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Federal Estate Taxation: Recent Developments in the Deductibility of Claims against the Decedent's Estate and Their Effect in Illinois

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FEDERAL ESTATE TAXATION: RECENT DEVELOPMENTS IN THE DEDUCTIBILITY OF CLAIMS AGAINST THE DECEDENT'S ESTATE AND THEIR EFFECT IN ILLINOIS*

Since the federal estate tax is a tax imposed upon the right to pass property at death,1 the Internal Revenue Code2 provides that certain items are deductible from the decedent's gross estate to assure that the tax is imposed upon only the property which is actually transferred at death.3 One of these deductions allowed under the Code, the deduction for claims against the estate,4 has aroused considerable controversy because neither the Code nor the Treasury Regulations specify what effect events subsequent to the decedent's death should have on the valuation of claims against the decedent's estate.5

Section 2053(a) of the Code merely requires that the value of the taxable estate be determined by deducting from the value of the gross estate such amounts for claims against the estate as are allowable under the laws of the jurisdiction in which the estate is being administered.6 Section 20.2053-4

* The assistance provided by Ruth Goldman of the law firm of Devoe, Shadur & Krupp of Chicago, Illinois in the development of this article is acknowledged with gratitude.


2. INT. REV. CODE OF 1954 [hereinafter referred to in the text as the Code].

Under section 2053 of the Code, funeral expenses, administrative expenses, claims against the estate, unpaid mortgages on property includable in the gross estate, and certain state and foreign death taxes are deductible. Casualty losses incurred during the settlement of the estate, charitable contributions, and bequests to the surviving spouse are also deductible under sections 2054, 2055 and 2056 of the Code respectively.


5. Since section 20.2053-1(b)(3) of the Treasury Regulations provides that "[n]o deduction may be taken upon the basis of a vague or uncertain estimate," events subsequent to the decedent's death must be considered when valuing disputed or contingent claims. It is only when claims against the estate are certain in amount and enforceable at the decedent's death, that it is unclear whether later events, which alter the amount necessary to discharge the claim, should be considered in valuing the claim.

6. INT. REV. CODE OF 1954, § 2053(a), in pertinent part, reads as follows:

General Rule. For purposes of the tax imposed by section 2001, the
of the Treasury Regulations simply limits the deduction for claims against a
decedent's estate to those claims which are enforceable under the laws of the
jurisdiction where the estate is being administered.7 As a result, neither the
Code nor the Treasury Regulations state when claims against the estate
should be valued and two theories have developed to fill this void:8 (1)
value of the claims should be determined as of the date of death and
subsequent events are irrelevant, and (2) only claims actually paid or to be
paid should be allowed and subsequent events which change the amount or
nature of a claim existing at death should control.9 The Commissioner's

value of the taxable estate shall be determined by deducting from the value of
the gross estate such amounts—

(3) for claims against the estate . . .

as are allowable by the laws of the jurisdiction, whether within or without the
United States, under which the estate is being administered.

Since estates which are subject to the federal estate tax may come into existence
in any one of the fifty states and are governed by the intestate or testate laws of such
states, it is a basic principle of federal estate taxation that the extent of a decedent's
interest in property at the time of his death is generally determined by state law even
though the question of what is subject to the federal tax is determined by the federal
law. That is, the general laws of each state concerning estate administration and credi-
tor's rights with respect to decedent's estates control. 1 HARRIS, supra note 1, § 7; 34

For a more detailed discussion of this provision, see LOWNDES, supra note 1, § 15.5;
4 J. MERTENS, THE LAW OF FEDERAL GIFT AND ESTATE TAXATION § 26.16 (1959)
[hereinafter cited as MERTENS].

7. Treas. Reg. § 20.2053-4 (1958), in pertinent part, reads as follows:

Deduction for claims against the estate; in general.

. . . Only claims enforceable against the decedent's estate may be de-
ducted. . . .

Three additional limitations on the deductibility of claims against the estate have
been imposed under the Code and the Treasury Regulations:

(1) In order for the items enumerated in section 2053(a) of the Code to be de-
ductible, they may not exceed the value of the property included in the gross estate
which is subject to claims. INT. REV. CODE OF 1954, § 2053(c)(2). Under the Treas-
ury Regulations, the total allowable amount of deductions is expanded to include amounts paid out of property not subject to claims against the decedent's estate within
nine months after the decedent's death (the period within which the federal estate tax
return must be filed under section 6075 of the Code) or within any extension of time
for filing the return granted under section 6081 of the Code. Treas. Reg. § 20.2053-
1(c) (1958).

(2) A claim founded on a promise or agreement is deductible only to the extent
that it is contracted bona fide and for an adequate and full consideration in money or
money's worth. INT. REV. CODE OF 1954, § 2053(c)(1)(A). For more detailed discus-
sion of this provision, see LOWNDES, supra note 1, § 15.14; 4 MERTENS, supra note 6,
§§ 26.21-26.23.

(3) A claim must represent a personal obligation of the decedent existing at his
discussion of this provision, see 4 MERTENS, supra note 6, § 26.40.

8. Comment, Effect of Events Subsequent to the Decedent's Death on the Valua-
tion of Claims Against His Estate Under Section 2053 of the Federal Estate Tax, 1972
U. ILL. L.F. 770, 776; Comment, Estate and Income Tax: Claims Against the Estate
and Events Subsequent to Date of Death, 22 U.C.L.A. L. REV. 654, 672 (1975).

9. Examples of subsequent events which might change the amount or nature of
position in a recent Tax Court decision, Estate of Frank G. Hagmann, and two recent Revenue Rulings indicate that the Internal Revenue Service has adopted the latter theory.

Acceptance by the IRS of the position that events subsequent to the decedent’s death should be considered in determining the value of claims against the decedent’s estate has widespread ramifications in Illinois because Illinois precedent is contrary to the IRS position on this issue. At the present time, the determining factor in Illinois is that the claim is enforceable on the date of death and the fact that the nature or amount of the claim is changed by events subsequent to the decedent’s death is immaterial. Because of this conflict between Illinois precedent and the IRS position, it is unclear at this moment whether claims which are enforceable at the decedent's death, but which under Illinois law become unenforceable due to events subsequent to the decedent’s death, are deductible under section 2053 of the Code and section 20.2053 of the Treasury Regulations.

