Estate of Ella J. Davis, Deceased, Miles S. Davis, As Sole Devisee and Legatee, Petitioner v. Commissioner of Internal Revenue, Respondent, 57 T. C. 833 (1972)

A sealed note and mortgage, even if enforceable under state law, do not establish adequate and full consideration in money or money's worth for the purpose of an estate tax deduction under section 2053 of the Internal Revenue Code.

Summary

Ella J. Davis executed a sealed promissory note and mortgage for $30,000 to her son, Miles S. Davis, without receiving any payment. After her death, Miles, as executor, sought an estate tax deduction for the claim against the estate represented by the note and mortgage. The Tax Court held that the execution of a sealed note and mortgage does not automatically constitute adequate and full consideration in money or money's worth under section 2053(c)(1)(A) of the Internal Revenue Code. The court found no evidence of consideration that augmented the decedent's estate or granted her a new right, thus disallowing the deduction and emphasizing that federal tax law governs the consideration requirement, not state law.

Facts

Ella J. Davis, an 82-year-old widow, executed a promissory note and mortgage under seal on December 24, 1962, promising to pay her only son, Miles S. Davis, $30,000 plus interest within ten years. The mortgage was secured against property she owned. Miles received the documents after Christmas and considered them a gift, without paying any money to his mother. Ella claimed a lifetime gift tax exclusion, and Miles filed gift tax returns. No payments were made on the note or mortgage by the time of Ella's death in 1967. Miles, as executor and sole beneficiary of the estate, sought an estate tax deduction for the $30,000 claim represented by the note and mortgage.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in the estate's tax return, disallowing the deduction for the note and mortgage on the grounds that they were not supported by adequate and full consideration in money or money's worth. Miles S. Davis, as petitioner, appealed to the United States Tax Court.

Issue(s)

1. Whether the execution of a note and mortgage under seal establishes that adequate and full consideration in money or money's worth was given for them, as required by section 2053(c)(1)(A) of the Internal Revenue Code?

Holding

1. No, because the execution of a note and mortgage under seal does not automatically establish adequate and full consideration in money or money's worth under federal tax law. The court found no evidence that any consideration passed to the decedent that augmented her estate or granted her a new right or privilege.

Court's Reasoning

The Tax Court applied the rule that for a claim to be deductible under section 2053 of the Internal Revenue Code, it must be supported by "adequate and full consideration in money or money's worth. " This standard is a statutory concept and is not determined by state law, even if the note and mortgage are enforceable under state law. The court cited cases such as *Taft v. Commissioner* and *Estate of Herbert C. Tiffany* to establish that "consideration" in this context means "equivalent money value. " The court noted that Ella Davis received no money or equivalent value from her son for the note and mortgage, which were considered a gift. The court rejected the argument that the seal on the documents conclusively established consideration under Wisconsin law, stating that federal tax law governs the interpretation of section 2053. The court concluded that the petitioner failed to prove that the note and mortgage were contracted bona fide and for full and adequate consideration in money or money's worth.

Practical Implications

This decision clarifies that the enforceability of a claim under state law does not automatically qualify it for an estate tax deduction under federal tax law. Practitioners must ensure that any claim against an estate is supported by adequate and full consideration in money or money's worth as defined by federal tax statutes. The case has implications for estate planning, especially when using notes and mortgages as estate planning tools. It highlights the need to carefully document any consideration given in such transactions to withstand IRS scrutiny. Later cases, such as *Estate of Maxwell v. Commissioner*, have cited *Estate of Davis* to support the principle that federal tax law's definition of consideration prevails over state law interpretations.

