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TAXATION OF POWERS OF APPOINTMENT
UNDER THE ILLINOIS INHERITANCE
TAX LAW

FREDERICK O. DICUS*

A DECISION rendered in 1934 by the Supreme Court of the State of Illinois dealing with the question of the taxation of powers of appointment caused considerable confusion among practitioners and fiduciaries as to the present status of the law.1 The complications created by this decision, in the light of recent statutory amendments, and by the lack of judicial precedents in this state have proved somewhat bewildering to those who by force of circumstances have been confronted with this problem. It is hoped, therefore, that the following discussion will clarify the issues involved and suggest a satisfactory answer to most of the many questions which have arisen.

We are principally concerned with the question whether property passing under a power of appointment should be presently taxed in the estate of the donor, or whether the tax should be postponed and collected in the estate of the donee of the power, and if the former is true, whether the tax should be assessed upon the supposition of exercise or of non-exercise of the power.

We are confronted at the outset with the necessity of reviewing thoroughly the cases and statutes in the state of New York, from which the Illinois Act was adopted in the first instance, and the amendments to it which have been followed in many respects in this state. It is a familiar rule of statutory interpretation that when a statute is adopted from another state, the legislature will be presumed to have adopted it in the light of the judicial construction theretofore placed upon it by the

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1 People v. Linn, 357 Ill. 220, 191 N. E. 450 (1934).
courts of the foreign state.\(^2\) Because of this legal principle and the relationship between the statutes of Illinois and New York on this subject, the decisions of the latter state become singularly important in this discussion.

Obviously it is uncertain, until the exercise or non-exercise of the power, to whom the property will pass. At common law an appointee was deemed to take the property directly from the donor, although until the appointment was made the appointee remained unknown, or at least his interest was contingent.\(^3\) The common law rule, which still exists in several states, has been abrogated in most states by statutory provisions regarding the taxation of contingent interests at the highest rate. The rules developed by the common law were intended to circumvent another ancient rule that the title to property could not be held in abeyance.\(^4\) The donee of the power merely acted for the donor to the extent of the power conferred upon him,\(^5\) and until the interest over was finally disposed of by the exercise of the power, the estates limited upon default of exercise were considered as vested subject to being divested.\(^6\) This brief statement of the common law rules applicable to powers of appointment is made only as a background for the statutory alterations for tax purposes which are about to be discussed.

To deal with the present problem more comprehensively, it is wise to consider fully the changes which have


\(^4\) Sugden on Powers (8th ed.), Ch. 1, sec. 1.

\(^5\) See In re Luques Estate, 114 Me. 235, 95 A. 1021; U. S. v. Field, supra, n. 3; Kidder, State Inheritance Tax and Taxability of Trusts, p. 41.

\(^6\) Sugden on Powers (8th ed.), Ch. 13, p. 622.
been effected in the New York law. The first provision in the New York statute for the taxation of powers of appointment appeared in 1897\(^7\) when section 220 of the Tax Law was amended to provide for a taxable transfer resulting from the exercise or non-exercise of the power in the estate of the donee. This provision, which was identical with that in Illinois prior to the 1933 amendment, provided as follows:

Whenever any person or corporation shall exercise a power of appointment derived from any disposition of property, made either before or after the passage of this chapter, such appointment when made shall be deemed a transfer taxable under the provisions of this chapter in the same manner as though the property to which such appointment relates belonged absolutely to the donee of such power and had been bequeathed or devised by such donee by will, and whenever any person or corporation possessing such a power of appointment so derived shall omit or fail to exercise the same within the time provided therefor, in whole or in part, a transfer taxable under the provisions of this chapter shall be deemed to take place to the extent of such omission or failure, in the same manner as though the persons or corporations thereby becoming entitled to the possession or enjoyment of the property to which such power related had succeeded thereto by a will of the donee of the power failing to exercise the power, taking effect at the time of such omission or failure.

The first portion of the foregoing section changed the common law rule\(^8\) and provided that the exercise of the power should constitute the transfer deemed to be taxable under the Act; that is, that the tax should be levied in the estate of the donee rather than in the estate of the donor of the power. By force of the statute, the appointee is deemed to take the property from the donee and not from the donor for the purposes of taxation, the property passing as part of the donee's estate upon the exercise of the power.\(^9\) This provision has been subjected

\(^7\) Laws of 1897, C. 284, p. 150.
\(^8\) See n. 5, ante.
\(^9\) In re Dimock's Estate, 168 N. Y. S. 584 (1918); In re Turner's Estate, 222 N. Y. S. 645 (1927).
to scrutiny on constitutional grounds and has been upheld repeatedly. Although, for tax purposes, the transfer is deemed to be effected by the appointment, still the title is actually derived from the donor.

The second portion of section 220 provided that when there was a failure or omission to exercise the power, a taxable transfer in the estate of the donee should be deemed to take place, which again was a statutory alteration of the common law for tax purposes.

The provisions of this section standing alone would cause no dilemma, and in such cases the taxing authorities would postpone the assessment until the donee of the power appointed the property or there was a failure to exercise. When this portion of the statute is construed in connection with section 230 of the same act, the legislative intent is not clear, and it is this vexatious predicament with which we are chiefly concerned.

In 1899 section 230 of the New York Law was amended to provide:

... when property is transferred in trust or otherwise, and the rights, interests or estates of the transferees are dependent upon contingencies or conditions whereby they may be wholly or in part created, defeated, extended or abridged, a tax shall be imposed upon said transfer at the highest rate which, on the happening of any of said contingencies or conditions would be possible under the provisions of this article. ...


12 Under a statute similar to section 220, Massachusetts postpones the tax and assesses it in the donee's estate. There is no statute, however, providing for the taxation of contingent interests. See Minot v. Stevens, 207 Mass. 588, 93 N. E. 973 (1910).

13 Laws of 1899, C. 76, p. 100.
It was also provided that if, on the happening of the contingency or condition, the property should be transferred to a person exempt from taxation, or taxable at a rate less than that imposed, such person should be entitled to a refund equal to the difference between the amount paid and the amount which said person should pay.

It should be observed that section 230 applies generally to contingent interests and does not specifically mention powers of appointment. Framed in this general manner, the foregoing section indicates the intent of the legislature to assess the tax in the estate of the grantor or testator “at the highest rate” possible upon the happening of any contingency or condition limited in the will, in order to avoid the possible difficulties in assessing and collecting an additional tax at the time the contingent interest ultimately vests.

The first leading case in New York involving the interpretation of these statutory provisions was In re Howe,\textsuperscript{14} decided in 1903, which held that the inheritance tax was to be postponed until the exercise or non-exercise of the power by the donee created a taxable transfer within the meaning of section 220. The facts of the case were that Elizabeth L. Howe, the testatrix, created a testamentary trust giving to Leavitt Howe a life estate and a general power of appointment over the remainder, provided that if there was not a valid exercise of the power the remainder should go to his children and their heirs. A similar trust was created for Edward Howe. The executors of the estate contended that it was the exercise of the power and not its creation which effected the taxable transfer under the provisions of subsection 5 of section 220, C. 284, p. 868 of the Laws of 1896, as

\textsuperscript{14} 86 App. Div. 286, 83 N. Y. S. 825 (1903), affirmed in 176 N. Y. 570, 68 N. E. 1118 (1903).
amended. The State contended, however, that the amendment of section 230 by the Act of 1899, providing for the immediate taxation of contingent interests, repealed by implication the section relied on by the executors, and that a tax should therefore be presently levied at the highest rate. Justice Bartlett, writing for the court, stated that the amendment did not by implication repeal section 220, and that the tax should be postponed until the exercise or non-exercise of the power in the estate of the donee, thus giving full effect to the fifth subdivision of section 220 of the New York Tax Law.

This case, which is the first expression by an appellate court in the state of New York under the statutes as then in existence, annunciates the law in that state until 1911, at which time both sections 220 and 230 were amended, the effect of which amendments, according to subsequent decisions, was to change the law and to supersede the

See Matter of Seaver, 63 App. Div. 283, 71 N. Y. S. 544 (1901), and Matter of Walworth's Estate, 66 App. Div. 171, 72 N. Y. S. 984 (1901), relied upon by the executors to the effect that it is not the creation but the exercise of the power which creates the taxable transfer.

"The phraseology of this amendment of 1899 is not such as necessarily to embrace a case like the present, where a testamentary power of appointment is bestowed upon the life beneficiary of a trust. ... It is to be observed that the amendatory statute ... makes no change whatever in any section of the transfer tax law, except section 230. It leaves unchanged section 220, the fifth subdivision of which, relating to powers of appointment, has already been quoted. The effect of the amendment, therefore, was the same as though one statute had been enacted containing subdivision 5 of section 220 and section 230 as changed in 1899. We thus have, in contemplation of law, an act of the Legislature containing specific directions as to the taxation of estates in regard to which a power of appointment is conferred upon the original transferee; and I do not see how it can well be held that a subsequent provision in the same statute in regard to the taxation of transfers of property where the estates of the transferees are dependent upon contingencies or conditions effects a repeal by implication of the specific provisions relating to transfers through the instrumentality of the donee of the power. Neither the Matter of Vanderbilt's Estate, 172 N. Y. 69, 64 N. E. 782, nor the Matter of Brez's Estate, 172 N. Y. 609, 64 N. E. 958, bears upon the question in controversy here. Those decisions relate wholly to the effect of section 230 of the transfer tax law, and the opinions contain nothing in conflict with the views which have been expressed."
doctrine of the Howe case.\(^{17}\)

In 1911 the portion of section 220 providing for a taxable transfer in the estate of the donee upon the omission or failure to exercise the power was stricken.\(^{18}\) Section 230 was also amended to provide for the entry of a temporary order by the surrogate assessing the tax, the order to become final after a reassessment upon the happening of the contingency or condition.\(^{19}\)

It should be noted that there was nothing in the amending act of 1911 which made section 230 specifically applicable to powers of appointment, the general nature of the section being retained as in its original form.

The amendment to section 220 followed an opinion handed down by the Court of Appeals in 1905 in *Matter of Lansing*,\(^{20}\) which held that the omitted portion was unconstitutional in that it endeavored to predicate a tax on a transfer which could never take place.\(^{21}\)

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\(^{17}\) Prior to In re Howe there was some conflict as to the proper interpretation to be given to the New York statutes. In re Field's Estate, 36 Misc. 279, 73 N. Y. S. 512 (1901), and In re Howell's Estate, 34 Misc. 432, 69 N. Y. S. 1016 (1901), gave effect to section 220 and postponed the tax, which principle was subsequently adopted by the Howe case. However, the case of In re LeBrun's Estate, 80 N. Y. S. 486 (1902), held that the property subject to the power was presently taxable under section 230 as amended. The court stated, on the authority of *Matter of Vanderbilt*, 172 N. Y. 69, 64 N. E. 782 (1902), reversing 68 App. Div. 27, 74 N. Y. S. 450 (1902), and *Matter of Brez's Estate*, 172 N. Y. 609, 64 N. E. 958 (1902) (both of which were discredited by In re Howe) that the transfer subject to tax was the passing of title or interest out of or from the estate of the decedent, even though the transferee is not ascertainable at the time, and without regard to how obscure, remote, or contingent the remainder might be. The court stated that it had not overlooked section 220 in reaching its decision. This may be seriously questioned.

\(^{18}\) Laws of 1911, C. 732, sec. 1.

\(^{19}\) Laws of 1911, C. 800, sec. 1.


\(^{21}\) Justice Vann, writing for the court, stated: "Where there is no transfer there is no tax, and a transfer made before the passage of the act relating to taxable transfers is not affected by it, because, as we held in the Pell case, such an act imposes no direct tax, and is unconstitutional, since it diminishes the value of vested estates, impairs the obligation of contracts, and takes private property for public use without compensation."
words, if the power were not exercised the transfer would not take place in the estate of the donee as provided by the statute, but would relate back to the estate of the donor.