Most of the writers who have examined the effect of events subsequent to the decedent’s death on the valuation of claims against the estate have only suggested answers to the question of whether events subsequent to the decedent’s death should be considered when valuing claims against the decedent’s estate and have not discussed the effect of the IRS position on the deductibility of such claims in light of a particular state’s pertinent statutes.

a claim existing at the date of death are: compromising the claim for a lesser amount (Commissioner v. State Street Trust Co., 128 F.2d 618 (1st Cir. 1942); Estate of Isaac W. Baldwin, 18 CCH Tax Ct. Mem. 902 (1959), reopened on other grounds, 20 CCH Tax Ct. Mem. 339 (1961), appeal dismissed, (3d Cir., June 24, 1963) (unpublished opinion); abandonment by the creditor (Jacobs v. Commissioner, 34 F.2d 233 (8th Cir. 1929), cert. denied, 280 U.S. 603 (1929)); extinguishment by legislative act (John Jacobs, 34 B.T.A. 594 (1936), remanded on stipulation, 95 F.2d 1006 (6th Cir. 1938)); payment of the debt by someone other than the estate (Buck v. Helvering, 73 F.2d 760 (9th Cir. 1934)); occurrence of a condition subsequent (Commissioner v. Shively's Estate, 276 F.2d 372 (2d Cir. 1960), rev'g 17 CCH Tax Ct. Mem. 965 (1958)); creditor's failure to file a claim against the decedent's estate within the statutory claim period (Russell v. United States, 260 F. Supp. 493 (N.D. Ill. 1966); Winer v. United States, 153 F. Supp. 941 (S.D.N.Y. 1957)).

10. 60 T.C. 465 (1973), aff'd per curiam, 492 F.2d 796 (5th Cir. 1974).
12. Hereinafter referred to in the text as the IRS.
13. Russell v. United States, 260 F. Supp. 493 (N.D. Ill. 1966), stands for the proposition that subsequent events are not to be considered when valuing claims against the estate. See notes 36-44, 77-79 infra and accompanying text.
14. This writer has been advised that the Chicago Bar Association Committee on Probate Practice has established a special subcommittee to consider this issue.
15. See periodicals cited note 8 supra.
16. The only article which has discussed this issue, Note, Taxation-Income and Estate Taxes-Claims Against the Decedent's Estate, 10 WAKE FOR. L. REV. 328 (1974), did not discuss in detail the provisions under section 2053 of the Code and section 20.2053 of the Treasury Regulations regarding claims against the estate and the cases which consider when claims against the estate should be valued.
By way of contrast, this note will not consider how that question should finally be resolved but will analyze instead the possible far-reaching consequences of the IRS position in Illinois under the applicable Illinois statute.

The first section of this note will examine the major cases which discuss when claims against the estate should be valued. The second section will review the Revenue Rulings which delineate the IRS position on this problem. Finally, the third section will analyze the effect the IRS position will have in Illinois in light of the applicable Illinois statute and will consider approaches which might be taken to avoid having claims against the decedent’s estate disallowed because of events subsequent to the decedent’s death.

**The Case Law**

*Ithaca Trust Co. v. United States*\(^17\) is the only United States Supreme Court decision to consider whether the value of a deduction should be determined by facts known at the decedent’s death or in light of events happening after the decedent’s death but before the calculation of the federal estate tax. In *Ithaca Trust* the decedent left his estate in trust and gave his wife a life estate in the corpus of the trust and power to withdraw as much of the principal as might be necessary to continue the standard of living she then enjoyed. At her death the remainder was bequeathed to charity. Under section 403(a)(3) of the Revenue Act of 1918,\(^18\) the estate was allowed to deduct gifts to charity to arrive at the value of the net estate and the tax payable thereon. When the decedent’s wife died before the federal estate tax return was filed, it was unclear whether the value of the charitable deduction should be the value of the residuary estate at the decedent’s death less the value of the wife’s interest for her actual life or less the value of the wife’s interest estimated by mortality tables. The Court reasoned that the word “value” depended on certain predictions of the future and, since value was no less real if the prediction turned out to be false, held that “[t]he estate so far as may be is settled as of the date of the testator’s death.”\(^19\) Thus, according to *Ithaca Trust*, subsequent events should not be considered when determining the value of the deductions allowed under the Code.

Even though *Ithaca Trust* is a United States Supreme Court decision concerned with the valuation of deductions from the decedent’s gross estate, it is not controlling authority on valuation of the deduction for claims against

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17. 279 U.S. 151 (1929).
the estate because it deals with a different deduction, the one for charitable contributions.\(^{20}\) For this reason, \textit{Ithaca Trust} was distinguished on its facts in \textit{Jacobs v. Commissioner}.\(^{21}\) In \textit{Jacobs} the decedent prior to death entered into an antenuptial contract with his widow in which it was agreed that she would be paid $75,000 out of his estate upon his death in lieu of her dower and marital rights. In addition, the decedent's will provided that his widow could choose to be paid during her lifetime the net income from $250,000 of his estate instead of the $75,000 under the terms of the antenuptial contract. Before the federal estate tax return was filed, the widow notified the executors of her husband's estate that she had decided to take the life estate under the will rather than the lump sum under the antenuptial contract. Despite the fact that the $75,000 contractual obligation was never going to be paid, the executors deducted it on the federal estate tax return because the widow's claim under the antenuptial contract was an existing and enforceable claim against the estate at the time of her husband's death. The court rejected this argument and held that the $75,000 was not deductible because it concluded that Congress had only intended claims which were actually paid or were going to be paid to be deductible.\(^{22}\)

