The Impact on the Marital Deduction of Expenses Chargeable to Post-Mortem Income: Does United States v. Stapf Answer the Question?

Martha W. Jordan, Duquesne University School of Law
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Martha W. Jordan
Associate Professor of Law

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THE IMPACT ON THE MARITAL DEDUCTION OF EXPENSES CHARGEABLE TO POST-MORTEM INCOME: DOES UNITED STATES V. STAPF ANSWER THE QUESTION?

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I. INTRODUCTION

During the 1996-97 term, the Supreme Court is scheduled to hear Estate of Hubert v. Commissioner, which concerns issues of extreme importance to estate tax practitioners. The Court granted certiorari in Hubert to resolve a split of authority among the circuits regarding whether administration expenses allocable to post mortem income reduce the marital deduction. Since the tax court first adopted the pro-taxpayer position endorsed by the Eleventh Circuit in Hubert, commentators have been analyzing, supporting and justifying the tax court's position. This article uses the Court's reasoning in United States v. Stapf to predict the Court's resolution of the issues raised in Hubert.

One of the issues raised in Hubert is whether administrative expenses charged to post mortem income reduce the marital deduction. Although a

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* Associate Professor of Law, Duquesne Law School.
4. Hubert also holds that administration expenses chargeable to income do not affect the charitable deduction. Estate of Hubert, 63 F.3d at 1090. This holding conflicts with Burke v. United States, which, relying on Estate of Street, held that administration expenses chargeable to estate income reduce the value of the charitable deduction. Burke v. United States, 994 F.2d 1576 (Fed. Cir. 1993), cert. denied, 114 S. Ct. 546 (1993). The Supreme Court will consider the impact of administration expenses on both the marital deduction and the charitable deduction; however, since section 2055, which provides for the charitable deduction does not contain a provision analogous to section 2055(b)(4)(B), consideration of the impact on the charitable deduction raises issues outside the scope of this article.
decedent's estate is allowed an unlimited marital deduction, section 2056(b)(4)(B) requires that the value of the marital deduction take into account the effect of any obligation that the decedent requires the surviving spouse to incur. In the context of the facts posed in Hubert, the issue is whether administration expenses charged to income earned by the marital share during administration of the estate constitute such an obligation and, therefore, reduce the marital deduction. The Court of Appeals for the Eleventh Circuit held in Estate of Hubert v. Commissioner that administration expenses allocated to post mortem income do not affect the marital deduction if state law allows allocation between income and principal. Hubert contradicts the prior holding of the Court of Appeals for the Sixth Circuit in Estate of Street v. Commissioner that administration expenses reduce the marital deduction regardless of whether the expenses are charged to principal or income. The courts and the Internal Revenue Service agree, however, that interest expense, if allocated to post mortem income, does not reduce the marital deduction.

In United States v. Stapf, the Supreme Court interpreted sections 812(e)(1)(A) and 812(e)(1)(E)(ii) of the Internal Revenue Code of 1939, the predecessors to section 2056(b)(4)(B). Notwithstanding this fact, none of the courts that have addressed the issues raised in Hubert considered the reasoning adopted in United States v. Stapf in their analysis.

5. I.R.C. § 2056(a) of 1986, as amended. The amount of the marital deduction equals the value of all property interests passing to the surviving spouse. All references and citations to sections in this article are to sections of the Internal Revenue Code of 1986, (the "Code") as amended to date of publication, unless otherwise indicated.
9. For purposes of this article the term “interest expense” refers to interest payable either with respect to deferred federal or state estate or inheritance taxes or with respect to federal or state estate or inheritance tax deficiencies.
10. Estate of Street v. Commissioner, 974 F.2d 723 (6th Cir. 1992); Estate of Whittle v. Commissioner, 994 F.2d 379 (7th Cir. 1993); Estate of Richardson v. Commissioner, 89 T.C. 1193 (1987); Rev. Rul. 93-48, 1993-2 C.B. 270. Because the Internal Revenue Service acquiesced with respect to the impact of interest expense chargeable to estate income on the marital deduction prior to the tax court's consideration of Hubert, consideration of that issue is not before the Court.
12. The Court of Appeals for the Sixth Circuit cited United States v. Stapf as standing for the proposition that "the marital deduction is limited to the value of the property that is actually received by the surviving spouse, or the "net benefit" received by the spouse . . . ." Estate of Street
This article will suggest how the interpretation advanced in *United States v. Stapf* will affect the Court's decision in *Hubert*. This article will also examine the Internal Revenue Service's current position regarding interest expense in light of the Court's reasoning in *United States v. Stapf*.

