1960

Taxation

Joseph Curtis

TAXATION

*Joseph Curtis**

JUDICIAL DECISIONS

The only tax case decided by the Supreme Court of Appeals of Virginia during the period covered by this Survey involved the troublesome federal tax lien[1] and the frequently litigated issue of its priority. The lien arises and

48. Johnson v. Nationwide Mut. Ins. Co., 276 F.2d 574, 577 (4th Cir. 1960).

49. 6 APPLEMAN, INSURANCE LAW AND PRACTICE § 4185 (1942); 6 COUCH, CYCLOPEDIA OF INSURANCE LAW § 1442 (1930).

50. See, *e.g.*, McMillan v. Farm Bureau Mut. Auto. Ins. Co., 282 App. Div. 1091, 126 N.Y.S.2d 436 (1953).

51. 276 F.2d 132 (4th Cir. 1960).

52. Oral assignments are valid in Virginia. Hughes v. Burwell, 113 Va. 598, 75 S.E. 230 (1912).

*Professor of Law, William and Mary. Member, New York and Virginia Bars. B.S., 1934, LL.B., 1937, LL.M., 1948, New York University.

1. See INT. REV. CODE OF 1954, § 6321.

becomes fixed upon assessment of the tax[2] as to all but bona fide purchasers, mortgagees, pledgees and judgment creditors whose priority rights are measured with reference to the time the tax lien is recorded[3] and not to the time the tax is assessed.

Solely as a proposition of Virginia law the landlord's lien for rents arises upon commencement of the tenancy;[4] the lien is specific and perfected independently of the right to proceed by distress warrant or attachment.[5] In *United States v. Lawler*[6] a tenancy was commenced seven years prior to federal income tax assessments made against the tenant, but notice of the federal tax lien was docketed prior to the landlord's bringing an action to enforce his statutory lien for unpaid rents. The trial court, in finding for the landlord, applied the common law rule of "first in time—first in right" on the theory that the federal statutes creating and defining the tax lien[7] did not assert its priority and the federal statute establishing priority of United States claims to the assets of insolvent debtors[8] was inapplicable. Following the reasoning of *United States v. Waddill, Holland & Flinn, Inc.*,[9] the Supreme Court of Appeals reversed. The Court held it to be a federal question as to whether a landlord's lien is perfected prior in time to a federal tax lien and thus, the Virginia statute, while controlling as to matters of state law, must yield on the federal issue to federal precedent. In *Waddill, Holland & Flinn, Inc.*, the United States Supreme Court had held that the Virginia landlord's lien, until actually enforced by levy, was merely a caveat of a more perfect lien to come and thus junior in time to a federal claim. Since landlord Lawler's distress warrant, writ of attachment, and execution sale followed the federal assessment, the tax lien was held by the Court to be first in time.

Legislation

While tax matters occupied little of the time of the Supreme Court of Appeals, the legislature was somewhat more active in the field. The following notations do not purport to cover all of the innumerable rewrit-

2. Int. Rev. Code of 1954, § 6322.

3. Int. Rev. Code of 1954, § 6323.

4. See Va. Code Ann. §§ 55-227, -231, -233 (Repl. Vol. 1959).

5. United States v. Waddill, Holland & Flinn, Inc., 323 U.S. 353, 356 (1945) (dictum), *reversing* 182 Va. 351, 28 S.E.2d 741 (1944). The United States Supreme Court held that the priority of a federal lien over a landlord's lien was a federal question and state law was not binding on the issue of when the landlord's lien becomes perfected.

6. 201 Va. 686, 112 S.E.2d 921 (1960).

7. Int. Rev. Code of 1954, §§ 6321-23.

8. 31 U.S.C. § 191 (1958).

9. 323 U.S. 353 (1945).

ings, revisions and substantive changes made by the General Assembly in the 1960 Regular Session. They are intended to bring to attention some of the amendments and additions to the tax laws of most general interest.