In reaching this conclusion, the court acknowledged that under \textit{Ithaca Trust} there were deductions which could only be determined by facts and conditions existing at the date of death. The court distinguished \textit{Ithaca Trust}, however, on the grounds that it was concerned with the value of a charitable deduction under section 403(a)(3)\(^{23}\) while \textit{Jacobs} was concerned with the value of a deduction for claims against the estate under section 403(a)(1).\(^{24}\) Since section 403(a)(1) also allowed funeral and administrative expenses as deductions and since these expenses must be ascertained by facts and circumstances which arise after death, the court held that \textit{Ithaca Trust} was not controlling and that subsequent events must be considered when valuing claims against the estate.\(^{25}\) In support of its decision, the

\(^{20}\) See notes 23 and 24 \textit{infra} and accompanying text.
\(^{21}\) 34 F.2d 233 (8th Cir. 1929), \textit{cert. denied}, 280 U.S. 603 (1929).
\(^{22}\) 34 F.2d at 235.
\(^{25}\) 34 F.2d at 236. \textit{But see} Estate of Carlton A. Shively, 17 CCH Tax Ct. Mem. 965, 967-968 (1958), which rejected the \textit{Jacobs} rationale because that case and the cases which had adopted it (Estate of William P. Metcalf, 7 T.C. 153 (1946), \textit{aff'd}, 47-2 U.S. Tax Cas. 12,992 (6th Cir. 1947) and Estate of Ethel M. DuVal, 4 T.C. 722 (1945), \textit{aff'd}, 152 F.2d 103 (1945), \textit{cert. denied}, 328 U.S. 838 (1946)) involved situations where the estate was disputing its liability for a claim, where the claim was compromised or relinquished, or where the event considered was not subject to a probable estimate at the time of decedent's death. The court held that \textit{Jacobs} and the decisions which had followed it did not stand "for the proposition that actual events occurring after the decedent's death may be substituted for the estimate of probable events made as of the time of the decedent's death and based upon circumstances as they existed at that time."
court also emphasized the fact that this conclusion was in harmony with the regulations of the Treasury Department. Since the United States Supreme Court has not considered when the deduction for claims against the estate should be valued, the Jacobs rationale that subsequent events must be considered when determining the value of claims against the estate has been interpreted by some courts as being more persuasive than Ithaca Trust.

Although all of the cases involving claims against the estate since 1929 followed Jacobs, in 1957 the courts began to adhere to the Jacobs rationale with less consistency. The first departure, Winer v. United States, is especially noteworthy because it is the first case to cite Ithaca Trust and apply its rationale in determining whether subsequent events should be considered when valuing claims against the estate. In Winer the decedent’s daughter had a valid and enforceable claim against her mother’s estate but through inadvertence failed to file her claim with the probate court in accordance with the Florida statute which stated that claims not so filed were void. The court interpreted the term “allowed” in section 2053(a) of the Code to mean that a claim against the estate does not have to be

17 CCH Tax Ct. Mem. at 967-968. This case, however, was reversed in Commissioner v. Shively’s Estate, 276 F.2d 372 (2d Cir. 1960). Article 32 of Regulation 63, 1922 Edition, provides:

An item may be entered on the return for deduction though the exact amount thereof is not then known, provided it is ascertainable with reasonable certainty, and will be paid. No deduction may be taken upon the basis of a vague or uncertain estimate.

34 F.2d at 236.

27. Estate of Frank G. Hagmann, 60 T.C. 465 (1973), aff’d per curiam, 492 F.2d 796 (5th Cir. 1974); Gowetz v. Commissioner, 320 F.2d 874 (1st Cir. 1963); Commissioner v. Shively’s Estate, 276 F.2d 372 (2d Cir. 1960), rev’g 17 CCH Tax Ct. Mem. 965 (1958); Commissioner v. State Street Trust Co., 128 F.2d 618 (1st Cir. 1942); Estate of William P. Metcalf, 7 T.C. 153 (1946), aff’d, 47-2 U.S. Tax Cas. 12,992 (6th Cir. 1947); John Jacobs, 34 B.T.A. 594 (1936), remanded on stipulation, 95 F.2d 1006 (6th Cir. 1938).

28. Commissioner v. State Street Trust Co., 128 F.2d 618 (1st Cir. 1942); Buck v. Helvering, 73 F.2d 760 (9th Cir. 1934); Estate of William P. Metcalf, 7 T.C. 153 (1946), aff’d, 47-2 U.S. Tax Cas. 12,992 (6th Cir. 1947); John Jacobs, 34 B.T.A. 594 (1936), remanded on stipulation, 95 F.2d 1006 (6th Cir. 1938).

29. “Although Smyth v. Erickson, 221 F.2d 1 (9th Cir. 1955), and Commissioner v. Strauss, 77 F.2d 401 (7th Cir. 1935), have been cited for the proposition that subsequent events are irrelevant in valuing claims against the estate, these cases did not squarely decide the issue.” Comment, Effect of Events Subsequent to the Decedent’s Death on the Valuation of Claims Against His Estate Under Section 2053 of the Federal Estate Tax, 1972 U. Ill. L.F. 770, 779 n.72.


31. The court in Winer stated that only Florida had such a nonclaim statute. 153 F. Supp. at 943. While this may have been true when Winer was decided in 1957, this is not true today. Creditors must file valid claims with the probate court within a specified period after death in states such as Alabama, Florida, Idaho, Illinois, Iowa, Minnesota, Montana, New Mexico and Utah. Note, Taxation-Income and Estate Taxes—Claims Against the Decedent’s Estate, 10 Wake For. L. Rev. 328, 329 n.5 (1974).

32. The fact that the word “allowable” has been substituted for “allowed” in the
allowed by the state court in order to be deductible\textsuperscript{33} and applied the \textit{Ithaca Trust} rationale without citing or distinguishing any of the previous decisions to the contrary. Since the federal estate tax payable must be determined as of the date of death, the court held that the daughter's claim, which was enforceable at the time of the decedent's death, was deductible and adopted the theory that subsequent events should not be considered in determining the value of claims against the estate.\textsuperscript{34} It was in response to \textit{Winer} that the first Revenue Ruling expressing the IRS position, Revenue Ruling 60-247,\textsuperscript{35} was issued.