Before considering the cases which arose subsequent to these important amendments, a qualification of the rule laid down in the case of *In re Howe* should be mentioned. In 1912 an opinion was written by the Court of Appeals in *Matter of Burgess*, which limited the postponement of the tax to those cases where the power of appointment was absolute and it was certain that the property would pass upon the exercise or non-exercise of the power. After expressing affirmation of the principle annunciated in the Howe case, the court distinguished the cases on their facts and held that the power was not absolute, and for that reason taxed the remainder in the estate of the donor.

The effect of the amendment of 1911 was not immediately reflected in the decisions which followed. Except for the modification made by *Matter of Burgess*, the rule established by *In re Howe* was followed and approved on several occasions.


23 "The embarrassment as to the taxation of the remainders in the residuary estate is caused by the fact that it is not certain whether there will be any power of appointment to be exercised over the whole or any part of the residuary estate. The executors are to divide the property into as many shares as there may be living daughters or issue of a deceased daughter at the death of the widow. If at such time any daughter shall have died, leaving issue then surviving, such issue will inherit directly under the will, and not by virtue of the exercise or non-exercise of any power of appointment, and such inheritance will comprise a part or the whole of the property, dependent on whether any of the other daughters shall survive that period. If none of the daughters shall live until that time, none will have any power of appointment. The result would be that, if the rule of *Matter of Howe*, supra, was applied to the present case, the remainders might escape taxation altogether. For that reason, the learned courts below held that the rule applies only where there is an absolute gift of a power of appointment, so that the property is certain to pass, either under the exercise or non-exercise of the power of appointment, and that the case before them was not within the rule. In this view we concur." 204 N. Y. 265, at p. 270 (1924).

In 1916 the Surrogate’s Court wrote an opinion in the case of *In re Neher’s Estate*, where the will gave the life tenant a power of appointment over one-half of the remainder. It is apparent from the opinion that no significance was then attached to the amendments which were subsequently held to change the doctrine of *In re Howe*.

In the same year *In re Moore’s Estate* held that the tax was postponed. As late as 1919 the Surrogate’s Court in the case of *In re Stebbins’ Estate* postoned the tax where the decedent’s son had a life estate in one-fifth of the residuary estate with a special power of appointment, which was deemed by the court to be absolute in nature. The Howe case and *Matter of Burgess* were cited and relied upon.

It was not until 1921 that it was held that the tax should be assessed and collected in the donor’s estate. *In re Canda’s Estate* was the first to deviate from the rule followed by the line of cases heretofore noted. The Appellate Division, however, held that no tax was due at all and that there was no need to decide the question.

25 95 Misc. 69, 158 N. Y. S. 454 (1916).
26 “The one-half of the remainder over which the widow has a power of appointment is not presently taxable. [Citing Matter of Howe.] The amendment of section 230 of the Tax Law . . . did not change the language of the statute, so as to make the principle of the decision in the Matter of Howe inapplicable, as that amendment provided only for the entry of a temporary order by the surrogate. That part of section 230 which provides for the imposition of a tax at the highest rate was in force at the date of the decision in the Matter of Howe, supra. Therefore that decision is still controlling, and a remainder which is subject to an absolute power of appointment is not taxable until the power is exercised.” 158 N. Y. S. 454, at p. 455 (1916).
27 162 N. Y. S. 213 (1916).
30 114 Misc. 161, 185 N. Y. S. 903 (1921).
31 The court stated: “The amendments of 1911 to section 230 and the additional provisions for interest or income in favor of the beneficiaries in section 241 require that the tax shall be presently imposed and not suspended. There is nothing peculiarly sacred about estates which are transmitted by means of powers, and there is no sound reason why they should not be governed by the same rules which control the devolution of estates by other methods.”
as to the time of assessment.\textsuperscript{32} The opinion of the lower court is not, therefore, authority on this point.

\textit{In re Duff's Estate}\textsuperscript{33} followed shortly thereafter and reaffirmed the point that the taxable transfer took place in the estate of the donor, although under the peculiar circumstances involved it is not a clear-cut authority as to the present taxability in the donor's estate.\textsuperscript{34}

The next case decided was \textit{In re Trumbull's Estate}.\textsuperscript{35} A trust under the decedent's will was created, a life estate and a general power of appointment being given to his son. In default of appointment the remainder was to go to the issue of the son living at his death. The court held that the remainder was presently taxable for two reasons: first, that the power was not absolute as the donee was not the owner of the legal title under the real property laws of that state (a factual differentiation from \textit{In re Howe}); second, that the amendments to sections 220 and 230, and the addition of section 241\textsuperscript{36} by the Act of 1911 effected a change in the law as set forth in the Howe case. The court stated:

\ldots Section 241 of the Tax Law \ldots makes clear the legislative intent of requiring prompt payment of taxes at the highest rate at which they may be taxed, and the immediate imposition of taxes on remainders subject to conditions and contingencies. \textit{Matter of Zborowski}, 213 N. Y. 109, 107 N. E. 44, \textit{In re Parker's Estate}, 226 N. Y. 260, 123 N. E. 366.\textsuperscript{37}

\ldots

By the same amendment in 1911 this legislative purpose was em-

\textsuperscript{32} 197 App. Div. 597, 189 N. Y. S. 917 (1921).
\textsuperscript{33} 114 Misc. 309, 186 N. Y. S. 259 (1921).
\textsuperscript{34} The donor died in 1904 and the donee in 1918. The power had been ineffectively exercised. It was held that inasmuch as the order in the donor's estate did not mention the remainders it was not a binding adjudication as to the liability for present or future taxation. The court, therefore, decided the tax was assessable in the estate of the donor because of the unconstitutionality of section 220 as decided by \textit{In re Lansing}, 182 N. Y. 238, 74 N. E. 882 (1905), and that the transfer took place in the estate of the donor.
\textsuperscript{36} Discussed later herein.
\textsuperscript{37} Where reference is made to \textit{In re Parker's Estate}. 

phased by providing in section 230 of the Tax Law for the entry of a temporary order. These amendments, and the recent decisions of the Court of Appeals, supra, have entirely overcome the force and reason expressed in the opinion of In re Howe's Estate, . . . which held that taxation should be suspended where the power given was absolute. At the time of the latter decision, subdivision 6 of section 220 of the Tax Law provided for the taxation in the estate of the donee of the property affected by the exercise (or nonexercise) of the power. Apparently the court regarded this language as assuring the taxation of the property in the grantee's estate only. Subsequent to this decision in 1904, the Court of Appeals held that the statutory provisions for the tax in the donee's estate on the nonexercise of the power were unconstitutional. In re Lansing's Estate, 182 N. Y. 238, 74 N. E. 882. It will be noted that the provisions of section 241 were not effective until July 28, 1911.

The language of the court in the foregoing opinion and in the two cases following should be carefully noted.

It was in 1922 that the first leading case was decided in which an opinion was handed down by an appellate court. In that year the Appellate Division reviewed the case of In re Cole's Estate. The testator had created a testamentary trust giving to his daughter a life estate and a general power of appointment over the remainder. In the event there was not a valid disposition or exercise of the power the remainder was to go to the daughter's children. The residuary estate was bequeathed to trustees for the benefit of the testator's son for life, with a power of appointment over the remainder of the trust, and to his issue in default of appointment. The Surrogate held that it was the exercise of the power and not its creation which provided the taxable transfer and that the tax, therefore, was not presently payable in the estate of the donor of the power. This position was reversed when the case went to the Appellate Division, the court stating:

Respondent seeks to sustain that portion of the order appealed from relating to the present taxability of the remainders by the decisions in *Matter of Howe's Estate*, . . . and *Matter of Burgess' Estate* . . ., while it is urged by the appellant under the amendments to the Tax Law (sections 230 and 241), made by chapter 800 of the Laws 1911, and the recent decisions of the Court of Appeals (*In re Zborowski's Estate*, . . .; *Matter of Howe's Estate*, supra), which held that taxation should be suspended where the power given was absolute (*Matter of Trumbull's Estate*, . . .; *Matter of Parker's Estate*, . . .), that it is entirely possible that the powers of appointment will not be exercised, and that the taxation will therefore ultimately be assessed against the donor's estate (*Matter of Canda's Estate*, . . .). The decision in *Matter of Howe's Estate* seems to indicate that it is based upon the ground that section 230 did not by implication repeal subdivision 6 of section 220 of the Tax Law; but the conclusion reached by Judge Cardozo, 226 N. Y. 260, 123 N. E. 366, indicates that it was the intention of the Legislature to provide for the present taxation of remainders limited upon conditions and contingencies.

An appeal was taken to the Court of Appeals, which affirmed the opinion of the Appellate Division. Because of the importance of this decision, the full opinion of Justice McLaughlin pertaining to this question is quoted. Whether the remainders in these two trusts are presently taxable is one of the questions presented. Its solution necessarily turns upon the construction to be put upon section 220, subd. 6, of the Tax Law (Consol. Laws, c. 60), when the same is read in connection with section 230 of the same act, as amended by Chapter 801 of the Laws of 1911. These two sections are, apparently, in hopeless conflict, but, when read in the light of judicial construction placed upon them, it seems to me that each can be given full force and effect, and in such a way as not to make them inconsistent. Undoubtedly, if section 220 be considered in and by itself without reference to section 230, Tax Law, (Consol. Laws, c. 60; Laws 1909, c. 62), then these remainders are not presently taxable, and a tax cannot be imposed.

40 138 N. E. 733, at p. 734 ff.
until the power of appointment has been exercised. (Matter of Burgess, 204 N. Y. 265, 97 N. E. 591; Matter of Howe's Estate, 86 App. Div. 286, 83 N. Y. Supp. 825; affirmed, 176 N. Y. 570, 68 N. E. 1118.) But after these decisions were made section 230 was amended (Laws 1911, c. 800; Laws 1916, c. 550) so as to seemingly change the law on that subject, so that section 230, after those changes were made, provided:

"... When property is transferred in trust or otherwise, and the rights, interests or estates of the transferees are dependent upon contingencies or conditions whereby they may be wholly or in part created, defeated, extended or abridged, a tax shall be imposed upon said transfer at the highest rate which, on the happening of any of said contingencies or conditions, would be possible under the provisions of this article and such tax so imposed shall be due and payable forthwith by the executors or trustees out of the property transferred, and the surrogate shall enter a temporary order determining the amount of said tax in accordance with this provision; provided, however, that on the happening of any contingency whereby the said property, or any part thereof, is transferred to a person or corporation exempt from taxation under the provisions of this article, or to any person taxable at a rate less than the rate imposed and paid, such person or corporation shall be entitled to a return of so much of the tax imposed and paid as is the difference between the amount paid and the amount which said person or corporation should pay under the provisions of this article...."

When this statute was enacted the Legislature must be presumed to have known what construction had theretofore been put upon the statutes by the courts; in other words, it was charged with knowledge of certain legal principles in framing the statute. The general rule, as I understand it, is that when the Legislature amends or enacts anew a statute, it will be assumed that it had full knowledge of all the judicial decisions theretofore made interpreting the statute as then existing, and that being so, the new enactment must be read in the light of such previous interpretation. Orinico Realty Co. v. Bandler, 233 N. Y. 24, 134 N. E. 823; Komanda & Co. v. United States, 215 U. S. 392, 30 Sup. Ct. 136, 54 L. Ed. 249; Ceasar v. Bernard, 156 App. Div. 724, 141 N. Y. Supp. 659, affirmed, 209 N. Y. 570, 103 N. E. 1122.