A. *Income Tax*

1. *Individuals*

The maximum medical expense deduction was increased to fifteen thousand dollars for each disabled spouse who has attained age sixty-five.[10] These maximums and the specific requirements to qualify for them conform with the 1958 amendment to section 213 of the Internal Revenue Code of 1954.[11]

A nonresident beneficiary of an estate or trust will be taxed on his distributive share of the estate or trust income only to the extent that such income is derived from real estate or tangible personal property located in Virginia, or from the operation of an unincorporated business or trade carried on in this state.[12] However, this provision is not applicable to income accumulation trusts, discretionary distribution trusts, or non-distributing estates where in each case the tax is imposed upon the trust or estate and not upon the beneficiary.[13]

2. *Corporations*

The most significant change in the tax law made in the 1960 session is that of the adoption of a new allocation formula for determining what part of the net income of a corporation doing business both within and without the state shall be taxed by this state. Effective for taxable years commencing after December 31, 1961, the determination shall be made by an allocation by source for rents, royalties, capital gains, interest and dividend income, coupled with a three-factor formula of property, payroll, and sales applicable to all other classes of income.[14] This will supplant the present alternatives of the nebulous separate accounting[15] and the inadequate two-factor formula of property and gross receipts.[16]

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10. VA. CODE ANN. § 58-81(p)(3) (Supp. 1960).

11. INT. REV. CODE OF 1954, § 213(g).

12. VA. CODE ANN. § 58-121 (Supp. 1960).

13. VA. CODE ANN. § 58-120 (Repl. Vol. 1959); see VA. CODE ANN. § 58-118 (Repl. Vol. 1959).

14. See VA. CODE ANN. §§ 58-131.1 to .18 (Supp. 1960).

15. VA. CODE ANN. § 58-132 (Repl. Vol. 1959).

16. VA. CODE ANN. § 58-131.1 (Repl. Vol. 1959). The formulae are discussed in more detail in Hirshberg & Nadry, *A Federal Concept of Doing Business*, 46 VA. L. REV. 1241, 1247-48 (1960).

B. *Intangible Personal Property Tax*

Commencing in 1963 the capital of a trade or business not otherwise specifically taxed will be taxed at sixty-five instead of seventy-five cents per one hundred dollars worth,[17] and henceforth such capital subject to tax will not include the value of life insurance policies owned by the business.[18]

C. *Excise Taxes*

Increase of the motor fuel tax by one cent per gallon[19] and enactment of the sales and use taxes on tobacco products[20] are now well-known to all—at least to all who drive cars or smoke.

D. *Estate and Gift Taxes*

Noteworthy in this field is what the General Assembly declined to enact. The proposal to eliminate the gift tax and to replace the present inheritance tax by an estate tax, designed to conform substantially with that of the federal tax, failed to pass.

WILLS, TRUSTS AND ESTATES

*Ellsworth Wiltshire**

LEGISLATION

One important enactment of the General Assembly of 1960 relates to the transfer of securities. The Uniform Act for Simplification of Fiduciary Security Transfers[1] appears with only three changes.[2] The act, among other things, severely limits the duty to inquire and the concepts of "knowledge" and "notice" as applied to the issuing corporation and its

17. See VA. CODE ANN. § 58-418 (Supp. 1960).

18. VA. CODE ANN. § 58-411(4) (Supp. 1960).

19. VA. CODE ANN. § 58-711 (Supp. 1960).

20. See VA. CODE ANN. §§ 58-757.1 to .27 (Supp. 1960).

* Professor of Law, University of Richmond. Member, Virginia Bar. B.A., 1919, LL.B., 1922, University of Virginia; S.J.D., 1923, Harvard University.

1. Approved by the National Conference of Commissioners on Uniform State Laws. 9C UNIFORM LAWS ANN. 43-51 (Supp. 1959). The act is discussed in further detail in Gibson & Freeman, *Business Associations, 1959-1960 Ann. Survey of Va. Law*, 46 VA. L. REV. 1481 (1960).