Another case which departed from the \textit{Jacobs} rationale was \textit{Russell v. United States}.\textsuperscript{36} Although it followed the majority of decisions since 1957 by adopting \textit{Ithaca Trust} and rejecting \textit{Jacobs}\textsuperscript{37} without adding anything to the development of the case law in this area, it is particularly significant because it is the only case which applies to Illinois law in determining whether subsequent events should be considered when valuing claims against the decedent's estate.\textsuperscript{38} In \textit{Russell} the court was faced with a factual situation identical to \textit{Winer}. The decedent's husband had left each of their two children several thousand shares of stock in a trust to be administered by their mother. The decedent subsequently sold the stock and comingled the proceeds with her own funds. After her death, the two children learned of the existence of these trust funds and filed claims against her estate with the probate court after the period for filing claims under the Illinois statute had run.\textsuperscript{39} At this time section 204 of the Illinois Probate Act\textsuperscript{40} created a nine month period of limitation on claims against an estate which may be paid from estate assets inventoried within that period.\textsuperscript{41} The probate court allowed the claims even though they were filed after the period of limitation on claims had run and they were taken as deductions on the federal estate tax return. The government contended, however, that since the children's claims were unenforceable under state law at the time they were filed with the probate court, they were not deductible.

current Code has no effect on the applicability of this decision. 4 MERTENS, \textit{supra} note 6, § 26.16.

33. \textit{Accord}, Smyth v. Erickson, 221 F.2d 1 (9th Cir. 1955); Commissioner v. Strauss, 77 F.2d 401 (7th Cir. 1935); Buck v. Helvering, 73 F.2d 760 (9th Cir. 1934).

34. 153 F. Supp. at 943-44.


38. See notes 77-79 \textit{infra} and accompanying text.

39. ILL. REV. STAT. ch. 3, § 204 (1939).

40. ILL. REV. STAT. ch. 3, § 1 et seq. (1939).

41. Section 204 of the Illinois Probate Act has been amended and now allows a six month claim period. ILL. REV. STAT. ch. 3, § 204 (1939), \textit{as amended}, ILL. REV. STAT. ch. 3, § 204 (1973).
In order to determine whether these claims against the estate were deductible under section 2053 of the Code, the court had to refer to the applicable Illinois statute and to the cases which had construed section 204 of the Illinois Probate Act. In so doing, the court noted that section 204 was not an ordinary statute of limitations which created a defense to be raised or lost by the party in whose favor the statute operated. Instead, this section created a nonclaim statute which operated as a limitation upon the jurisdiction of the probate court. Since the children's claims were filed after the nine month period of limitations and there were no after-inventoried assets from which their claims could be satisfied, the court found that the probate court was without jurisdiction and that the order allowing the claims was void.

Because the children's claims against the estate were unenforceable under Illinois law at the time they were filed with the probate court, it was then necessary for the court to construe the language of section 2053 of the Code. By following what it interpreted the persuasive weight of case law to intend, the court defined the phrase "as are allowable by the laws of the jurisdiction . . . under which the estate is being administered" to mean that claims which are allowable at the time of the decedent's death under the laws of Illinois are deductible. In expressly adopting the *Ithaca Trust* rationale, the court held that the determining factor was that the claims were allowable in Illinois on the date of the decedent's death and the fact that the claims were subsequently lost by lapse of time was found to be irrelevant. Therefore, *Russell* agreed with *Winer* and the tide of cases since 1957 which adopted *Ithaca Trust* but disagreed with the IRS position on this issue.

Two of the most recent cases to consider whether subsequent events should affect the valuation of claims against the estate are *Estate of Donald Albert Lester* and *Estate of Frank G. Hagmann*. Until Hagmann, the most recent cases had rejected *Jacobs* and it could have been assumed that *Ithaca Trust* had become controlling. Therefore, *Lester* and *Hagmann* are noteworthy because they are recent Tax Court cases in which contradictory decisions resulted and because they indicate that the issue of whether events subsequent to the decedent's death should be considered when valuing claims against the decedent's estate still has not been resolved.

In *Lester* the decedent agreed to pay his former wife $1,000 per month as alimony until the sum of $130,000 was paid and this liability was to be binding on his estate. Since the decedent died when only nineteen payments had been made, the estate was obligated to pay the decedent's former wife...

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42. 260 F. Supp. at 498.
43. *Id.* at 499.
44. *Id*.
45. 57 T.C. 503 (1972).
46. 60 T.C. 465 (1973), *aff'd per curiam*, 492 F.2d 796 (5th Cir. 1974).
$111,000 in $1,000 monthly installments. After the estate had paid $24,000, the probate court, in order to facilitate the prompt settlement of the estate, ordered the executor to purchase an annuity which would pay the decedent's former wife $1,000 per month until the remainder of $87,000 was paid. Although the purchase price of this annuity was $78,700, the estate took a deduction on the federal estate tax return for the face amount of the installments outstanding at the date of death. The government contended, however, that the amount of the deduction should be the commuted value of this debt based upon actuarial tables. In following Ithaca Trust, the Tax Court held that there was no need to consider the effect of events subsequent to the decedent's death and that the value of the former wife's claim was to be determined as of the date of his death by the use of actuarial tables.

Nevertheless, the opposite result was reached in Hagmann, a Florida case which is factually similar to both Winer and Russell because all three concern nonclaim statutes. In Hagmann the estate deducted debts which were bona fide obligations at the time of the decedent's death. The applicable Florida statute required that any claim not filed within six months from the first publication of notice to creditors was void even if recognized by the estate's representative. When no claims with respect to such debts were filed against the estate, the claims became unenforceable under Florida law and were not paid by the estate.