This view was clearly expressed by Justice Miller, speaking for this court in Matter of Zborowski's Estate, 213 N. Y. 109,
112, 116, 107 N. E. 44, 45, where he said: "The Legislature has unmistakably expressed the intention that all transfers shall be assessed for the purpose of taxation as of the date of the transfer, and, however unjust that may be thought to be, it is not open to objection on constitutional grounds. . . . In one aspect it may be unjust to the life tenant to tax at once the transfer, both of the life estate and of the remainder, though contingent, and it may seem unwise for the state to collect taxes which it may have to refund with interest, but those considerations are solely for the Legislature, who are to judge whether they are more than offset by the greater certainty which the state thus has of receiving the tax ultimately its due under the statute. However unwise or unjust it may seem in a particular case like this for the state to collect the tax at the highest rate when in all probability the remainder will vest in a class taxable at the lowest rate, it is the duty of this court to give effect to the statute as it is written.'"

This authority was followed in Matter of Parker's Estate, 226 N. Y. 260, 123 N. E. 366. Each of these remainders, therefore, was properly assessed, and at the rate stated, and the order appealed from, to this extent, is affirmed.

The fact that the Court of Appeals stated that section 230 was amended so "as to seemingly change the law on that subject" should be carefully noted. It should also be observed that the court has quoted from and relied upon Matter of Zborowski's Estate and Matter of Parker's Estate as indicating the intention of the Legislature in amending the Tax Law. A further discussion of these salient features of this decision is reserved at this point.41

The most recent case arising in New York overruling the decision reached in the Howe case is In re Davison's Estate, decided in 1929.42 The important issue in the case involved the question of perpetuities which is not here discussed. The facts of the case were that the testator set aside two-thirds of his estate for the creation of trusts, one share to go to each child surviving him,

41 These matters will be mentioned later herein.

42 134 Misc. 769, 236 N. Y. S. 437 (1929).
or if any child predeceased him to the children of such child per stirpes. Upon the death of each beneficiary his portion was to be divided among his children, provided, “Should he leave none, or should any child of mine or child predeceasing me die leaving no such child, then I direct that the respective shares or portion be paid unto the person or corporation in such manner, as the last beneficiary of the income of such share or sub-share shall direct by duly executed and probated last will and testament, and in default of such appointment, or insofar as the same, if made, shall not be effectual then such share or subshare shall be paid to the persons who shall then constitute the heirs at law of such last beneficiary.” The opinion of the court with reference to the question involving the power of appointment is brief, and is quoted in full.

There remains for consideration on this phase of the problem only the question of the death of a primary or secondary life tenant without issue, which is the phase of the matter involving the propriety of the transfer tax assessment. If any life tenant leaves issue, such issue will take under the terms of the will; the taking being either in trust or outright, depending on the considerations just discussed. Failing such issue, however, the life tenant is given a power of appointment, the manner of exercise of which cannot presently be determined, and which, conceivably, may be in favor of a person in the 5 per cent class. Thus it is entirely possible that any one of the present life beneficiaries might have no children living at his or her decease (Ruth D. Stewart has none at the present time), and that he might exercise the power of appointment in favor of a stranger. It follows, therefore, that the remainders are presently taxable at the highest rate. Tax Law, sec. 230, Matter of Cole’s Estate, 235 N. Y. 48, 138 N. E. 733; Matter of Kenly’s Estate, 133 Misc. Rep. 718, 233 N. Y. S. 681; Matter of Sperling’s Estate, supra. [133 Misc. 834, 234 N. Y. S. 119 (1928).]

It is to be noted from the short opinion that the court has not entered into an independent discussion of the principles involved, and has considered the question
closed by the authorities cited. The real basis for this opinion is found in Matter of Cole, inasmuch as the last two cases cited by the court are foreign to the subject at hand and do not involve the question of the present taxability of a power of appointment.

After examining all of the New York cases on this subject which have effected a reversal of the doctrine adopted in the Howe case, one may justifiably ask upon what basis In re Howe has been overruled. Much has been said in the opinion referred to as to the effect of sections 230, 241, 222 and the cases of Matter of Zborowski’s Estate and Matter of Parker’s Estate, and although section 220 as amended in 1911 has been mentioned, the full significance of its terms and provisions has been overshadowed by the repeated references to other statutory provisions and cases which, it is submitted, have no effect upon the question at all. Quotations have been made freely, and in many instances at length, for it is believed that the vagueness of the opinions can be most convincingly presented in that fashion.

Upon what basis has In re Howe been overruled? What is the effect of the amendments to section 230? What is the effect of sections 222 and 241? After we have attempted to answer these questions, we shall undertake to discuss in greater detail the provisions of section 220 as amended in order to show that the correct basis for nullifying the Howe case lies in and only in the amendment to this section. The political and social philosophy to be extricated from the other provisions of the statute mentioned may justify the ultimate decision in view of the fact that the state is assured greater certainty in the collection of the tax, but this philosophy does not seem to be sufficiently cogent to warrant and justify its application as the principal basis for the

48 See Kidder, State Inheritance Tax and Taxability of Trusts, p. 58, wherein he discusses some of the hazards incurred in postponing the tax.
change made in the face of express statutory regulation with reference to powers of appointment.

*In re Trumbull's Estate* was based upon the amendments to sections 241 and 230, which together with "the recent decisions of the Court of Appeals, have entirely overcome the force and reason expressed in the opinion of *In re Howe's Estate.*" (It was first decided by the court, however, that the power of appointment under review was not absolute, and that *Matter of Howe's Estate*, therefore, "would in no event be applicable to this estate for there the power was absolute.") The recent decisions referred to are *In re Parker's Estate* and *Matter of Zborowski's Estate.*

The Parker case, however, is not authority for the question under consideration inasmuch as the court was there concerned only with the question of whether the contingent remainder should be added to the residuary estate, both of which might conceivably vest in the same person, in computing the amount of tax presently payable.\(^{44}\)

\(^{44}\) A testamentary trust was established, the income from which was to go to Edith Parker for life, and at her death to her issue then living, and to the children of any issue who predeceased her *per stirpes*, for life. Each child or grandchild who survived to receive his or her share had a power of appointment over his or her portion of the estate. In default of appointment the remainder was to go to their heirs. The residuary estate was bequeathed to John H. Parker, a nephew, including all lapsed legacies. The residuary, therefore, might include the principal of the trust in the event the life tenant died without issue. The question before the court was whether for purposes of taxation at the highest rate the residuary and the remainder should be added together and taxed to the nephew.

A portion of Justice Cardozo's opinion, which is frequently cited and quoted, is as follows: "Remainders are to be appraised at their present value. . . . They are gifts, like present interests. In fixing their value, no distinction is to be drawn between the classes of remainders, whether vested or contingent. For the purposes of taxation, the contingency is eliminated, and the gift is classed as absolute. . . . The value of other gifts to the same legatee must be reckoned in computing the tax when the remainder is vested. The method of computation is not different when the remainder is contingent. It is argued that in providing against contingencies, we should limit ourselves to those that the testator may be supposed to have foreseen. We need not stop to inquire whether that is so. There is nothing to show that this contingency was not foreseen by the testator, and covered by his will. He might have said, in so many words, that the nephew should receive the remainder in default of issue of the life tenant. He said the same thing in
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Nor is the case of Matter of Zborowski’s Estate, cited and relied upon, support for the decision reached, as the court is there only confronted with the taxation of remainders generally, contingent and vested, and does not deal with a power of appointment at all. The consideration of that general question, of course, does not call for a construction and interpretation of the amended portion of the statute dealing with powers of appointment, with which we are primarily concerned.

Although the dicta extracted from Matter of Parker and Matter of Zborowski, regarding the desirability of the state’s collecting at the earliest possible date the greatest amount of tax which may be due under any contingency, may sound convincing in its general scope, it bears no weight in application in the light of the factual circumstances of the cases in question.

The only statement made by the court in the Trumbull case with reference to the amendment to section 220 was that In re Howe regarded that section in its original form “as assuring the taxation of the property in the effect when he provided that his nephew should be the residuary legatee. Gifts have the same value whether they are stated separately or collectively. The rate of taxation does not vary with the paragraphs of scriveners.

“This construction of the statute maintains the consistency of the law and its singleness of purpose. The state has secured itself against all contingencies, remote as well as probable. That is the dominant scheme, which it is our duty to preserve. In the case before us, the contingency is in all likelihood remote, and so the mind rebels a little against the tying up of money. But in other cases it may be less remote, and the need of protection greater. Whether in improbable contingencies the risk justifies the burden it is not for us to say. That is a question for the Legislature. Our duty is done when we enforce the law as it is written.” Matter of Parker, 226 N. Y. 260, 123 N. E. 366 (1919), reversing 185 App. Div. 300.

The income of a residuary trust was to go to the son of the testatrix until he reached the age of 21, at which time he was to receive the principal. If the son should die before reaching 21, the principal was to go to his issue, and if no issue, to named persons who were in the highest taxable class. The court referred to section 230 and stated, on page 112: “The Legislature could not have used plainer language to express a purpose to impose a tax on all transfers immediately upon the death of the transferor regardless of the fact that particular transfers may be of contingent estates in remainder which may not ultimately be taxable at all.” Matter of Zborowski’s Estate, 213 N. Y. 109, 107 N. E. 44 (1914), reversing 163 App. Div. 947. See also portion of opinion quoted by the court in In re Cole’s Estate, supra.

45 The income of a residuary trust was to go to the son of the testatrix until he reached the age of 21, at which time he was to receive the principal. If the son should die before reaching 21, the principal was to go to his issue, and if no issue, to named persons who were in the highest taxable class. The court referred to section 230 and stated, on page 112: “The Legislature could not have used plainer language to express a purpose to impose a tax on all transfers immediately upon the death of the transferor regardless of the fact that particular transfers may be of contingent estates in remainder which may not ultimately be taxable at all.” Matter of Zborowski’s Estate, 213 N. Y. 109, 107 N. E. 44 (1914), reversing 163 App. Div. 947. See also portion of opinion quoted by the court in In re Cole’s Estate, supra.
grantee's estate only," and that the omitted portion was declared unconstitutional after the decision in the Howe case was handed down. There is no discussion as to the effect the remaining portion of section 220 might have.

The second leading case, In re Cole's Estate, is likewise based upon In re Parker's Estate and Matter of Zborowski. That the court has been confused and has given undue consideration to the general language in those two cases is obvious from the opinion itself.

The court recognized the conflict which existed between sections 230 and 220, and stated that if the latter were considered by itself the remainders could not be presently taxed, citing Matter of Burgess and In re Howe's Estate. In the next sentence, however, the court stated, "But after these decisions were made, section 230 was amended... so as to seemingly change the law on that subject." The court therefore held that the temporary order provision of the 1911 amendment to section 230 completely overruled the effect of section 220 in its amended form. The suggested uncertainty would seem to be warranted in view of the inapplicability of that section of the statute as subsequently pointed out. The opinion of the Court of Appeals is unsatisfactory in clearly establishing the basis upon which it is founded, and were it not for the opinion written by the Appellate Division the decision would be lacking in merit.

The third and last leading case, In re Davison's Estate, refers to section 230 and Matter of Cole's Estate to support the decision. The other two cases cited, Matter of Kenly's Estate, and Matter of Sperling's Estate, are as foreign to the subject under discussion as the Zborowski case, none of which involves the taxation of a power of appointment.

46 Supra, n. 22.
What is the effect of the amendments to section 230 of the New York Tax Law? The principal alteration in section 230 made by the amendment of 1911 was the addition of the provision that "the surrogate shall enter a temporary order determining the amount of said tax in accordance with this provision." The remaining provisions of this section provide that within six months after the happening of the contingency or condition upon which the remainder is limited, the representative of the estate shall make application for a final determination of the tax. In the event the tax as redetermined is less than that originally paid, a refund of the difference is to be made. Provision is also made for the deposit of a bond to cover any subsequent assessment in the event the personal property is less than the amount of tax required in the first instance. After the final determination, the court is to enter a "final" order assessing the tax.

