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Taxation - Income Under Oklahoma Community Property Law

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Notes

TAXATION—INCOME UNDER OKLAHOMA COMMUNITY PROPERTY LAW—As the Review goes to press it seems desirable to call attention to the case of *Commissioner of Internal Revenue v. Harmon*[1] even though time and space preclude an extended discussion of this important decision. The facts may be summarized as follows: In July 1939 the state of Oklahoma adopted a community property law which was of a permissive nature. One C. C. Harmon and his wife filed their written election to come under its provisions, and in 1939 submitted their separate income tax returns wherein each reported one-half of the November and December income received by both as community income under the act. The Commissioner of Internal Revenue ruled that the husband was taxable on all the income received by him, and was not liable on any of the income received from his wife's separate property. The Tax Court and the Circuit Court of Appeals reversed this ruling, and decided that the spouses were right in filing separate returns for one-half of the joint income, relying upon the position adopted by the federal courts in *Poe v. Seaborn*.[2] The Supreme Court, however, reinstated the holding of the commissioner under the case of *Lucas v. Earl*.[3] It grounded its decision on the optional feature of the Oklahoma community property act, indicating that the "legislative permission" was a mere variation and added nothing to this "consensual contract" of the parties in their own regulation of their rights in income and hence fell under the bann of the *Lucas* case. The majority opinion, delivered by Mr. Justice Roberts, recognized a definite distinction between Oklahoma's permissive system and a legal system "dictated by state policy as an incident of matrimony."[4] The fact was stressed that those states which had long had the legal community were in an entirely different category.

The very old controversy of "the nature of the wife's interest" in the community was touched upon but lightly as a matter

1. 65 S. Ct. 103 (U. S. 1944).
2. 282 U. S. 101, 51 S. Ct. 58, 75 L.Ed. 239 (1930).
3. 281 U. S. 111, 50 S.Ct. 241, 74 L.Ed. 731 (1930).
4. Commissioner of Internal Revenue v. Harmon, 65 S.Ct. 103, 105 (U. S. 1944).

settled by the states themselves. It was stated that the California Act of 1927[5] was but a legislative declaration of this controversial question which still left California in an entirely different class from Oklahoma with the latter's *permissive statute,* even though the California Supreme Court and the legislature of California had previously indicated that the wife had but an expectancy and not a vested interest in community during the life of that entity. No mention whatever was made of tax evasion or saving by legislative process, nor is there any suggestion as to what the rule might be should Oklahoma or any other state[6] or states adopt community as its *legal* system, whatever their motive. This decision is most heartening to citizens of community property states where the legal community has been the "inveterate policy of the State." The court pointed out that Congress had full knowledge of the tax variations caused by the differences in the settled policies of the various states, that it had been asked to revise the revenue act to change the "incidents of the tax" and had refused.

Satisfaction flows from the majority opinion to those who have long believed in the community property system as a family binder founded on sound principles of justice and fair dealing between spouses long before income taxes were a matter of apparently paramount concern. Legislative juggling with the system solely for tax reasons has been frowned upon by many thoughtful persons. While the majority opinion in no wise purports to act as a brake upon such legislation it may be a deterrent because of the stress on "inveterate policies."

This satisfaction is marred somewhat by the vigorous dissent of Mr. Justice Douglas who already has one concurrer in the person of Mr. Justice Black. Mr. Justice Douglas seems to be concerned solely with loss to the United States Treasury, and with "unjustifiable discrimination against the residents of non-community property states." His position is that marriage or change of domicile is also a consensual act and hence that the distinction made by the majority is one without a difference. He feels that the vested interest theory of the wife in the husband's earnings is the distinguishing feature if any of Oklahoma's law together with that of other community property states. He apparently does not like any part of the community property idea, particularly the notion of a wife having a property interest in the *husband's* earnings. It might be said, in passing, that the

5. Calif. joint resolution 17; Calif. Stats. of 1927, c. 68.
6. Oregon Laws of 1943, c. 440.

theory may also apply as to the wife's earnings which under present social and economic conditions are considerable.