The Tax Court rejected the executor's position that Ithaca Trust was controlling, that the debts were deductible because they were bona fide obligations of the decedent at the time of his death and that it was inconsequential that the claims subsequently became unenforceable. Instead the court agreed with Jacobs and held that the debts were void and unenforceable under the Florida statute because events occurring subsequent to the decedent's death must be taken into consideration in determining the deductibility of claims under section 2053(a)(3) of the Code. In so holding, the court also rejected the argument that the courts have only considered events subsequent to death when the claim was contingent because such an argument was based on too narrow a reading of the cases. In reaching this conclusion, the court distinguished Winer and Russell on the

47. 57 T.C. at 507.
49. 60 T.C. at 469. Accord, Estate of Claire M. Conrad, 34 CCH Tax Ct. Mem. 1071 (1975). In Conrad decedent's obligation as a guarantor of loans became unenforceable under Kansas law when the creditor failed to file a claim against the estate within nine months of publication of the first notice to creditors. The Tax Court followed Jacobs and Hagmann and ruled that if an enforceable claim exists at a decedent's death, but subsequent events relieve the estate of liability, the claim is not deductible.
51. 60 T.C. at 469.
grounds that those cases had applied the broad doctrine of *Ithaca Trust* without considering the contrary cases which limited the applicability of that doctrine in the area of claims against the estate. By disagreeing with *Winer* and *Russell*, *Hagmann* also demonstrated that an underlying consideration in determining whether to consider events subsequent to death when valuing claims against the estate may be whether such claims have been or will be paid by the estate. Thus, one of the most recent cases to consider this issue has adopted the *Jacobs* rationale by considering events subsequent to the decedent's death when valuing a claim against the decedent's estate.

In retrospect, it is clear that neither *Ithaca Trust* nor *Jacobs* have become controlling on the question of how events subsequent to the decedent's death should affect the valuation of claims against the estate. Instead, the determination as to whether *Ithaca Trust* or *Jacobs* will prevail depends upon the jurisdiction. Because the ultimate impact of the federal estate tax is a matter for state law determination, except as it has been specifically dealt with in the federal statutes, and because the courts have been unable to resolve whether claims against the estate should be valued at the date of death or at some later time, the Commissioner has issued three Revenue Rulings during the last fifteen years which set forth the IRS position.

**THE REVENUE RULINGS**

Since the extent to which events which occur subsequent to the decedent's death affect the amount of the deduction otherwise permissible has been discussed by the IRS in several Revenue Rulings, there is no doubt as to its position on this issue. The first of these, Revenue Ruling 60-247, was issued as a direct response to and in complete disagreement with the decision reached in *Winer*. After reviewing the reasoning of several of the cases which held that subsequent events are to be considered when determining the value of a deduction for claims against the estate, the IRS decided that a claim against the estate which is enforceable at the time of the decedent's death will not be allowed as a deduction in a case where the

52. *Id.*
53. It is unlikely that the United States Supreme Court will resolve this issue since it has denied certiorari in *Jacobs v. Commissioner*, 34 F.2d 233 (8th Cir. 1929), *cert. denied*, 280 U.S. 603 (1929), and *Estate of Ethel M. DuVal*, 4 T.C. 722 (1945), aff'd, 152 F.2d 103 (1945), *cert. denied*, 328 U.S. 838 (1946).
54. *Riggs v. Del Drago*, 317 U.S. 95 (1942) (final determination of the ultimate burden of the federal estate tax is left to individual states except where Congress has specifically provided to the contrary).
56. See text at notes 30-35 supra. By suggesting that the court in *Winer* determined that no more was needed than enforceability at death to warrant deduction and attached no importance to the fact that the debt could not be collected, it appears that the Revenue Ruling was issued to express IRS disapproval of the decision.
creditor fails to enforce payment.58 As nonexclusive illustrations of what constituted a failure to enforce payment, the Revenue Ruling specifically mentioned waivers of payment and failures to file claims under the conditions and within the time limit prescribed by the applicable state law. The IRS did, however, recognize an exception to this rule when it stated that "... a deduction would be allowed for a claim in favor of the sole beneficiary of an estate, where the claim is not formally presented and not formally paid, but where it is clear, under the facts of the case, that the claim may be deemed to have been paid through the payment of the legacy in an amount at least equal to that of the claim."59 Since the claim in Winer had become void because it was not filed within the statutory period, the IRS impliedly expressed its disagreement with Winer and took the position that subsequent events should be considered when valuing claims against the estate.

Two more recent Revenue Rulings60 indicate that despite the conflict in interpretation in even the most recent cases considered by the courts, the IRS still takes the position that claims which were valid but not filed within the local claim period and which become barred by reason of a nonclaim statute are not deductible for federal estate tax purposes. Therefore, evidence of those events which transpire after the death of a decedent must be considered in valuing claims against the decedent's estate.

In Revenue Ruling 75-24, the IRS was asked to rule on a situation where a claim for an unsecured debt was not filed with the probate court within the Mississippi statutory claim period,61 the claimant informally asserted his claim against the executor and the claim was paid after it was approved by all of the estate's beneficiaries. The debt was subsequently deducted as a claim against the decedent's estate on the federal estate tax return. The Mississippi statute required that all claims against a decedent's estate be registered, probated and allowed in the probate court within six months after publication of notice to creditors. The statute also charged the executor with the duty of promptly paying all claims against the estate and provided that the executor might be surcharged if a claim was paid without complying with the requirements of Mississippi law. This statute had been construed by the local courts to mean that the fiduciary could not be surcharged where payment of a valid but unprobated claim was made within the statutory claim period if the claim had been approved by all of the beneficiaries of the estate within the time in which the claim was enforceable. Since such approval rendered filing of the claim unnecessary to prevent

58. Winer was subsequently followed and Revenue Ruling 60-247 was expressly rejected in Russell.
59. 1960-2 CUM. BULL. at 274.
61. MISS. CODE ANN. § 91-7-151 (1972).
surcharge of the executor, the IRS concluded that the claim was allowable as a deduction under section 2053 of the Code.\textsuperscript{62}

It is important to note that if approval by all of the beneficiaries of the estate would not have prevented the executor from being surcharged under Mississippi law, then the deduction would not have been allowable under section 2053 of the Code.\textsuperscript{63} Since no deduction would have been allowed for the valid but unfiled claim, except for the approval of the beneficiaries, this Revenue Ruling also stands for the proposition that subsequent events must be considered in determining the value of a claim against the decedent's estate.

