted and they were subject to a tax.

Another situation arises when both the donor and the beneficiary have possession. Where the donor died first a North Carolina court in \textit{Watkins v. Shaw},\textsuperscript{29} found that such joint possession alone did not establish an inter vivos gift; but that the gift was "intended to take effect in possession or enjoyment at or after his death. . . ." Therefore the entire amount of the bonds was subject to the inheritance tax statute by implication. However, when the beneficiary died first a Pennsylvania court held that the inheritance tax applied, but assessed it on only one-half of the value of the bonds.\textsuperscript{30}

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\textsuperscript{23} \textit{In re Myer's Estate}, 359 Pa. 577, 60 A.2d 50 (1948).
\textsuperscript{25} \textit{Supra} note 8.
\textsuperscript{26} \textit{Littlejohn v. County Judge}, 79 N.D. 550, 58 N.W.2d 278 (1958).
\textsuperscript{27} 146 Me. 371, 88 A.2d 416 (1951).
\textsuperscript{28} 31 C.F.R. §§ 315.45, 315.46 (Supp. 1956).
\textsuperscript{29} 234 N.C. 96, 65 S.E.2d 881 (1951).
\textsuperscript{30} \textit{In re Graham's Estate}, 358 Pa. 388, 57 A.2d 853 (1948).
\end{flushright}
STUDENT NOTES

Section (c) of the West Virginia inheritance tax statute\textsuperscript{31} is very similar to this North Carolina statute and there should be no question as to the taxability of the bonds under these circumstances. However, the question as to the amount of the bonds that is to be taxed will still remain.

Where the donor retains sole possession and the beneficiary dies first, one-half of the value of the bonds are subject to the Connecticut inheritance tax statute which imposes a tax on the right of survivor to property in joint names of decedent and survivor.\textsuperscript{32} Section (d) of the West Virginia inheritance tax statute\textsuperscript{33} could be applied to this situation although the court may have difficulty in doing so.

Conclusion

The general rule is that inheritance tax statutes are to be construed in favor of the taxpayer, and most strongly against the government.\textsuperscript{34} However, as was stated in a Tennessee case\textsuperscript{35} the courts must still be careful to “give full scope to the legislative intent and apply a rule of construction that will not defeat the plain purposes of the act.”

The mere fact that John Doe adds such words as “or Jane Doe” after his name in the registering of a bond should not have the effect of avoiding an inheritance tax on his death. By keeping possession of the bond he has absolute control as a practical matter, the same as if the bond were registered in his sole name, for under the federal regulations he can cash the bond without the signature of Jane Doe.\textsuperscript{36} Therefore, it is submitted that courts should be primarily engaged with the legislative intent concerning the policy behind the statute, rather than with the encouraging of persons to avoid tax statutes by the use of mere technicalities.

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\textsuperscript{31} Supra note 8.
\textsuperscript{32} Connelly v. Kellogg, 136 Conn. 83, 68 A.2d 170 (1949).
\textsuperscript{33} Supra note 8.
\textsuperscript{34} Central Trust Co. v. Tax Comm’r, 116 W. Va. 37, 178 S.E. 520 (1935).
\textsuperscript{35} Bergeda v. State, 179 Tenn. 460, 167 S.W.2d 338 (1943).
\textsuperscript{36} Supra note 3.