Considerable importance has been attached to the "temporary order" provisions of this section by the cases referred to. Whatever may be the name, the procedure in the final analysis is not different from that employed in Illinois where the original order is final in its nature but is subsequently abrogated when the tax is reassessed and finally determined upon the happening of the contingency or condition. The original order in each instance accomplishes the necessary results and is sufficiently elastic to allow modification and a final determination at a later date.

The procedural provisions of section 230 may be significant in many respects, but the manner in which they change the substantive provisions of other sections is not apparent from the statute itself or from the judicial comments which have been made. As was said by the court

in the matter of In re Neher's Estate.\textsuperscript{51} "The amendment of section 230 of the Tax Law... did not change the language of the statute so as to make the principle of the decision in the Matter of Howe inapplicable, as that amendment provided only for the entry of a temporary order by the surrogate."

What does seem significant in this section is the absence of any reference to powers of appointment. Had the Legislature intended to include all cases involving a power of appointment within the general provisions of section 230, it would have used express language of inclusion. The absence of specific exclusion of this class of contingent remainders certainly does not imply inclusion in view of the fact that powers of appointment are specifically dealt with in section 220.

It is submitted that the amendment to section 230 providing for the entry of a temporary order did not warrant the construction and effect given to it—that the tax in all instances should be presently assessed in the estate of the donor.

What effect have sections 222 and 241 of the New York Tax Law? These two sections which have been cited and relied upon have no effect upon the principle involved. Section 241 was amended in 1911 to provide that the Tax Commission shall deposit in a sound bank all tax monies which are collected on contingent interests at the highest rate, and shall hold the same until the contingency or condition occurs, at which time the amount by which the tax as finally determined exceeds the amount of the deposits is to be turned over to the representative of the estate, and the balance, if any, is surrendered to the State Treasurer.\textsuperscript{52} It was the purpose of the amend-

\textsuperscript{51} Supra, n. 25.

\textsuperscript{52} It is unfortunate that provisions similar to those in section 241 are not to be found in the Illinois Act. Many of the difficulties encountered in obtaining refunds, and the objections on behalf of the life tenant as to the loss of income from the amount deposited, are satisfactorily eliminated.
ment to this section to eliminate the objection commonly raised that the assessment at the highest rate inflicts a hardship on the life tenant. In entering the temporary order the court determines the lowest and the highest taxes possible under the contingencies expressed in the will, the difference between these two sums bearing interest while deposited. The increment from the interest-bearing portion is paid to the executor of the estate who in turn distributes it in accordance with the provisions of the will. This provision is a successful expedient in surmounting the objectionable difficulties formerly incident to the collection of the tax at the highest possible rate. Its scope is general, however, and aside from indicating the intent to eradicate administrative difficulties in the assessment, it would seem to have no more application to those cases involving a power of appointment than the provisions of section 230 which deal with contingent remainders generally.

Section 222 provides that the tax on any interest limited, conditioned, or dependent upon a contingency or future event, so that the fair market value thereof cannot be ascertained at the time of the transfer, shall accrue when the beneficial interest vests in possession or enjoyment. This section was in substantially the same form at the time the Howe case was decided. It is obvious after a cursory examination that the contingencies referred to in section 222 are dependent upon the property to pass and not the person to take.

It is impossible, therefore, to see any effect these two sections have upon the specific question with which we are concerned, and a further discussion of them is not deemed requisite.

What is the effect of the amendment to section 220 of the New York Tax Law? Section 220 in its original form

provided that a taxable transfer should be deemed to take place in the estate of the donee either upon the exercise or non-exercise of the power. The latter portion as we have seen was declared unconstitutional by *Matter of Lansing* and then repealed in 1911. In spite of the repeated utterances as to the effect of other statutory provisions with reference to the doctrine of *Matter of Howe*, we can, in considering the amendment of 1911 to section 220 establish the basic principle upon which the present New York law is predicated.

The remaining portion of section 220, dealing with the taxable transfer by the exercise of the power of appointment, is still in effect, and under its terms the transfer from the donee is for tax purposes the one subjected to the duty. No statutory change whatsoever has been made which affects the treatment of this class of taxable transfers.

The unconstitutionality of the non-exercise portion of section 220 has reinstated the common law doctrine, and upon the non-exercise of the power the property passing thereby is rightfully considered as taxable in the estate of the donor, from which the passage of ownership or beneficial interest to the appointee actually takes place. In the event there is no default clause in the instrument creating the power, the property passes by intestate succession in the donor’s estate if there is a failure to or defective exercise of the power. In the absence of specific authority to the contrary, this devolution must control for tax purposes as well. If there is a remainder over in the event of non-exercise, the transfer is still effected in the donor’s estate and must there be taxed.

There is little difficulty in applying the theory of section 230 to this situation, and this must be readily admitted. It will be recalled *Matter of Howe* decided that section 230 did not impliedly or inferentially overrule and render impotent the provisions of section 220, and that
the specific language of the latter with reference to powers of appointment must therefore govern. By virtue of the 1911 amendment, the force and reasoning of Matter of Howe has been restricted and limited to the side of the question dealing only with the transfer effected by the exercise of the power. The difficulty in applying section 230 to a transfer by reason of the non-exercise having been eliminated by the amendment, it necessarily follows that to the extent the doctrine of Matter of Howe has failed, section 230 has been given effect.

This seems to be the only reasonable interpretation to be put upon the provisions of section 220 as amended, and its real effect upon the rule of the Howe case would be to limit its application to those cases where there is a general power of appointment and there is no possibility of assessing the tax upon the assumption of non-exercise of the power. Its application has therefore been restricted to the point of practical extinction.

With but one exception, the New York decisions discussed have held the tax should be assessed upon the assumption of non-exercise. In re Trumbull's Estate involved a general power of appointment with a default clause in favor of the son's issue living at the time of his death. There is not one word in the opinion indicating that the court entertained the thought that it was possible to assess the tax on the assumption of exercise. The second question raised on appeal by the executor was that "the order improperly provides that the remainder interest should be taxed against the 5 per cent. class, instead of the 1 per cent. class." To this question the court replied:

The appeal upon this ground is sustained. No provision was made in the will of decedent for the disposition of the remainders in case his son should die without issue and without having exercised the power of appointment. In this contingency the

54 191 N. Y. S. 759 (1921).
estate would vest as a reversion in the son as the sole next of kin of decedent. . . . Under the donor's will, the remainders, therefore, must ultimately pass to a person in the 1 per cent. class. . . . The tax should therefore be fixed at that rate, and the order should be modified accordingly.55

Since a general power had been granted to the donee, the tax could have been assessed to a stranger had the assumption of exercise been resorted to. It clearly appears, therefore, that the tax was there assessed upon the assumption that the power would not be exercised, although the court has not in so many words made the distinction.

The opinion of the Court of Appeals in the case of In re Cole's Estate,56 considers only the question of the present taxability and does not mention the assumption upon which the tax is based. The court does, however, indicate that it affirmed this method of assessment by stating: "Each of these remainders, therefore, was properly assessed, and at the rate stated. . . ."57 By referring to the opinion of the Appellate Division in the same case, there can be no question as to the decision of the court, for it is there stated, "I am therefore of the opinion that the surrogate erred in failing to provide for the present taxation of the remainders limited upon the default in the exercise of the powers, and of issue. . . ."58

Although the Surrogate in the case of In re Canda's Estate59 was overruled by the Appellate Division,60 on the ground that no tax was due at all under the facts presented, he had correctly interpreted the statute in assessing the tax upon the assumption of non-exercise.

It would seem from the foregoing authorities that it

55 Ibid, p. 761. The 1% and 5% classes were the lowest and highest classes respectively under the New York Act.
56 235 N. Y. 48, 138 N. E. 733 (1923).
57 138 N. E. 733, at p. 734.
58 195 N. Y. S. 541, at p. 546.
59 185 N. Y. S. 903.
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should have been well settled in New York that the tax could only be presently assessed upon the assumption of non-exercise after the 1911 amendment to section 220. However, the most recent case, *In re Davison's Estate,* reached a contrary decision, the court stating that it was entirely possible that the power would be exercised in favor of a stranger in the 5 per cent class, and that the remainders were therefore taxable at the highest rate.

This antithetical decision cannot be harmonized with the cases already pointed out, but it should be kept in mind that it is an opinion of the Surrogate's Court, whereas *In re Cole's Estate* was passed upon by the Court of Appeals, and *In re Trumbull's Estate* was affirmed without opinion by the Appellate Division.

By way of summary, therefore, the law of the State of New York may be stated as follows: The inheritance tax upon transfers of property passing under a power of appointment is to be presently assessed in the estate of the donor upon the assumption of non-exercise of the power.

After reviewing and discussing the cases arising in New York, the full significance of *People v. Linn,* decided by the Supreme Court of Illinois, can be more readily appreciated. It should be remembered that since the adoption of section 25 into our Inheritance Tax Law in 1909, which section provides for the immediate taxation of contingent interests at the highest rate, the general practice followed in this state has been to impose the tax in the estate of the donor of the power at the highest rate which, under the contingencies or conditions surrounding the remainder interest, could be assessed upon the assumption of exercise or of non-exercise. Certain instances have been mentioned by others in which the

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61 134 Misc. 769, 236 N. Y. S. 437 (1929).
62 See opinion quoted ante.
63 357 Ill. 220, 191 N. E. 450 (1934).
tax was postponed, but they constitute the exception and not the rule. *People v. Linn* was the first decision in Illinois subsequent to the addition of section 25 to pass upon the question with which we are concerned, and for that reason great importance is attached to it.

On April 21, 1934, the Supreme Court handed down its opinion in the Linn case in which it was decided that a power of appointment was not taxable in the estate of the donor at the highest rate, but that the tax was to be postponed until the exercise or non-exercise of the power created a taxable transfer in the estate of the donee. William R. Linn, the testator, died January 28, 1930. Under the terms of his last will and testament, residuary trusts were created for the benefit of his two daughters, Mabel and Dorothy, who were given life estates and general powers of appointment over their respective trusts. The provisions of the two trusts with reference to the powers of appointment are identical, the paragraph applicable to the trust for Mabel Linn being as follows:

(c) Upon the death of my daughter Mabel said trustee shall distribute and pay over the principal of said trust estate to whomsoever my daughter Mabel shall by her last will and testament appoint to receive the same, and in default of such appointment then to her issue living at the time of her death in equal shares *per stirpes*. If my daughter Mabel shall die intestate and fail to appoint said trust estate by will and shall leave no issue surviving her, then said trustee shall distribute and pay over said trust estate to my issue surviving at the date of the death of my daughter Mabel, in equal shares *per stirpes*, and in default of such issue then to the persons who at the date of the death of my daughter Mabel would have been my heirs-at-law under the laws of the State of Illinois then in force if I had died intestate.

The County Court of Cook County had presently assessed the tax on the remainders to a nephew of the decedent. From this decision the executors of the estate appealed. The principal contention of the executors on appeal, which was sustained by the court, was that under
subsection 4 of section 1 of the Illinois Inheritance Tax Law, the remainders which were subject to the powers of appointment were not presently taxable, but that the tax should be postponed, determined and collected in the estates of the donees of the powers. The controversy which created the important issue in the case was the construction to be placed upon that subsection in the light of section 25 of the same Act. Subsection 4 of section 1 of the Illinois Act as then in effect, was identical with section 220 of the New York Tax Law prior to the amendment of 1911, and provided that the taxable transfer was deemed to take place in the estate of the donee upon the exercise or the non-exercise of the power. Section 25 of our law was also copied from section 230 of the New York statute as it existed prior to 1911, and its provisions as to the taxation of contingent interest at the highest rate are substantially the same.