2. VA. CODE ANN. §§ 13.1-424 to -433 (Supp. 1960). The changes are: (1) the inclusion of registrar in the definition of transfer agent; (2) the omission of tutor from the definition of fiduciary; (3) and the omission of § 9 as inapplicable under Virginia law.

transfer agent,[3] renders unnecessary much of the burdensome documentation which transfer agents have required, provides a simple method of resolving claims adverse to the transfer of a security by a fiduciary,[4] and limits liability of third persons participating in the acquisition, disposition, assignment, or transfer of a security by or to a fiduciary.[5]

The administration of small estates is greatly simplified by two enactments. One eliminates the appointment of appraisers if the decedent's estate does not exceed one thousand dollars.[6] The other permits a personal representative, in lieu of a settlement of his accounts, to file with the commissioner of accounts a statement under oath that he has paid all known charges against the estate and delivered the residue to himself, if he is the sole distributee or the sole beneficiary under the decedent's will, or if he is the residuary beneficiary under such will and his statement is accompanied by vouchers of satisfaction of all other bequests in the will.[7]

The danger resulting from a testator's failure to mention after-born children in his will is removed to a considerable extent by an amendment providing that a pretermitted child shall not share in the estate of a testator, if such testator has a child or children living when the will is made and such living child or children be not provided for by the will or by any settlement.[8] Apparently the statute operates on the theory that if a testator cuts out all children living when his will is executed, he would desire to eliminate likewise all after-born children.

Section 26-17,[9] providing for the annual settlement of fiduciaries' accounts, has been amended to substitute "testamentary trustee, trustee under § 37-141,[10] and receiver under § 55-44[11]" for "trustee acting under a trust created by any recorded instrument except those named in § 26-15.[12]" Hence, now no trustee under an inter vivos trust is required to make an annual settlement of his accounts, even though the trust instrument is recorded.

Section 26-40(23)[13] has been amended so that it no longer requires a

3. See VA. CODE ANN. §§ 13.1-426 to -428 (Supp. 1960).
4. See VA. CODE ANN. § 13.1-429 (Supp. 1960).
5. See VA. CODE ANN. § 13.1-431(a) (Supp. 1960).
6. VA. CODE ANN. § 64-126 (Supp. 1960).
7. VA. CODE ANN. § 26-20.1 (Supp. 1960).
8. VA. CODE ANN. § 64-70 (Supp. 1960).
9. VA. CODE ANN. § 26-17 (Supp. 1960).
10. VA. CODE ANN. § 37-141 (Supp. 1960) (trustees for incompetent ex-service persons and their beneficiaries).
11. VA. CODE ANN. § 55-44 (Repl. Vol. 1959) (receiver for a married woman who is a minor).
12. VA. CODE ANN. § 26-15 (1950). This section relates to accounts of sales made under any recorded deed of trust, mortgage, or assignment for benefit of creditors.
13. VA. CODE ANN. § 26-40(23) (Supp. 1960).

minor's guardian to obtain court approval to keep its ward's funds invested in certificates of deposit or in savings accounts for longer than six months.

For a deed by a foreign executor conveying land in Virginia under a testamentary power to the effective, an amendment to section 64-140[14] requires that it be signed and acknowledged by an ancillary administrator duly appointed and qualified in Virginia.

JUDICIAL DECISIONS

A. *Wills*

Other than the case first mentioned below, the few decisions involving wills decided by the Supreme Court of Appeals present no unusual principles or facts.

1. *Revocation*

The most controversial and the most important case involving wills is *Timberlake v. State-Planters Bank.*[15] There the testatrix executed a will in 1954 and another will in 1955. The 1955 will expressly revoked all prior wills. She deposited both wills in executor bank for safekeeping. Later, she withdrew the 1955 will stating she intended to make a new will with changes. At her death, the 1955 will could not be found and was presumed destroyed by her. When the 1954 will was offered for probate, the decedent's heirs at law contended that it was revoked by the 1955 will and that she accordingly had died intestate. The Supreme Court of Appeals held that the 1954 will was not revoked by the 1955 will and should be admitted to probate. The majority opinion was written by Justice Buchanan. Justice Spratley wrote a vigorous dissenting opinion concurred in by Justice I'Anson.[16]

The majority opinion took the position that, when a will contains a clause revoking earlier wills, this clause as well as the rest of the will becomes operative only upon and by reason of the testator's death and that, if the testator destroys or cancels this will with intent to revoke it, the revoking clause never becomes effective and hence does not operate to revoke prior testamentary papers.