After the Tax Court's decision in \textit{Hagmann}, the Florida legislature prospectively amended its nonclaim statute\textsuperscript{64} in 1973 by adding that an executor was permitted to pay a claim without the necessity for filing if payment was either approved by the heirs or beneficiaries adversely affected or accounted for in accounts to the court and if payment was made within the claim period.\textsuperscript{65} Even though Revenue Ruling 75-177 was issued in response to a Florida case, it was concerned with a factual situation almost identical to that which Revenue Ruling 75-24 was asked to consider. In this latest Revenue Ruling, the decedent was indebted to an unsecured creditor who had not filed a claim with the probate court. The creditor, however, had informally asserted his claim against the executor and had been paid after the executor obtained the approval of all of the estate's beneficiaries. This claim was then taken as a deduction on the decedent's federal estate tax return. The question arose because the Florida statute prior to the post-\textit{Hagmann} amendment had been construed to mean that the required filing of claims could not be waived.

Since the estate was opened prior to the effective date of the statutory amendment, this claim was not allowable as a deduction under section 2053 of the Code because it was unenforceable under Florida law.\textsuperscript{66} The deduction would have been allowed under Revenue Ruling 75-177, however, if the administration of the decedent's estate had been begun on or after the effective date of the statutory amendment.\textsuperscript{67} Although this Revenue Ruling only impliedly adopted \textit{Jacobs}, it agreed with the previous Revenue Rulings that subsequent events must be considered in valuing claims against the decedent's estate.

Since neither the case law nor the Revenue Rulings are controlling, it is evident that there is no definitive answer to the question on what date claims

\begin{itemize}
  \item \textsuperscript{62} 1975 \textit{Int. Rev. Bull.} No. 3, at 35.
  \item \textsuperscript{63} \textit{Id.}
  \item \textsuperscript{64} \textit{Fla. Ann. Stat.} § 733.16 (1969).
  \item \textsuperscript{66} 1975 \textit{Int. Rev. Bull.} No. 19, at 22.
  \item \textsuperscript{67} \textit{Id.}
\end{itemize}
against the estate should be valued in order to determine whether they are deductible under section 2053 of the Code and section 20.2053 of the Treasury Regulations. Inasmuch as the position taken by the IRS in *Hagmann* and the Revenue Rulings that events subsequent to the date of death are to be considered in valuing claims against the estate is in conflict with the only Illinois case on this issue, *Russell*, the crucial question is whether the IRS position will have any effect in Illinois. The next section of this note will suggest answers to this question and will consider possible approaches that might be taken.

**APPLICATION TO ILLINOIS**

Because section 2053(a) of the Code provides that only claims against the estate which are allowable by the laws of the jurisdiction under which the estate is being administered and section 20.2053-4 of the Treasury Regulations states that only claims enforceable against the decedent's estate may be deducted,\(^6^8\) it is necessary to look at the applicable provisions of the Illinois Probate Act\(^6^9\) to determine whether a claim which is enforceable on the date of death but which changes in either nature or amount due to events subsequent to the decedent’s death is deductible.

Section 204 of the Act\(^7^0\) creates a six month period of limitation on claims against the estate which may be paid from estate assets inventoried within six months from the issuance of letters of office. Section 204 also provides that claims not filed within the six month claim period may be paid from assets discovered after six months from the issuance of letters, if the executor files an inventory listing those assets not previously inventoried and publishes a notice stating that claims may still be filed against the estate for an additional six months. If the claimant does not file his claim with the probate court during this additional claim period, then the claim is absolutely

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68. See notes 6 and 7 *supra*.
69. ILL. REV. STAT. ch. 3, §§ 1 et seq. (1973) [hereinafter referred to in the text as the Act]. As this article went to press, the Probate Act was renumbered in the Probate Act of 1975, ch. 3, §§ 1-1 et seq., [1975] Ill. Laws 404. Hereinafter the new section in the Probate Act of 1975 will be noted in parentheses.
70. ILL. REV. STAT. ch. 3, § 204 (1973) (now § 18-12), in pertinent part, reads as follows:

*Limitations on payment of claims*

(a) All claims against the estate of a decedent, except expenses of administration and surviving spouse's or child's award, not filed within 6 months from the issuance of letters of office are barred as to the estate which has been inventoried within 6 months from the issuance of letters. If after 6 months from the issuance of letters the representative files an inventory listing estate not previously inventoried and thereafter the clerk of the court publishes once each week for 3 successive weeks a notice informing all persons that claims may be filed against the estate on or before a date as designated in the publication . . . , all claims not filed on or before the designated date are barred as to the estate listed in such inventory.

(b) All claims barrable under this Section are, in any event, barred unless letters of office are issued upon the estate of the decedent within 3 years after his death.
barred as to the inventoried estate. This does not mean, however, that claims cannot be paid out of noninventoried assets in the estate.

Section 204 of the Act has been construed by the Illinois Supreme Court to be a specific act adopted for the particular purpose of facilitating the early settlement of estates and, therefore, is not a general statute of limitations which takes away all remedies whether personal or against the property of the decedent. Because section 204 does not operate as an absolute bar to the recovery of a judgment, the failure to file a claim against the estate within the six month statutory claim period does not operate as an absolute bar to the debt. Its only effect is to prevent any participation in the assets of the estate previously inventoried by the executor and the claimant may only have his debt satisfied out of noninventoried or subsequently inventoried property, if any. Since the executor is required to file an inventory of assets discovered any time after the decedent's death, the courts have interpreted the intention of this section to be to allow a debtor who has neglected to present his claim against the estate within the statutory period, to seek satisfaction out of any property belonging to the estate which has not been previously inventoried. In order for a creditor to benefit from any subsequently inventoried assets, however, he still must have his claim filed with and allowed by the probate court.