The Illinois court, after considering the two sections above mentioned, decided that section 25 was qualified by subsection 4 of section 1, stating the familiar rule that the legislative intention is to be gathered from an entire act and not from a particular section thereof, and that one portion of an act may be intended to qualify, extend,

64 See ante, where section 220 of the New York Tax Law is quoted.

65 Sec. 25. "When property is transferred or limited in trust or otherwise, and the rights, interest or estates of the transferees or beneficiaries are dependent upon contingencies or conditions whereby they may be wholly or in part created, defeated, extended or abridged, a tax shall be imposed upon said transfer at the highest rate which, on the happening of any of the said contingencies or conditions, would be possible under the provisions of this Act, and such tax so imposed shall be due and payable forthwith by the executors or trustees out of the property transferred; Provided, however, that on the happening of any contingency whereby the said property, or any part thereof is transferred to a person, corporation or institution exempt from taxation under the provisions of the inheritance tax laws of this state, or to any person, corporation or institution taxable at a rate less than the rate imposed and paid, such person, corporation or institution shall be entitled to a reassessment or redetermination of the tax and to a return by the State Treasurer of so much of the tax imposed and paid as is the difference between the amount paid and the amount which said person, corporation or institution should pay under the inheritance tax laws, with interest thereon at the rate of three per centum per annum from the time of payment." Ch. 120, sec. 419, Cahill's Rev. St. 1933.
limit or abridge other portions. Since the provisions of subsection 4 are special in nature, and have reference and application to a specific class of transfers, it was decided that the generally inclusive provisions of section 25 are to that extent qualified. It is difficult to argue that a portion of the act which specifically provides that all transfers effected by the exercise or non-exercise of a power of appointment are to be taxed in the estate of the donee, should be harmoniously applicable with a provision of the same act which in general and broad terms provides that wherever a contingency controls the vesting of interest or possession a tax should be presently collected at the highest possible rate.

Importance was also attached to section 3 of the Illinois Act, which provides that all taxes imposed by the act "unless otherwise herein provided for, shall accrue and be due and payable at the death of the decedent," indicating that the Legislature had intended that there should be a postponement of the tax under certain circumstances.

Having determined that section 25 and subsection 4 of section 1 were conflicting, and that the provisions of the latter relating specifically to powers of appointment should prevail over the general language of the former, the decision of the court would seem to be well reasoned and correct. It will be remembered that, although *In re Howe's Estate* interpreted the effect of the addition of section 230 by the amendment of 1899 subsequent to the incorporation of section 220 in the Tax Law, and reached the same conclusion as did *People v. Linn*, it was there

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stated that the effect of the amendment "was the same as though one statute had been enacted containing subdivision 5 of section 220 and section 230." Thus, the fact that in Illinois section 25 and subsection 4 of section 1 were adopted concurrently in 1909 does not alter in any way the argument resorted to in the Howe case.

The court next considered the relationship between the Illinois and New York statutes, and after referring to the sections hereinbefore discussed stated:

These apparently conflicting provisions were construed in the case of In re Howe, 86 App. Div. 286, 83 N. Y. Supp. 825; affirmed by the Court of Appeals, 176 N. Y. 570.... The State contended that the enactment in 1899 of the provision which corresponds to section 25 of the Illinois act repealed by implication the provision which is the counterpart of sub-section 4 of section 1 of our act. The court held that the amendment of 1899 did not repeal or render nugatory the section enacted in 1897, and that the remainders over which the sons had absolute powers of appointment were not taxable until the deaths of the donees. .... There is no expression or even manifestation of a legislative intent that the provisions of our act under review were not enacted in the light of the construction given them by the courts of the State of New York. When a statute is adopted from another state, the judicial construction previously placed on the statute by the courts of that State accompanies it, and is treated as incorporated therein....

The appellee maintains that the contrary construction of the New York statute now obtains, and that the Howe case, supra, has been overruled by later decisions. The provisions of the New York act, adopted in sub-section 4 of section 1 and section 25 of our Inheritance Tax Act in 1909, were amended in New York in 1911....

It is manifest that the subsequent amendments to the Inheritance Tax Law of New York differ essentially from the corresponding provisions of the Illinois act in effect on January 28, 1930, the day William R. Linn died. Sub-section 4 of section 1, postponing the tax on the transfer of property subject to powers of appointment, had not been changed at that time and differed

67 See n. 16 ante.
68 The court here stated the changes made by the amending act of 1911.
materially from the New York law then in effect. The statutory provisions relating to the imposition of inheritance taxes upon transfers subject to powers of appointment were the same on January 28, 1930, as when originally adopted in 1909 from the New York law. At the date of the death of the testator, William R. Linn, section 25 of the Inheritance Tax Act was still limited by sub-section 4 of section 1, and, accordingly, the remainders of the testamentary trusts over which his daughters have absolute powers of appointment were not presently taxable.

The analogy between the statutory provisions in effect at the time *In re Howe* and *People v. Linn* were decided makes the similarity of these two decisions strikingly apparent. In each instance the statute provided that the taxable transfer should be deemed to take place in the estate of the donee upon the exercise or non-exercise of the power, and in each instance the specific treatment of powers of appointment was held to be unaffected by the sections providing for the taxation of contingent interests generally at the highest rate. Inasmuch as *In re Howe* had so construed the New York Act prior to the adoption of similar provisions in Illinois in 1909, the principle of statutory construction resorted to by the court in *People v. Linn* is convincing and conclusive.

The decision of the court in the Linn case seems to be well reasoned and correct upon the theory that section 25 is modified and limited by the specific provisions of sub-section 4 of section 1, and is equally sound in the application of the rule of statutory construction referred to. The issues presented were properly decided and the statutory provisions then in effect were properly construed. Chief Justice Orr, who was joined by Justice Farthing, dissented from the majority opinion stating that the tax should be presently assessed in the estate of the donor.69

Since the decision in the Linn case has been announced,

69 The dissenting Justices wrote a vigorous opinion in support of their contention. Although this belief was not accepted by the majority of the court, it evidences a decided disagreement with the position herein submitted as the logical basis for future decisions, and for that reason merits mention at this time.
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the question has often been asked, "What is the present practice followed in this state as to the taxation of powers of appointment?" The inheritance tax on transfers subject to a power of appointment is now being presently assessed in the estate of the donor at the highest possible rate under the contingencies and conditions expressed in the will. It is immaterial whether the highest possible tax is produced by an assumption of exercise or non-exercise, for either assumption may be resorted to as a means to the desired end.

Two recent cases which were before the Inheritance Tax Office of Cook County, illustrate the position taken in dealing with this class of transfers. In one estate, two

Justice Orr takes the position that there is no conflict between subsection 4 of section 1 and the provisions of section 25. Divergence from the majority upon this score is fundamental and presages possible future difficulties depending upon the persuasiveness of his argument to the other members of the bench in the light of the 1933 amendment. He states that section 25 is unlimited in scope, whereas subsection 4 of section 1 is concerned only with transfers in the estate of the donee. If it is true as he believes that the latter section is not applicable in the estate of the donor, there can be no question as to the applicability of section 25 in all cases. When the transfer mentioned in subsection 4 of Section 1 is effected by the exercise or non-exercise of the power in the estate of the donee, there will be a redetermination and refund if necessary so that he contends both sections may be harmoniously and concurrently applicable. He states that if this were not the intention of the Legislature, express language of exclusion would be found in section 25.

If there is no conflict between these two sections, it was erroneous for the majority of the court to invoke the rule that particular and specific provisions of the act must prevail over those more general in character. This conclusion, of course, necessarily follows the premise already established.

Justice Orr endeavors to negative the significance attached to In re Howe by the majority, in stating that the New York Court was principally concerned with the question of whether the adoption of section 230 impliedly overruled the provisions of section 220, stating, "It thus appears that the taxation of remainders subject to powers of appointment in estates of donors was not before the court... in the Howe case."

Justice Orr further states that In re Howe was overruled by Matter of Cole, Matter of Parker, In re Davison's Estate, and Matter of Zborowski, and that "In the later decisions above cited, the New York courts, notwithstanding the specific provisions of subdivision 5 of section 220 (corresponding to the first part of our subsection 4 of section 1), imposing a tax on the exercise of a power of appointment by a donee, held that a remainder subject to a power of appointment is taxable in the first instance in the estate of the donor under sections 230 and 241, on the assumption that the donee might exercise the power in favor of a stranger."

70 Inheritance Tax Case No. 27164.
testamentary trusts were created, the income to be paid to cousins of the testatrix for life, and the remainders to pass as they by will should appoint. In default of appointment, the remainders were limited to named persons, who were in fact children of the life tenants. The tax was assessed upon the remainders in each instance to one child of the life tenant of each trust, being one of the individuals to whom the remainder had been limited in default of appointment.71

Another estate reviewed in this county shortly after the one just referred to illustrates the tax being assessed upon the assumption of exercise to a stranger.72 A life estate was given to a widow with remainders over to the testator's children. In the event the widow survived all of the beneficiaries named, she was to have a power of appointment over one-third of the entire estate. There was no default clause in the will. The tax was levied upon the theory that the widow would survive all the named beneficiaries and would appoint to a person who was a stranger in blood to the testator.73

The reason for the variance and inconsistency in method in the above estates cannot be explained in theory, but the latter represents the strict rule of assessments at the highest rate and is now unqualifiedly stated to be the

71 It should be pointed out that in People v. Linn the tax was originally assessed upon the assumption of non-exercise to a nephew (the default clause in the will limiting the remainder to persons in the first or second classes). In both of these cases the greatest possible tax could have been assessed by taxing to a stranger.
72 Inheritance Tax Case No. 27167.
73 The common law rule and the practice followed in this state is that the relationship of the appointee to the donor governs. Subsection 4 of section 1 provides that the exercise of the power shall be deemed a taxable transfer in the same manner as though the property "belonged absolutely to the donee." It would seem, therefore, that the relationship to the donee should control where the tax is levied upon the transfer effected by the exercise of the power. See the following cases so holding: Matter of Rogers, 71 App. Div. 461, 75 N. Y. S. 835, 172 N. Y. 617, 64 N. E. 1125 (1902); Matter of Walworth, 66 App. Div. 171, 72 N. Y. S. 984 (1901); In re Seaver's Will, 63 App. Div. 283, 71 N. Y. S. 544 (1901). For the common law rule see Gleason & Otis, Inheritance Taxation (3d. ed.), p. 171, citing Galard v. Winans, 111 Md. 434, 74 A. 626 (1909).
practice adopted by the members of the Attorney General’s office in charge of inheritance taxation. It is unfortunate that in neither of the instances referred to was the tax sufficiently large to warrant a contest and an appeal to the Supreme Court. The desire to make law must yield to the exigencies and financial expediencies involved in any case.

We have considered only general powers concerning which, by way of summary, we may state that the assumption of exercise in practically all cases will be made, as it is then possible to tax the remainder to a stranger.

Where a special power has been given, the highest possible tax will still be assessed under section 25, but the assumption upon which it is based may vary. For instance, a power may be limited to A, B, and C, all of whom are in the first or second class for tax purposes, and in default of appointment to D, E, and F, who are also in the same class. It makes no difference here whether the tax be assessed upon the assumption of exercise or non-exercise, and either may be used as a basis for the tax. On the other hand, if F happened to be a stranger, the tax would be levied upon the basis that there would be a default in appointment, and that D and E predeceased F. It has been a common belief by many that the tax will be assessed only upon the assumption of exercise, and by others upon the assumption of non-exercise. There is no justification for this misunderstanding under the present practice, and it is certain that whichever assumption affords the highest possible tax under the theory of section 25 will be indulged in by the officials levying the tax.