Mr. Justice Douglas seems to read the majority opinion as resting upon the "new born" versus the "traditional" community property idea of those states who adopted it long before tax controversies arose rather than upon the "legal" versus the "optional" idea of Oklahoma. Mr. Justice Douglas makes it quite clear that his dissent is not in defense of the vested interest distinction made in previous cases but in the interest of uniformity. His thought seems to be not that we should leave to Congress the task of finding a new incident of taxation but that the court should look after federal finance by simply overruling *Poe v. Seaborn.*[7] He uses the phrase "disastrous to federal finance." The loss in ease to tax leviers and collectors for achievement of uniformity and efficiency is a small price to pay for the satisfaction of the thus far willing tax-paying citizenry by preservation of bona fide distinctions between theories regarding property in which the states believe. Certainly the fine minds and demonstrated ingenuity of our tax leviers can be depended upon to find a taxable incident which will prevent "disaster" and yet preserve property distinctions which mean much in keeping the faith and which are not "elusive and subtle casuistries" to those who happen to like their particular property systems which, moreover, they can change themselves if they care to.

Doubtless every citizen in a disgruntled mood has at some time either orally or in writing put the word law in quotes. Nevertheless, from the pen of a justice of the Supreme Court of the United States it is disturbing,[8] as is the statement that "the formula for some states . . . should be the formula for all."[9] Every tax formula is traditionally bitter. If minor variations founded upon bona fide distinctions are made in deference to the palates of the several states a cure can be obtained with much greater cheerfulness from the patient who must swallow the dose. The old fable of the wolf and the lamb recites that the wolf complained to the lamb that the latter was muddying the water of the stream from which they both were drinking. The lamb pointed out that he was below the wolf and hence could not be disturbing the water running by the wolf. Whereupon, the wolf stated that

7. 282 U. S. 101, 51 S.Ct. 58, 75 L.Ed. 239 (1930).

8. See, for example, the statements in Commissioner of Internal Revenue v. Harmon, 65 S.Ct. 103, 105 (U. S. 1944).

9. 65 S.Ct. 103, 107.

he would eat the lamb anyhow. However badly the treasury may need meat it is the hope of the writer that the bona fide property distinctions of the states will continue to be recognized as they are in the majority opinion of the case under discussion and that more tax money, if needed, will be raised by other methods than by overruling a line of decisions which were considered in the light of the community property system as such and not as a foregone conclusion which would bring more money into the treasury.

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COMMUNITY PROPERTY—COST OF ADMINISTRATION—The surviving spouse of Vaccaro became, at his death, the full owner of one-half of the community property. Vaccaro's estate was settled, but there were considerable charges upon the estate: attorneys' fees, executrix's commission, and other costs of administration. These amounted to more than seventy-three thousand dollars. Plaintiff, the surviving spouse, attempted to deduct these charges from her husband's gross estate under Section 303, Revenue Act of 1926, as amended. The commissioner refused, and allowed only the deduction of one-half of the charges, asserting that one-half of such expenses were incurred in the administration of the widow's one-half of the community estate. *Held,* the entire amount is deductible from the decedent's gross estate because, since the community terminated at the death of the husband, it was no longer capable of being charged with expenses and no part should be charged to the half of the community owned by the surviving spouse. *Vaccaro v. United States,* 4 Prentice-Hall 1944 Fed. Tax Serv. ¶ 62,646, C.C.H. Fed. Estate and Inheritance Tax Serv. ¶ 10,129 (E.D. La. 1944).

This decision is based largely upon a ruling by Justice Odom in *Succession of Lewis*[1] to the effect that "all costs of the administration should be paid out of the estate of the deceased, and that the community was not liable for any portion thereof."[2] In support of his ruling, Justice Odom cites *Succession of Solis*[3] and *Succession of Pizatti.*[4] These cases, however, are authority only

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1. 192 La. 734, 189 So. 118 (1939).
2. 192 La. 734, 743, 189 So. 118, 121 (1939).
3. 10 La. App. 109, 119 So. 768 (1929).
4. 141 La. 645, 75 So. 498 (1917).