The question presented in Hagmann and the Revenue Rulings cannot be readily answered when related to the applicable section of the Illinois statute. In those situations, the Florida and Mississippi statutes provided for

71. Waughop v. Bartlett, 165 Ill. 124, 128, 46 N.E. 197, 198 (1897). See Kittredge v. Nicholes, 162 Ill. 410, 44 N.E. 742 (1896) where the debtor, the holder of a note against the decedent secured by a trust deed on real estate, had two remedies for the collection of his debt and could either file a claim against the estate in the probate court based on his note or foreclose the trust deed. The fact that he failed to file his claim in the probate court within the statutory period had no effect on his right to pursue his other remedy.

This interpretation of this section of the Probate Act was adopted by the Supreme Court of the United States in Pufahl v. Estate of Parks, where the Court held that a claim by the receiver of a national bank against a former stockholder was subject to the time limitation provision . . . of the Illinois Probate Act, and since it was not filed within the time prescribed therein, the claim, though not barred, could not be satisfied against inventoried assets, but only against subsequently discovered assets. The court did not regard the provision as a general statute of limitations.

In re Estate of Bird, 410 Ill. 390, 395, 102 N.E.2d 329, 332 (1951) (citation omitted).

72. E.g., Sanders v. Merchants' State Bank, 349 Ill. 547, 566, 182 N.E. 897, 904 (1932); Waughop v. Bartlett, 165 Ill. 124, 128, 46 N.E. 197, 198 (1897); Shepard v. Nat'l Bank, 67 Ill. 292, 294 (1873); Bradford v. Jones, 17 Ill. 93, 94 (1855).


74. E.g., Ryan v. Jones, 15 Ill. 1, 5 (1853); Sloo v. Pool, 15 Ill. 47, 48 (1853).

75. E.g., Bradford v. Jones, 17 Ill. 93, 94 (1855). Although this case was decided under a statute which placed the burden upon the debtor to find any inventoried assets, the intent of both statutes is the same.

76. E.g., Wingate v. Pool, 25 Ill. 118, 122 (1860).
an absolute bar to payment by the executor. In other words, those statutes were general statutes of limitation. Section 204 of the Illinois Act, however, does not provide an absolute bar to payment of claims not filed within the six month statutory claim period. Rather, these claims are only barred as to that part of the estate which has been inventoried. It should be noted, nevertheless, that section 204 does eventually provide for a general statute of limitation by providing that all claims which are barrable under this section are ultimately barred three years after the decedent’s death.

Therefore, if a fact situation similar to the ones considered in Hagmann and the Revenue Rulings were to occur in Illinois, it is uncertain whether the same result would be reached under the applicable section of the Illinois statute. This dilemma can best be analyzed in terms of the following hypothetical example.

A died testate while domiciled in Illinois and the only two items in his gross estate were a bank deposit of $20,000 in his name alone, an inventory asset, and a bank deposit of $150,000 which was payable on his death directly to the decedent’s surviving spouse and thus a noninventory asset. Letters of office were issued in Illinois. At his death A was indebted in the amount of $19,000 to an unsecured creditor, B, who did not file his claim with the probate court within the six month statutory claim period. Less than six months after A’s death, however, B informally asserted his claim against the executor of A’s estate and it was promptly paid out of the property which had been inventoried within six months from the issuance of letters. Since payment of the claim had been approved by the beneficiaries of the estate, the claim was deducted on the federal estate tax return filed on behalf of A’s estate.

According to the position taken by the IRS in Hagmann and the Revenue Rulings, events subsequent to the decedent’s death will be considered and the claim will be barred as to the estate inventoried within six months from the issuance of letters under section 204 of the Act because the creditor had not filed the claim within the six month statutory period. Therefore, in spite of the fact that the debt was a bona fide, personal obligation at the date of the decedent’s death, the debt would not be deductible under either section 2053(a)(3) of the Code, because it is not one considered allowable by the laws of the jurisdiction under which the estate was administered, or section 20.2053-4 of the Treasury Regulations, because it was not a claim enforceable against the decedent’s estate.

Application of the IRS position is not this clear-cut, however, because neither Hagmann nor the Revenue Rulings are controlling in Illinois and because of the contrary decision reached in Russell,77 which is controlling until overruled. Since the claim was allowable under local law at the time of

77. See text at notes 36-44 supra.
the decedent's death, the court in Russell reasoned that a deduction should be allowed even though it had not been timely presented to the probate court. Significantly, the court declined to follow Revenue Ruling 60-247, the first ruling to express IRS agreement with Jacobs that events subsequent to the decedent's death should be considered when valuing claims against the decedent's estate. Therefore, under Russell allowability is to be determined as of the decedent's death and the fact that the claim later becomes unenforceable because of tardiness in filing is immaterial.

Since Russell is the only case construing section 204 of the Act and since it is only a district court decision, it is unclear whether Russell is still good law in light of Hagmann and the Revenue Rulings. If, however, Hagmann, and thus Jacobs, become controlling on the question of how events subsequent to the decedent's death should affect the valuation of claims against the estate, Russell will be overruled upon consideration by the Court of Appeals for the Seventh Circuit. Nevertheless, until overturned, Russell constitutes controlling precedent but the paying of unfiled claims by the executor does run the risk of disallowance by the IRS.