As to decedents dying prior to July 1, 1933, the doctrine of People v. Linn is now controlling, and the tax will be postponed. By reason of the amendment striking out the non-exercise provision of subsection 4 of section 1, the authorities in this state have looked to the New
York decisions, and have evolved the system of taxation herein discussed to be applied to those estates wherein the decedent died subsequent to July 1, 1933, the effective date of the amendment. It is submitted, however, that the interpretation given the decisions of that state is not correct to the extent that a tax may here be assessed upon the assumption of exercise.

What effect should properly be given the amendment of 1933 to subsection 4 of section 1 in the light of People v. Linn? No specific change has been made in the law as to those cases where the power is exercised, and there is no implication that a change was intended in the remaining portion of the section by the amendment of 1933. It is still required by the statute that in the event of exercise, the taxable transfer shall be deemed to take place in the estate of the donee in the same manner as though the property belonged absolutely to him. This would necessitate the tax being postponed and collected in the estate of the donee, except in those cases where the assessment can be made upon the assumption of non-exercise. The contradiction which existed at the time the Linn case was decided, between section 25 and the exercise provision of subsection 4 of section 1, still exists. The argument used by the court in that case so far as the exercise of the power is concerned, seems to be available and applicable at this time. It does not seem logical to read into the amendment an implication that any change was intended so far as the exercise of the power is concerned. On the contrary, the omission was identical with that made in New York in 1911, and as we have seen, with the exception of Davison's case, the decisions have limited the effect of the amendment to the non-exercise of the power.

The amendment of 1933 reinstates the common law doctrine as to those cases where there is a failure to exercise the power, so that the taxable transfer now takes place in the estate of the donor, and if it were not for the
provisions of section 25, the tax would be postponed in accordance with the practice prior to 1909.

It has been suggested that the similar amendment in New York modified and limited the ruling of In re Howe to those very few cases where the tax could not be assessed upon the assumption of non-exercise. This theoretical conclusion is applicable in this state as well. It clearly should not be assessed upon the assumption of exercise, because in that event the taxable transfer takes place in the donee's estate by virtue of the exercise provision of the statute still in force. A specific illustration will emphasize this. A creates a testamentary trust, giving a life estate to B with a general power of appointment, there being no default clause. When the estate is reviewed for inheritance tax purposes, the possibility that B might appoint to a stranger should not be the basis for assessing the tax immediately, as section 1 says the taxable transfer is to be in the estate of the donee. The tax should be assessed, therefore, upon the assumption that B will not exercise the power, and applying section 25, the tax may be presently levied at the highest possible rate under the circumstances. Now, suppose that a default clause has been attached whereby the donor provides that in the event the power is not exercised the property shall pass to X, Y, and Z, or the survivor of them. Again the tax would properly be levied on the assumption of non-exercise of the power and that X and Y would predecease Z, who would thereby take the entire remainder.

If the default clause provided that the remainder go to a local charity, it would follow that no tax would be presently assessed in the donor's estate, as the local charity would be exempt. Since no tax would be due at all in the event the power were not exercised, the assessment could only be made in the estate of the donee upon the exercise of the power. This appears to be the only instance where no tax is to be presently assessed and levied
in the estate of the donor, assuming that the tax cannot properly be predicated upon the assumption of exercise.

So long as subsection 4 of section 1 provides that the taxable transfer in the event of exercise of the power is deemed to take place in the estate of the donee, no other general theory as to the taxation of powers of appointment consistent with its presence seems logical. The conflict between section 25 and the foregoing provision is as obvious now, as it was prior to the amendment, and it is this fact which makes convincing the interpretation of the amended section which has been submitted that the tax cannot be presently levied upon the assumption of exercise. However, since the non-exercise provision of subsection 4 of section 1 has been stricken, there exists no conflict between section 25 and the theory that the tax can only be assessed upon the assumption of non-exercise, and the provisions of the latter section therefore may now be applied.

If the Supreme Court, in reviewing this question when it is again presented on appeal, is to give any credence to its opinion in the case of People v. Linn, it should agree with the conclusion reached herein. The court cannot give full force and effect to the theory of that decision in all cases involving a power of appointment, inasmuch as the amendment to subsection 4 of section 1 has eliminated entirely the argument employed that the tax should be postponed in cases where the taxable transfer takes place by reason of the failure to exercise the power. Nor, on the other hand, can it be logically decided that the tax in all instances should be presently assessed in the estate of the donor, for the argument resorted to in deciding that the tax should be postponed is still correct with reference to the remaining portion of the section and is not affected by the nature of the amendment in 1933. If both of these premises are sound, and it is believed that they
are in the light of this discussion, the only course open to the court is to hold that the tax cannot be presently assessed upon the assumption of exercise. To this extent the rule in *People v. Linn* should be modified.

If the practice now employed by the taxing officials of this state is subsequently upheld by the Supreme Court, in every instance where a power of appointment has been given, the tax will be presently assessed in the estate of the donor at the highest possible rate. This means, of course, that a large sum of money will be tied up during the existence of the preceding particular estate, thus diminishing the income to be paid to the life tenant. In most instances the interest paid by the state on any refund eventually obtained cannot compensate for this loss to the life tenant.

Should the Supreme Court, however, adopt the course submitted as the logical basis for its opinion, the tax would be presently assessed upon the assumption of non-exercise in all cases. Under such a ruling, of course, it is possible to avoid the onerous assessment to a stranger by carefully limiting the phraseology of the default clause.

Where the use of a power of appointment is advisable, a special power limited to named persons or a class affords more opportunity to guard against the undesirable features of section 25 than the general power. If the power be limited to the children of the life tenant, to his descendants, or to such other persons as the testator may desire, and coupled with such a provision is a default clause with similar provisions, the scope of the contingencies involved is narrowed down to a desirable point. The testator may limit the remainder to the natural objects of the donee's bounty or to his own preferences, and name individuals who are in the first and second class for taxation purposes. Where the remainder is limited to a class in lieu of named persons, section 25, of
course, will be applied to tax the entire remainder to one. Where the special power is used, the same theory is applicable to the exercise as well as the non-exercise provisions of the instrument, and each should be so framed as to limit the remainder to those in the first or second class.

Another great advantage to be gained by the use of a special power lies in the fact that for Federal Estate Tax purposes, the property passing under a special power will not be subject to tax in the estate of the donee.\(^7\) Property passing under a general power of appointment, however, is subjected to a Federal Estate Tax in the donee's estate.\(^8\)

It should be specifically pointed out that the possibility exists, although it is not here considered logical, that the desire of Justice Orr and Justice Farthing to interpret the existing statutory provisions as warranting the present taxability in all cases in the donor's estate, may be adopted by other members of the bench when the matter is again presented to the Supreme Court, and that no credence will be given to the theory of the argument used in the majority opinion in People v. Linn. In such event the decision of the court would permit the taxation in the donor's estate upon the assumption of exercise, which in turn opens the door to taxation in the third class in those cases where a general power has been used. It is to be noted that the dissenting opinion in the Linn case cited with approval In re Davison's Estate, in which the New York court upheld the assessment in the donor's estate upon the theory of the exercise of the power to a stranger. In order to avoid unfortunate complications in the event such a decision is forthcoming, a special power should be employed rather than a general one in all cases where it may be used satisfactorily.

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\(^7\) See Article 24, Federal Estate Tax Regulations 80.
\(^8\) Ibid.
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TAXATION OF INTERSTATE ELECTRICAL UTILITIES

The tremendous growth of interstate transmission of electric energy in the last decade\(^1\) has given rise to conflicting claims to jurisdiction for taxing and regulating purposes. This conflict characterizes the present chaotic taxing system with its forty-nine independent taxing authorities intermingled with numberless local bodies exercising similar functions and powers.\(^2\) It also emphasizes the need for revising the current methods of taxing.

Only by implication are the states forbidden to burden interstate commerce.\(^3\) However, the grant of power to the national government was early held to imply a converse prohibition upon state authority.\(^4\) This was not a total prohibition, but only such as was necessary to protect interstate commerce from being unduly burdened.\(^5\) Obviously, property used in interstate commerce is not, per se, exempted from the taxing power of the state, but may be taxed, provided, of course, there is no discrimination.\(^6\)

Railroads were the first interstate utilities to question the methods of allocating their property for taxation purposes among the various taxing units through which their lines extended. The courts first evolved the formula of the "unit rule";  

\(^1\) In 1933, for example, the national average for electricity delivered outside the state in which it was generated was about 20 per cent. Deliveries outside their boundaries varied among the states from 97.7 per cent for Maryland and 74.5 per cent for Virginia, at one extreme, to 3 per cent for Missouri at the other. More power crossed state lines in 1933 than was generated in the entire country in 1913. See table on "Interstate Electrical Energy Transactions during 1933," in the Interim Report of the National Power Survey, Federal Power Commission, 1935, at p. 46. See also the map facing p. 6 showing "Principal Generating Plants and Electrical Transmission Lines of the United States in 1934."

The principal interconnected networks or power areas include such units as (1) Vermont, New Hampshire, Massachusetts, Connecticut, and Rhode Island; (2) Pennsylvania, Maryland, Delaware, and New Jersey; (3) Alabama, Mississippi, Georgia and Tennessee; and, (4) the Pacific coast states.


\(^3\) "The Congress shall have the power . . . to regulate commerce . . . among the several states . . ." United States Constitution, Act. I, sec. 5, clause 3.

\(^4\) See Gibbons v. Ogden, 9 Wheat. 1 (1824).

\(^5\) Cooley v. Board of Wardens of Port of Phil. et al., 12 How. 299 (1851).

that is, each state in determining the value of property subject to its taxing power may find a value bearing the same proportion to the value of the entire property as the length of the railroad or telegraph or telephone lines within the state bears to the total length of the carrier system.\(^7\) Such a formula must obviously be one of convenience, not of inevitable application.\(^8\) If the court finds that it seems to operate inequitably in a particular case, its application will be pronounced violative of due process.

The general unit rule has long been applied to telephone and telegraph lines.\(^9\) However, the decisions are not yet clear regarding its application to interstate electrical utilities. In *Nevada-California Power Company v. Hamilton*,\(^10\) more than two-thirds of the value of the corporation's total property was represented by property and property rights in California, including the power plant and water rights; less than one-third of the value was represented by property in Nevada. However, approximately 85 per cent of the transmission lines was in Nevada while the other 15 per cent was in California. Nevada imposed a tax computed on 85 per cent of the use value of the corporation's property on the theory that a like proportion of the corporation's income was derived from its holdings in Nevada. It appeared that the State of California had actually taxed the cor-

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In Adams Express Co. v. Ohio, 165 U. S. 194 (1897), the rule was modified to the so-called "unit of use" formula: Property of an interstate carrier may be assessed for purposes of taxation at that value which, as a unity or single system, it has in use, to-wit, the net profits which it produces, irrespective of what may be the value of the tangible property which is owned or employed, apportionable as the amount of business done within the state is proportioned to the total amount of business done.

\(^8\) See Pitt., etc., Railway Co. v. Backus, 154 U. S. 421 (1894), where the large mileage in one state was over land where the construction cost was low and terminal facilities few and inexpensive, while in another state its mileage was small, but of expensive construction, with elaborate terminal facilities. See also Union Tank Line Co v. Wright, 249 U. S. 275 (1919); Wallace v. Hines, 253 U. S. 66 (1920); and New York Tax Commission, Special Report on Allocation of Corporate Income (1933).

\(^9\) See W. U. Tel. Co. v. State Board of Equalization, 91 Mont. 300, 7 P. (2d) 551 (1932), where the court treated landlines and ocean cables as an integral system. But compare Smith v. Ill. Bell Tel. Co., 282 U. S. 133 (1930), where the court (for rate-making purposes) treated the telephone company as a "segregated enterprise," although it admittedly had the advantages attached to being a component part of a large system and through such relations obtained cooperation with the manufacturing, research, engineering and financing departments of the holding company.