The Court refused to follow *Rudisill's Ex'r v. Rodes,*[17] which held exactly to the contrary, on the grounds that (1) the *Rudisill* case failed to cite

14. VA. CODE ANN. § 64-140 (Supp. 1960).

15. 201 Va. 950, 115 S.E.2d 39 (1960).

16. For a discussion of the position taken by the dissenting opinion see Barnett, *Revocation and Revival of Wills in Virginia,* 1 U. RICH. L. NOTES 147 (1960).

17. 70 Va. (29 Gratt.) 147 (1877).

Barksdale v. Barksdale;[18] and (2) the *Rudisill* case seems to have assumed or conceded that the second will with a clause revoking earlier wills operated upon its execution to revoke an earlier will and devoted its attention solely to whether the destruction of the second will revived the earlier revoked will. However, the *Rudisill* case appears clearly to be a direct holding that the second will upon its execution revoked the earlier will, for otherwise there would have been no reason for the Court to consider whether the earlier will was revived upon the revocation of the later will.

The doctrine of the *Rudisill* case was limited but not overruled by *Poindexter v. Jones*[19] decided in 1958 and holding that an earlier holographic will was not revoked by a later holographic will which contained no express clause of revocation but which was entirely inconsistent with the terms of the earlier will, when the testator cancelled the later wills with intent to revoke by tearing off her signature.

The law now appears settled in Virginia that a will is not operative or effective for any purpose while the testator is alive and, if a will is revoked prior to death, it cannot prevent the probate of an earlier will, whether it expressly revokes the earlier will or its dispositive provisions are entirely inconsistent with the earlier will.[20]

2. *Oral Agreement To Will*

Patton v. Patton[21] involved specific performance of a parol agreement to devise realty. A father orally agreed to devise his interest in certain realty to two of his children in return for their paying off encumbrances on his property and caring for his wife and himself during their lives. He executed a will devising the realty to them, and the children performed their part of the agreement. After his wife's death, the father remarried, was divorced, and later died. The Court held that, as the will was revoked by the later marriage,[22] he died intestate. However, it found that the parol agreement was certain and definite, the contributions and services of the two children grew out of, referred to, and were given and rendered in pursuance of the agreement, the parol agreement was so far executed by

18. 39 Va. (12 Leigh) 535 (1842). The *Barksdale* case appears to hold merely that an instrument intended as a will but attested to by only one witness when two were required did not revoke an earlier will, although the instrument was sufficiently executed to operate as a revoking instrument under the then existing statute.

19. 200 Va. 372, 106 S.E.2d 144 (1958).

20. See Note, *Revocation of Wills by Subsequent Instrument*, 46 VA. L. REV. 373 (1960).

21. 201 Va. 705, 112 S.E.2d 849 (1960).

22. VA. CODE ANN. § 64-58 (1950), was repealed by Va. Acts 1956, ch. 65.

them that a refusal to grant specific performance would operate as a fraud on them, and specific performance should accordingly be decreed.[23]

3. *Estate Created*

Since *May v. Joynes*,[24] the Supreme Court of Appeals has consistently held that where a person is willed property with absolute dominion over it but with a gift over to another of any portion left at the death of such person, a fee simple in real estate and an absolute estate in personalty passes to the first taker and the one who is to take what is left on the death of the first taker receives nothing. This doctrine is followed in *Gardner v. Worrell*,[25] which presents no unusual facts.

