Estate of Grace E. Lang, Deceased; Richard E. Lang, Executor, Petitioner v. Commissioner of Internal Revenue, Respondent, 64 T. C. 404 (1975)

State gift taxes paid after a decedent's death are deductible from the Federal gross estate as claims against the estate under Section 2053, even if used as a credit against state inheritance taxes.

Summary

Grace E. Lang made a gift before her death, incurring Washington state gift taxes which were paid posthumously. The gift was included in her estate as a transfer in contemplation of death, and the state gift taxes were credited against the state inheritance tax. The court held that these state gift taxes were deductible from the Federal gross estate as claims against the estate under Section 2053. Additionally, the court found that the decedent's failure to collect loans from her son constituted taxable gifts, and upheld penalties for failing to file gift tax returns on those gifts. This decision clarifies the treatment of state gift taxes and the tax implications of uncollected loans within families.

Facts

Grace E. Lang transferred stocks and bonds valued at $2,427,523. 49 to an irrevocable trust for her children on May 28, 1968. She died on June 10, 1968. Her estate paid Washington state gift taxes of $218,031. 96 after her death. The gift was included in her gross estate as a transfer in contemplation of death, and the state gift tax was credited against the state inheritance tax of $671,237. 09. Lang had also made several loans to her son Howard, which became uncollectible due to the statute of limitations. She did not file gift tax returns for these loans, leading to penalties.

Procedural History

The executor of Lang's estate filed a Federal estate tax return claiming a deduction for the state gift taxes. The Commissioner disallowed this deduction, leading to a deficiency determination. The case was brought before the United States Tax Court, which ruled in favor of the estate on the issue of the state gift tax deduction but upheld the Commissioner's determination regarding the loans to Howard and the penalties for failing to file gift tax returns.

Issue(s)

1. Whether the estate is entitled to deduct state gift taxes paid after the decedent's death from the Federal gross estate.
2. Whether the decedent made gifts to her son Howard equal to the amount of certain loans when she permitted the statute of limitations on the loans to expire.
3. Whether the estate is liable for penalties under section 6651(a) for failure to file Federal gift tax returns on the loans to Howard.

Holding

1. Yes, because the state gift taxes were claims against the estate under Section 2053, and not precluded from deduction by Section 2053(c)(1)(B) as they were not transformed into inheritance taxes by being credited against state inheritance taxes.
2. Yes, because the decedent's failure to act on the loans, allowing the statute of limitations to run, constituted taxable gifts to Howard.
3. Yes, because the estate failed to prove that the failure to file gift tax returns was due to reasonable cause.

Court's Reasoning

The court found that the state gift taxes, although credited against state inheritance taxes, remained state gift taxes and were deductible under Section 2053 as claims against the estate. The court rejected the Commissioner's argument that these taxes should be treated as inheritance taxes, disallowing the deduction under Section 2053(c)(1)(B). The court also determined that the decedent's failure to collect loans from Howard, allowing the statute of limitations to run, constituted taxable gifts under the broad definition of a gift in the tax code. The court upheld penalties for failure to file gift tax returns, noting the absence of evidence showing reasonable cause for the non-filing.

Practical Implications

This decision allows estates to deduct state gift taxes paid posthumously from the Federal gross estate, even when those taxes are credited against state inheritance taxes. Practitioners should ensure such taxes are claimed as deductions on Federal estate tax returns. The ruling also highlights the tax implications of allowing the statute of limitations to run on family loans, treating such inaction as taxable gifts. Attorneys should advise clients to file gift tax returns on such loans to avoid penalties. This case has been cited in subsequent rulings to support the deductibility of state gift taxes and the treatment of uncollected loans as gifts.