\(^10\) 240 F. 485 (1917), aff'd in 264 F. 643 (1920). Also see 235 F. 317 (1916).
poration on the same theory, that is, on 15 per cent of the use value of the total property. The Federal district court, later affirmed by the circuit court, declined to approve such method of apportionment, saying, "If the property in this case were homogeneous, that is, if it consisted entirely of one transmission line, if it were a telephone line, a telegraph line, or a railroad, it would be proper to pursue the method which has been used by the commission. . . ."\textsuperscript{11} This case, thus, may consequently be explained in terms of these particular facts. Yet, are not these precise facts characteristic of any interstate electrical transaction, where the generating plant is in one state and the transmission and distribution lines spread through several states? The court frowned on this attempt to tax property, the actual tangible value of which is situated outside the state by computing the tax on the proportion of transmission lines within the state.\textsuperscript{12}

However, the states have more than made up for this lost ground by developing a newer kind of tax, a tax upon the generation or distribution of electricity itself, without regard to the technical questions of the value of the network system. And, the Supreme Court of the United States has sustained it.

In \textit{Utah Power and Light Company v. Pfoist},\textsuperscript{18} a Maine corporation, doing business in Idaho, Utah, and Wyoming as a generating, transmitting, and distributing electrical utility, was subjected in Idaho to a license tax measured by the production of electricity, whether consumed inside the state or sent out, at the rate of one-half mill per kilowatt hour. The argument was made by the utility company that the generation and transmission of electricity was an instantaneous act, with no noticeable time differentiation, for electricity travels at the speed of approximately 186,000 miles per second. Transmission of electrical

\textsuperscript{11} At p. 489.

\textsuperscript{12} Line 6. Compare State v. Baker, 316 Mo. 853, 293 S. W. 399 (1927), involving an intercounty (i. e., intrastate) electrical utility, where apportionment on a mileage basis was approved. See also State v. State Board of Equalization, 56 Mont. 413, 186 P. 697 (1920).

Note that this limitation against taxing property beyond the jurisdiction of the taxing authority (as imposed by the due process clause of the 14th Amendment) has never been applied to the Federal government. Burnet v. Brooks, 288 U. S. 378 (1933). Theoretically this decision is directly contrary to First Nat. Bank v. Maine, 284 U. S. 312 (1932), except that the former involved international aspects, in which there is as yet no final judicial arbiter.

energy in interstate commerce is exempt, as such, from regulation by the state, and hence it may be assumed, from the state taxing power. It was urged that since there could be no difference between generation and transmission-distribution, the law should not make one. Consequently, it was argued, a state tax imposed indiscriminately upon such generation is violative of the commerce clause. But, the court reminded counsel that, in spite of all the scientific evidence as to the nature of electricity, "taxation is a practical matter." The court observed a distinction between the generation of electricity and its transmission in interstate commerce. The one was essentially a process of manufacture, and consequently precedent (in terms of logical analysis, if not in terms of fact) to the process of interstate commerce, and therefore subject to the taxing power of the state. The electrical utility was consequently found to be engaged in two activities, legally separable. So far as it produced electrical energy in Idaho, its business was purely intrastate, subject to state taxation and control. But, in transmitting the electricity across the state line into Utah, the utility assumed the character of an interstate business regarding which state legislation is subject to the paramount authority of the commerce clause. Mr. Justice Sutherland, in speaking for the court, said:

"While conversion and transmission are substantially instantaneous, they are, we are convinced, essentially separable and distinct operations. The fact that to ordinary observation there is no appreciable lapse of time between the generation of the product and its transmission does not forbid the conclusion that they are, nevertheless, successive and not simultaneous acts.... The effect of turning the switch in Utah is not to draw electrical energy directly from the waterfall, where it does not exist except as a potentiality, but to set in operation the generating appliances in Idaho, which thereupon receive power from the falling water and transform it into electrical energy. In response to what in effect is an order, there is production as well as transmission of a definite supply of an article of trade.... We think, therefore, it is wholly inaccurate to say that appellant's entire system is purely a transferring device. On the contrary, the generator and the transmission lines perform different functions, with a result comparable, so far as the question here under con-

15 U. S. v. E. C. Knight Co., 156 U. S. 1 (1895), where the court said, "Commerce succeeds to manufacture, and is not part of it." Compare the NRA decision.
consideration is concerned, to the manufacture of physical articles of trade and their subsequent shipment and transportation in commerce. . . . The evidence amply sustains the conclusion that this transformation must take place as a prerequisite to the use of the electrical product, and that the process of transferring, as distinguished from that of producing, the electrical energy, begins not at the waterfall, but definitely at the generator, at which point measuring appliances can be placed and the quantum of electrical energy ascertained with practical accuracy."

The full logic of this case received its application in *South Carolina Power Company v. South Carolina Tax Commission*,\(^\text{16}\) where a Federal district court sustained a tax imposed upon the sale (that is, distribution) of electricity by the state to which it had been transmitted, as well as a generating tax. The court reasoned that neither tax violated the commerce clause, for one was imposed before, and the other after, the process of interstate commerce. The transformer was singled out as of decisive importance—so much so, in fact, that it was suggested that the electricity taxed at the generating plant and at the distributing plant (at opposite ends of the process, so to speak) were different commodities of commerce from the electricity passing through the transmission lines (which was admittedly in interstate commerce), for in the latter case the electricity was in high voltage. In each instance the tax was imposed upon low voltage current. And the court cited as analogous the principle of "breaking the original package." The court said:

"Electricity is produced at a low voltage. For transmission over long distances it is 'stepped up' by a transformer to a very high voltage; and all of the current transmitted in interstate commerce is thus 'stepped up' before transmission in such commerce. Before it can be used by the consumer, it must be 'stepped down' again to a low voltage; and all of the current received by complainants in interstate commerce is thus stepped down before being sold to or used by the consumer. And this 'stepping up' or 'stepping down' is not a mere change produced in the current. . . . The principle of the transformer is that the current flowing in the wires coming into the transformer sets up an induced current . . . to flow in the wires going out of the trans-

\(^{16}\) 52 F. (2d) 515 (1931), affirmed without opinion in 286 U. S. 525 (1931). It was in this case that Millikan, the physicist, filed his elaborate affidavit in support of the view that the generation and transmission of electrical energy were essentially the same process—that they were instantaneous. See same case in 60 F. (2d) 528 (1932).
former; the voltage depending upon the relative number of the coils of the wires carrying the current in and those carrying the induced current out. These wires are insulated from each other, and the current going out is not the current coming in, but a new and different current, although induced by the former. . . . The current produced by induction in the transformer results from the use of the original current but is not that current, just as current produced by steam results from the use of coal but is not the coal.

"Now, so far as the production or generation tax on current is concerned, there can be no question as to its validity as applied to current transmitted in interstate commerce, we think, even though the current transmitted be conceived of as the identical current produced. The production of an article for transmission in interstate commerce is not in itself such commerce."

Generation and distribution taxes, measured by the amount of electricity generated or sold, thus are now clearly subject to state taxation, regardless of the interstate origin or distribution of the energy in question. For purposes of taxation, the courts have fashioned a fictitious concept of electricity. A legal fiction is not intrinsically bad, that is, it is not necessarily evil or useless merely because it has no basis in reality. In fact, the his-

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17 The courts have sensed a varying analogy between natural gas and electricity, and have frequently cited cases concerning the former kind of energy, in bearing upon problems concerning the latter, which may have some value in view of the relative scarcity of definite precedents in the field of electrical utility taxation.

In Hope Natural Gas Co. v. Hall, 274 U. S. 284 (1927), a state tax imposed on natural gas at the producing well was sustained, although a considerable portion of the gas so taxed was actually transported outside the state for consumption.

In East Ohio Gas Co. v. Tax Commission of Ohio, 283 U. S. 465 (1931), an excise tax imposed on corporations engaged in supplying natural gas to consumers within the state was sustained, although based on the gross receipts which included sales of gas piped in from other states. Analogous to the transformer, was found the pressure-reducing station through which the natural gas must pass before distribution. The "original package" doctrine was cited.

Note that while the court has thus sustained the taxation of both electricity and natural gas at the place of production, it has, on the other hand, held that the state has no regulatory power over the rates charged by local utilities for energy sold for use in another state and delivered at the state boundary, although admittedly the rates to local consumers might be adversely affected by the inadequacy of the former rates. See Public Utilities Commission v. Attleboro Steam & Electric Co., 273 U. S. 83 (1927).
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tory of the common law can be traced largely in terms of the rise and fall of fictions. So long as they perform some function which facilitates the accomplishment of objectives commanding general approval they are undoubtedly beneficial and necessary. But, when the attempt is made to extend their scope beyond the point of utility, they are no longer justified. To put it simply, legal concepts, or fictions, have only functional validity.\(^1\)

In respect to certain situations, the Supreme Court of the United States, observing the dangers of multiple taxation as applied to intangible personality, has forcefully rejected it and favored one taxing authority.\(^2\) Such restraints, however, in connection with interstate electrical utilities are not yet in appearance. In fact, it is just this mode of piecemeal construction and rectification by individual cases such as are here commented upon that has made the American tax structure into a virtual crazy-quilt. What is really the same kind of economic wealth (electrical energy) may now be taxed by at least three taxing authorities, the state of generation, the state of distribution, and the national government.

If the taxing authorities, in their constant search for revenue, proceed farther in the direction indicated, grave economic dangers may arise. Unless these authorities, from national government down to the smallest special district, arrange for some workable division among themselves of the tax income from the interstate electrical utilities, the business of transmitting power across state boundaries will be threatened with disintegration.

CLIFFORD J. HYNNING

WHEN COMPOUND INTEREST IS CHARGED AGAINST A TRUSTEE\(^1\)

In a late Connecticut case\(^2\) an administrator, authorized by the court to continue decedent’s business for six months, man-


\(^2\) State ex rel. Raskin v. Schachat et al., 180 A. 502 (Conn. 1935).
aged it for a much longer time without attempting to liquidate. He paid himself a salary, and utterly failed to keep intelligible accounts. In an action on his bond by his successor, the estate being insolvent, the court charged him with lost principal, and with compound interest thereon from the time when liquidation should have been completed. Following a custom prevailing in decisions upon the question whether simple or compound interest should be allowed against a defaulting trustee, the court cited but a few\(^3\) of the host of cases touching the subject, and refrained from theoretical explanation of its holding.

Investigation discloses ample authority consonant with this upon similar facts, and an irreconcilable conflict, both in theory and decision, on the general question of whether simple or compound interest should be charged. Several reasons appear. First, the matter is one which is left to the sound discretion of the court, a discretion which reacts differently to varying situations.\(^4\) Second, compound interest was a new remedy against trustees in the nineteenth century.\(^5\) Naturally its development could not be uniform in all jurisdictions. Third, a single fact, unimportant at first glance, may be the controlling element in a case. Thus, where the smallness of the fund might have precluded the trustee from keeping it at interest, the court may refuse to assess compound interest in an otherwise proper case.\(^6\)

Factual considerations have been decisive of most of the cases, and no principle capable of general application has yet been evolved. But so many decisions have passed upon the question that the factual grounds for allowing compound interest may be outlined.

The most common case is that in which the trustee uses trust funds for his own benefit, as in his own business. It is settled that the *cestui que trust* may elect to take the profits actually realized.\(^7\) But, as a prerequisite, the profits must appear. If the trustee has lost money, or has failed to keep accounts, no profits can be made to appear. Numerous decisions accord in allowing

\(^3\) Clement v. Brainard, 46 Conn. 174 (1878); Clement's Appeal from Probate, 49 Conn. 519 (1882); State v. Culhane, 78 Conn. 622, 63 A. 636 (1906); Mathews v. Sheehan, 76 Conn. 654, 57 A. 694 (1904).

