9 T.C. 782 (1947)

For federal estate tax purposes, a 99-year leasehold interest (exchangeable for a 999-year lease) in foreign land constitutes “real property situated outside of the United States” and is thus excluded from the gross estate.

Summary

The Estate of de Perigny sought a determination from the Tax Court regarding the excludability of leasehold interests in Kenyan land from the decedent’s gross estate. The leases were for 99 years, with an option to convert to 999-year leases. The court addressed whether these interests qualified as “real property situated outside of the United States” under Internal Revenue Code Section 811, thus being exempt from federal estate tax. The Tax Court held that the long-term leases, essentially conveying a fee simple interest, constituted real property and were excludable from the gross estate.

Facts

Margaret Thaw Carnegie de Perigny, a U.S. citizen residing in Pittsburgh, PA, died on January 9, 1942. At the time of her death, she held lessee interests in four leases covering approximately 14,691.7 acres of land with improvements in Kenya Colony, British East Africa. The leases were for 99 years, exchangeable for 999-year leases at the lessee’s option. The agreed value of these leasehold interests was $103,374.68 as of the optional valuation date for estate tax purposes.

Procedural History

The Fidelity Trust Company, as executor, filed the estate tax return, electing the optional valuation method. The Commissioner of Internal Revenue determined a deficiency, arguing the Kenyan leasehold interests should be included in the gross estate. The Tax Court was petitioned to resolve this issue.

Issue(s)

Whether 99-year leasehold interests (exchangeable for 999-year leases) in land located in Kenya Colony, British East Africa, constitute “real property situated outside of the United States” within the meaning of Internal Revenue Code Section 811, and thus are excludable from the decedent’s gross estate for federal estate tax purposes.

Holding

Yes, because long-term leases, especially those with terms effectively equivalent to a fee simple interest, are considered “real property” for the purpose of the estate tax exclusion, reflecting Congressional intent to exempt foreign real estate from U.S. estate tax.

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Court’s Reasoning

The court acknowledged the traditional common law distinction between real property and leasehold interests (chattels real). However, it emphasized that a long-term lease, particularly one for 999 years, is often treated as real property in various contexts. The court reasoned that Congress, when using the term “real property” in the estate tax exclusion, likely intended to encompass such long-term interests. The court cited the legislative history of the exclusion, noting Congress’s intent to align with the principle that real estate should be subject to death duties only in the country where it is situated. The court stated, “It is ‘not probable that Congress intended in this modern taxing act to use the phrase * * * in the technical nicety of the common law with respect to interests in lands flowing from a system of feudal tenure which did not exist in this country after the American Revolution.'” Given the substantial control and enjoyment afforded by a 999-year lease, the court concluded it was more realistic to treat it as the transfer of the real estate itself, consistent with the purpose of the exclusion.

Practical Implications

This case clarifies the scope of the “real property situated outside of the United States” exclusion from the federal gross estate. It suggests that the term “real property” should be interpreted broadly, considering the economic substance and practical control conveyed by the property interest, rather than adhering to strict common law definitions. Legal practitioners should consider the length of the lease term, the rights conveyed to the lessee, and the location of the property when determining whether a foreign leasehold interest qualifies for the estate tax exclusion. This ruling has implications for estate planning for individuals with significant property holdings abroad, emphasizing the importance of analyzing the nature of the property interest under both local and U.S. tax law. Later cases may distinguish de Perigny based on shorter lease terms or specific provisions that significantly limit the lessee’s control.

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