4. *Executor's Commissions and Liability for Interest*

Bickers v. Shenandoah V. Nat'l Bank[26] considers the proper commissions of an executor and the executor's liability to pay interest on distributions made after the one year statutory period.[27] Bickers created a life insurance trust agreement prior to his death. After his death, his widow prevailed in her suit to have the insurance trust agreement declared void as testamentary in character.[28] Thereupon the insurance proceeds were delivered by the trustee to itself as the testator's executor. In exceptions to the executor's account, the widow, who had renounced the will, claimed the executor was not entitled to the five per cent commission taken by it upon the one-third of the insurance proceeds distributable to her. She also contended that the executor should be charged with interest on all commissions taken by it before final distribution and also with interest on her distributive share in realty proceeds and in personalty from one year after its qualification until the distributions were made to her. The Supreme Court of Appeals held that (1) the chancellor acted within his reasonable discretion in allowing the commission on the insurance proceeds; (2) his decision that the executor had earned the commissions when taken and had acted in good faith was within his discretion and should not be disturbed; and (3) his holding that the executor should not be charged with interest because of the delay in making distributions must be presumed correct and

23. These requisites were prescribed in Wright v. Pucket, 63 Va. (22 Gratt.) 370 (1872).

24. 61 Va. (20 Gratt.) 692 (1871).

25. 201 Va. 355, 111 S.E.2d 285 (1959).

26. 201 Va. 257, 110 S.E.2d 514 (1959).

27. VA. CODE ANN. § 64-68 (1950).

28. Bickers v. Shenandoah V. Nat'l Bank, 197 Va. 145, 88 S.E.2d 889 (1955).

binding as the evidence in that regard was taken *ore tenus* and was not before the Court for consideration.

B. *Trusts*

1. *Irrevocable Inter Vivos Trust—Unhappy Widow*

In *Freed v. Judith Realty & Farm Prods. Corp.*,[29] a widow contended that an inter vivos trust created by her husband was in fraud of her marital rights and that it was illusory because there was no separation of the legal and equitable titles. The husband executed a trust agreement as to the majority of the shares of a corporation with that corporation as trustee, under which he was to be paid $1,500 annually during his lifetime from the dividends and, if the dividends were inadequate, from the proceeds of sale of sufficient shares of the stock to make up the difference. He reserved the sole right to vote the stock until his death. The corporation trustee in turn agreed to purchase sufficient stock of the trust to enable the $1,500 to be paid annually to him. At his death, the stock remaining in the trust was to become the treasury stock of the corporation.

The Supreme Court of Appeals held this was a valid irrevocable inter vivos trust for valuable consideration, in which the corporation was remainderman beneficiary and which was not testamentary and was not rendered invalid because it was created by the husband to prevent his wife from obtaining any part of the stock at his death. This case is in line with the earlier Virginia cases[30] giving to a married man the unqualified privilege of disposing of his personalty during his lifetime free of his wife's marital rights provided he has so dispossessed himself thereof as to put it beyond his power to reclaim it.

2. *Trustee's Right to Accounting From Agent*

The owners of a number of farms and a merchantile store employed Pulley to operate the properties as their agent. Later they transferred these properties to trustees to manage for them. Thereafter Pulley rendered to the trustees and the beneficiaries annually a list of items of income and disbursement for each preceding year, which items were not checked with the records by the preparing accountant, the trustees, or the beneficiaries. Upon a later audit had by the trustees, large discrepancies by Pulley were revealed. The trustees file suit against Pulley for an accounting and for judgment as to any deficiency. The Supreme Court of Appeals,

29. 201 Va. 791, 113 S.E.2d 850 (1960).

30. See, *e.g.*, Gentry v. Bailey, 47 Va. (6 Gratt.) 594 (1850); Lightfoot's Ex'rs v. Colgin, 19 Va. (5 Munf.) 42 (1813).

in *Bain v. Pulley*,[31] held that the trustees were entitled to an accounting because the annual lists of income and disbursement did not constitute settlements of Pulley's accounts, acquiescence in the method of bookkeeping, and conducting the work did not constitute an estoppel, and the trustees were not guilty of laches.

31. 201 Va. 398, 111 S.E.2d 287 (1959).