\(^4\) Dixon v. Storm, 5 Redf. Sur. 419 (N. Y., 1881); Wright v. Wright, 2 McCord's Eq. 185 (S. C., 1827).

\(^5\) Re Ricker, 14 Mont. 153, 35 P. 960, 29 L. R. A. 622 and note (1893).


\(^7\) Windmuller v. Spirits Distributing Co., 83 N. J. Eq. 6, 90 A. 249 (1914).
the *cestui* compound interest under these circumstances. In one of these, in which the trustee, empowered to enforce security, foreclosed and bid in the property for himself, and later sold at a profit, the court remarked: "The rule seems to be, that in all cases where the trustee has used the trust fund, and the court can see from the evidence that the trustee has realized large gains and profits to himself, and has failed to keep any exact account of the same, or has refused to render an account to the beneficiary, the law will require him . . . to account for the original fund so used, with interest computed with annual rests."

This "rule" just quoted was perfectly adapted to the case before the court, but falls far short of the limits of the cases charging compound interest against a trustee who has used the funds of his trust with the aim of personal gain without accounting. It leaves out the cases where the trustee has actually lost money, and the decided cases indicate that this is no obstacle to awarding compound interest. It also omits cases wherein the trustee attempted, but failed, actually to use the fund. A leading case has held that a trustee who invested in "speculative" stocks, with the acquiescence of the beneficiaries, and then held the title in his own name, should be charged compound interest, though he clearly derived no pecuniary benefit from this breach. The improper investment alone was not enough to surcharge him; the taking of title was the decisive element, as it revealed his personal object. The only common factual ground for this group of decisions seems to be actual or attempted private gain. Other misdeeds seem only to add to the propriety of the remedy.

An offense closely similar to attempted use of trust funds by the trustee is mingling of funds with his own. Mingling alone,
without some other element, such as bad faith, does not justify a court in allowing compound interest. Thus, in a recent case, a corporate trustee which acted in good faith in allotting a mortgage already held in its own name, to a specific trust, without transferring title to itself "as trustee," was held liable to beneficiaries only for funds taken from the trust with simple interest.\(^1\) And in another case, an individual trustee who mingled trust funds with those of the corporation of which he was a member, was not surcharged because he took care to keep the fund invested, and made no attempt to benefit the firm.\(^2\) But in an Illinois case, an assignee for the benefit of creditors mingled trust money with his own, failed to keep accounts, and refused to pay a dividend to the plaintiff, a creditor. Since he could not show that he had not profited, the court presumed that he had, and charged him compound interest from the time the claim was payable.\(^3\)

In all these cases of mingling or attempted use, the familiar principle that a trustee shall not profit from his trust has been applied. And where the facts have been strong enough to impute to the trustee an intent, in handling trust funds, to consider his own interest at the expense of his trust obligation, compound interest usually has been assessed. But inconsistent results are reached because courts differ as to what facts warrant imputing such an intent to the trustee.

Another important group of decisions involves the failure to make proper investments. By far the great majority of these deny compound interest if the breach has been the making of unsafe or improper investments, or failure to invest at all.\(^4\) Such conduct has been called "simple neglect." To distinguish from this the action which they conceive to be ground for allowing compound interest, courts have used such discordant phrases as "gross negligence," "positive misconduct," "gross delinquency," and "willful violation or omission of duty." As no

\(^1\) In re Yost's Estate, 316 Pa. 463, 175 A. 383 (1934).
\(^2\) Cornet v. Cornet, 269 Mo. 298, 190 S. W. 333 (1916).
\(^3\) Asey v. Allen et al., 124 Ill. 391, 16 N. E. 865 (1888). But see Forbes v. Ware, 172 Mass. 306, 52 N. E. 447 (1899), where no bad faith was shown. Also see McDonald v. Hartford Trust Co., 104 Conn. 169, 132 A. 902 (1926); Brown v. Tydings, 149 Md. 22, 130 A. 337 (1925).
two courts would define these terms in the same way, no uniformity of decision can be expected, and none is found.

A New York court last year held that a trustee, who had only the normal trust duty to invest, and who loaned funds on an unsecured note which proved worthless, could have earned at least 4 per cent compounded had he invested in Liberty Bonds at the time he made the loan, and charged him at this rate. In a Wisconsin case, a trustee who renewed a second mortgage note on a farm, and ultimately lost the entire investment, was charged with only simple interest at the legal rate from the time his duty to convert accrued. But in a leading Illinois case an executor, directed by will to sell real estate and invest, and required to account, held the money without investing, and failed to account. The court charged him 6 per cent, compounded.

Failure to discharge a duty fixed by the trust instrument has been used as a basis for imposing compound interest, in contradistinction to failure to discharge certain general duties that are imposed on all trustees, where simple interest only is charged. Duties fixed by statute are placed on the same basis as duties fixed by the trust instrument. Thus non-compliance with the statutory requirements for investments by guardians and conservators has been a ground for surcharging them for unsuccessful investments.

"The principle of liability," one court has said, "is accountability for what has been received, or ought to have been received, or must be presumed to have been received, and not punishment for a breach of duty." But in an earlier opinion the United States Supreme Court remarked that "Interest is compounded as a punishment, or as a measure of damages for undisclosed profits and in place of them."

16 In re Ayvazian's Estate, 153 Misc. 467, 275 N. Y. S. 123 (1934).
17 Estate of Dreier, 204 Wis. 221, 235 N. W. 439 (1931).
18 Hough v. Harvey et al., 71 Ill. 72 (1873).
19 Emmet v. Emmet, 17 Ch. D. 142, 50 L. J. Ch. 341, 29 W. R. 464 (1881); Feltham v. Turner, 23 L. T. 345 (1870). The same result is reached where a court order imposes a duty to sell and invest: Winder v. Diffenderffer, 2 Bland 166 (Md., 1829); Crimp v. First Union Trust & Savings Bank, 352 Ill. 93, 185 N. E. 179 (1933).
20 People v. Birket, 342 Ill. 333, 174 N. E. 388 (1931); Hughes et al. v. People, 111 Ill. 457 (1885).
The principle upon which compound interest has been assessed undoubtedly is accountability for what has been, ought to have been, or must be presumed to have been received. But the courts award only simple interest where the trustee, by failing to invest properly, cannot account for what "ought to have been received." And they compound the interest against him where, again failing to invest, and to account for what "ought to have been received," he also shows bad faith by taking title in his own name.

Clearly, compound interest is not always charged where it ought to have been received. Nor is it always charged when it has been, or may be presumed to have been, received. It is safe only to say that it may be charged when one of these three alternatives exists.

The principle is accountability, but the measure of accountability depends on the degree of the trustee's offense. The object is not alone to restore to the beneficiary what he has lost. Obviously he loses equally by improper investments whether the trustee takes title to himself or not. Compound interest is not charged alone as the measure of damages flowing from the trustee's breach. Its propriety depends not wholly on the plaintiff's loss, but mainly on the defendant's act. Therefore, it is imposed, with few exceptions, as a penalty. The factual ground for it, common to the overwhelming majority of the cases, is the trustee's breach of his foremost duty of absolute fidelity to his trust.

C. E. Fox

AMENDMENTS TO ILLINOIS ATTACHMENT ACT

One of the more important modifications in the statute law of Illinois made in the last session of the legislature, of especial interest to the practicing attorney, is the rather thorough and complete revision of several phases of the Attachment Act.¹

The first modification is an enlargement of the action to cover tort as well as contract cases, and to cover unliquidated as well as liquidated claims.² The nine grounds which serve as a basis for attachment, however, remain unchanged.³ Attachment suits are extended so that they may be used in place of attachment in aid, which action is specifically repealed;⁴ yet it seems that this modification allows the same remedy under a different name.

¹ Ill. State Bar Stats. (1935), Ch. 11.
² Ibid., par. 1.
³ Ibid.
⁴ Ibid., par 31.
Having granted attachment in the case of tort or unliquidated claims, the legislature was faced with the problem of determining a manner in which to fix a bond. Paragraph 2 of the Act has been amended to accomplish this.\(^5\) In substance, it requires that the plaintiff shall apply to a judge of a court of record or a master in chancery, to have the usual affidavit as to the amount of damages indorsed by such officer, and section 4\(^6\) of the old Act is repealed and sections 4A\(^7\) and 4B\(^8\) supplied to take its place, which sections require a bond in double the sum sworn to be due;\(^9\) or the court or a judge thereof upon \textit{ex parte} motion, without notice, may authorize a bond in double the value of the property to be attached instead of double the sum sworn to be due.\(^10\)

The conditions of the bond required are substantially the same as before, with the provision that it shall run to all parties who may be interested, not only to the defendant named in the writ.\(^11\) Attachment against a joint debtor is as formerly.\(^12\) The general procedure under the Act is, insofar as is possible, brought under the Civil Practice Act.\(^13\)

A forthcoming bond in double the value of the property attached is permitted in the same manner as formerly.\(^14\) Other sections of the Act as to a suit on a bond, sustenance of live stock, disposal of perishable property, remain unchanged.\(^15\) The declaration is now a complaint and the Practice Act applies as far as expedient.\(^16\) Interveners may appear in much the same manner as formerly, except that here, too, the rules under the Practice Act control the procedure.\(^17\) A set-off is now termed a counterclaim.\(^18\) The paragraph in aid of \textit{scire facias} is specifically repealed.\(^19\) Despite the fact that attachment in aid is specifically repealed, the statute permits proceedings in aid and

\(^5\) Ibid., par. 2.

\(^6\) Cahill's Ill. Rev. Stat. (1933), Ch. 11, par. 4.

\(^7\) Ill. State Bar Stats. (1935), Ch. 11, par 4 (1).

\(^8\) Ibid., par. 4 (2).

\(^9\) Ibid., par 4 (1).

\(^10\) Ibid., par. 4 (2).

\(^11\) Ibid., par. 5.

\(^12\) Ibid., par. 7.

\(^13\) Ibid., par. 26.

\(^14\) Ibid., par. 14.

\(^15\) Ibid., par. 18, 19, 20.

\(^16\) Ibid., par. 25, 26.

\(^17\) Ibid., par. 29.

\(^18\) Ibid., par. 30.

\(^19\) Ibid., par. 32.
gives further weight to the argument that only the name in such proceedings is changed.\textsuperscript{20} Appeal is as in other civil cases.\textsuperscript{21}

The new and vital elements of proceedings in attachment are actions on tort or unliquidated claims, and the manner of fixing the amount of the bond.

It would seem from a reading of the statute, before judicial interpretation has been given, that all the rights and remedies which were open to litigants under the prior Act still exist, with provisions added to cover more types of causes.

\textbf{J. E. BRUNSWICK}

\textbf{VENUE FOR CONFESSION OF JUDGMENT—STATUTORY CHANGE}

At the last session, the Illinois legislature amended the Civil Practice Act\textsuperscript{1} in such manner as to require application for confession of judgment to be made "in the county in which the note or obligation was executed or in the county where one or more of the defendants reside."

The statute declares expressly the effect of failure to select the proper venue: "A judgment entered by any court in any county other than those herein specified shall have no force or validity, anything in the power to confess to the contrary notwithstanding."

This amendment, of course, represents a distinct change in the procedural law of Illinois, and while it is hardly susceptible of misunderstanding or needy of interpretation, it is considered worthy of brief mention, because of the commonness of the proceeding and the possibility that in reliance upon settled custom it may be inadvertently overlooked if special attention is not directed to it.

\textbf{G. S. STANSELL}

\textsuperscript{20} Ibid., par. 33.
\textsuperscript{21} Ibid., par. 40.
\textsuperscript{1} Smith-Hurd's Ill. Rev. Stat. (1935), Ch. 110, par. 174.