Even though the beneficiaries of the estate in the hypothetical example approved payment of the claim, which had not been filed with the probate court within six months after the issuance of letters, before the statutory claim period had run, according to the IRS position in Hagmann and the Revenue Rulings, it still would not be deductible on the federal estate tax return under either section 2053(a)(3) of the Code or section 20.2053-4 of the Treasury Regulations. This is because section 203 of the Act has been construed by the Illinois Supreme Court to mean that the representative may be personally charged if he pays an unfiled and invalid claim. In addition, the Illinois courts have construed section 204 of the Act to mean that neither the probate court, nor the executor, nor the attorney for the estate, nor the distributees or legatees of the estate can waive filing of a

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78. 260 F. Supp. at 499.
79. See text at notes 55-59 supra.
80. ILL. REV. STAT. ch. 3, § 203 (1973) (now § 18-11), in pertinent part, reads as follows: Payment before Allowance
If a representative pays a claim before it is allowed, the court may require him to establish the validity . . . of the claim before he is credited therewith.
81. E.g., Walker v. Diehl, 79 Ill. 473, 476 (1875); In re Estate of Nonnast, 300 Ill.App. 537, 560, 21 N.E.2d 796, 807 (1939), modified on other grounds, 374 Ill. 248, 29 N.E.2d 251 (1940).
82. E.g., Bosnak v. Murphy, 28 Ill.App.2d 110, 114, 170 N.E.2d 640, 643 (1960); In re Estate of Nonnast, 300 Ill.App. 537, 560, 21 N.E.2d 796, 807 (1939), modified on other grounds, 374 Ill. 248, 29 N.E.2d 251 (1940).
claim within the time fixed by this section. Since no one can waive the filing of a claim, if an executor does pay a claim which has not been filed with the probate court within the statutory claim period, these payments may be surcharged to him and the claim will not be allowed. Because an unfiled creditor's claim paid with the approval of the beneficiaries of the decedent's estate is not allowable under Illinois law, it would not be an enforceable claim against the estate under section 20.2053 of the Treasury Regulations and therefore, would not be allowable as a deduction under section 2053 of the Code.

This does not mean, however, that under Illinois law claims not filed within the six months statutory claim period are never deductible on the decedent's federal estate tax return. If the facts in the hypothetical example were as follows, the results would be different.

B, the claimant who had not filed his claim with the probate court within six months after the issuance of letters, was not paid by the executor out of inventoried property after approval by the beneficiaries of the estate. Instead, the decedent's surviving spouse paid the creditor the $19,000 owed by the decedent out of the bank deposit payable on his death directly to her, before the executor filed the federal estate tax return.

Under these circumstances, the estate could claim a deduction for the claim which had been paid even though it had not been filed with the probate court. Since claims barred under section 204 of the Act are only barred as to inventoried assets and since the determination as to which property is and is not subject to claims is made under the applicable state law, claims otherwise barred under section 204 may be paid out of noninventoried assets and still be deductible. This is because section 2053(c)(2) of the Code and section 20.2053-1(c) of the Treasury Regulations allow the amount paid out of property included in the gross estate but not subject to claims to be deducted if actually paid within the time allowed for the filing of the federal estate tax return under section 6075 of the Code (nine months) or within any extension of time for filing the return granted under section 6081 of the Code. Therefore, the allowable deduction is the amount that is payable out of property subject to claims and is actually paid from any source in the gross estate but cannot exceed the value of the property subject to claims plus the amount actually paid out of property not subject to claims before the return is filed.

Under the last hypothetical example, the fact that section 204 of the Act does not create an absolute bar to payment of claims not filed within the six month statutory claim period is extremely significant. If this section had

86. E.g., In re Estate of Nonnast, 300 Ill.App. 537, 560, 21 N.E.2d 796, 807 (1939), modified on other grounds, 374 Ill. 248, 29 N.E.2d 251 (1940).
87. See note 7 supra.
created a general statute of limitation, as was the case in *Hagmann* and Revenue Rulings 75-24 and 75-177, according to the IRS position claims not filed within the six month statutory claim period would have been void and, therefore, could not have been paid out of noninventoried assets and could not have been deductible. The distinction that under section 204 unfiled claims may not be paid out of inventoried assets is only important, however, if the gross estate consists of both inventoried and noninventoried assets.

If the gross estate includes only inventoried assets, then *Hagmann* and the Revenue Rulings are directly on point. Since events subsequent to the decedent’s death are to be considered in valuing claims against the decedent’s estate under the IRS position, claims in Illinois which subsequently become unenforceable because they were not filed with the probate court within the six month statutory claim period are not deductible for federal estate tax purposes. However, under the Revenue Rulings, the opposite result would be reached if section 204 of the Act were amended to allow that the executor might pay from the estate any claim against the decedent’s estate inventoried within six months after the issuance of letters, even though the claim has not been filed with the probate court within six months from the issuance of letters, when the payment has been approved by the heirs or beneficiaries adversely affected or accounted for in accountings to the court and when the payment is made within six months from the issuance of letters.88 If such an amendment were adopted, it would not be necessary to file every claim with the probate court. Thus, if the executor paid an unfiled claim within six months and either received the approval of the beneficiaries of the estate or accounted for it in his First Current Account to the probate court, then under section 20.2053 of the Treasury Regulations, such a claim would be allowable under Illinois law, would be enforceable, and would, therefore, be allowable as a deduction under section 2053 of the Code.

**CONCLUSION**

There is no definitive answer to the question whether the estate is entitled to a deduction under section 2053(a)(3) of the Code for debts which were bona fide obligations at the date of the decedent’s death but which have become unenforceable under state law. If the *Ithaca Trust* rationale has been adopted in the jurisdiction, the fact that the claim has subsequently become unenforceable does not matter and the debt is deductible. If the *Jacobs* rationale has been adopted, however, then such a subsequent event is determinative and the claim will not be deductible. Since the IRS has adopted the *Jacobs* rationale, the effect of decisions which have adopted *Ithaca Trust* is uncertain.

At this moment, if an Illinois executor is administering an estate composed of only inventoried assets, in order to avoid the possibility of having a claim disallowed as a deduction, he should have it filed with the probate court within six months from the issuance of letters. This means that every debt of a decedent, no matter how large or small, would have to be filed with the probate court before payment could be made. If, however, the Illinois legislature amended section 204 of the Act as indicated, then the Illinois executor would have two alternatives: (1) obtaining the approval of all the beneficiaries of the estate before paying the claim within six months from the issuance of letters, or (2) listing the claim as a disbursement in his First Current Account filed with the probate court. In lieu of action by the United States Congress, action by the Illinois legislature is the only way to avoid having the courts flooded with claims because, according to the IRS position, every claim must be filed with the probate court in an estate composed only of inventoried assets in order for it to be deductible on the federal estate tax return.

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89. See text at note 88 supra.