Based on the interpretation of sections 812(e)(1)(A) and 812(e)(1)(E)(ii) adopted by the Supreme Court in *United States v. Stapf*, the conclusion of this article is that administration expenses allocable to post mortem income reduce the net economic benefit to the surviving spouse and, therefore, also reduce the amount of the marital deduction. In addition, this article concludes, based on the principles adopted in *United States v. Stapf*, that the current position regarding the impact on the marital deduction of interest expense chargeable to estate income is incorrect; interest expense allocated to estate income also reduces the marital deduction.

II. OVERVIEW OF APPLICABLE TAX PROVISIONS

An estate is potentially liable for both estate tax and income tax. Certain expenses incurred during the administration of an estate qualify as deductible expense for purposes of both the estate tax and the income tax. Because the same expense cannot be deducted twice, once to calculate the taxable estate and a second time to determine the estate's taxable income, the executor must decide where the deduction will be most beneficial and deduct the expense accordingly.

A. Estate Tax

The estate tax is an excise tax imposed on the privilege of transferring property at death. The tax base for imposition of the estate tax is the taxable estate, which the Code defines as the gross estate less allowable deductions. The gross estate equals the fair market value, determined as of the date of the decedent's death, of all property to the extent that the decedent had an interest.
in such property at death.\textsuperscript{18} Income earned after the decedent’s death is not included in the gross estate.

Several deductions are allowed in computing the taxable estate. Section 2053 provides for the deduction of administration expenses, funeral expenses, the decedent’s debts, and claims against the decedent’s estate.\textsuperscript{19} Section 2054 allows a deduction for casualty losses sustained during the administration of decedent’s estate.\textsuperscript{20} Section 2055 allows a deduction for the value of property devised or bequeathed to charity.\textsuperscript{21} And, section 2056 provides for the marital deduction.\textsuperscript{22}

The Code allows an unlimited marital deduction for the value of all property interests included in a decedent’s gross estate and passing to the decedent’s surviving spouse, provided such property interests do not violate the terminable interest rule.\textsuperscript{23} The terminable interest rule prohibits a property interest from qualifying for the marital deduction, if (1) the spouse’s interest may terminate; (2) after termination of the spouse’s interest, the property will pass to someone other than the spouse; and (3) such other person’s interest was received from the decedent “for less than full and adequate consideration in money or money’s worth.”\textsuperscript{24} The terminable interest rule limits the availability of the marital deduction to those property interests passing to the surviving

\textsuperscript{18} I.R.C. §§ 2031, 2033 (1986). In certain instances the gross estate includes the value of property even though the decedent did not possess an interest in the property at death. I.R.C. § 2036(a) (1986) (including in the decedent’s gross estate the date-of-death value of property transferred by the decedent during life for less than full and adequate consideration if the decedent retains a life estate), or even though the decedent never had an interest in the property, id. § 2041 (including in the decedent’s gross estate the value of all property over which the decedent possesses a general power of appointment at death).

\textsuperscript{19} I.R.C. § 2053(a) (1986). Administration expenses are those expenses necessary to “the settlement of an estate and the transfer of the property of the estate to individual beneficiaries.” Treas. Reg. § 20.2053-3(a). Expenses necessary to the settlement of a decedent’s estate are expenses incurred to collect the decedent’s property, to pay the decedent’s debts, and to transfer the decedent’s property to the heirs or devisees. Id. Expenses incurred in the settlement of the decedent’s estate that do not relate to the collection and transfer of the decedent’s property or the payment of the decedent’s debts are not deductible as administration expenses, even though state law recognizes them as administration expenses. Id.

\textsuperscript{20} I.R.C. § 2054 (1986). A casualty loss is any loss incurred during the administration of the estate if the loss arises from fire, storm or other casualty or from theft, but only to the extent that the loss is not compensated for by insurance or otherwise. Id.

\textsuperscript{21} I.R.C. § 2055 (1986).

\textsuperscript{22} I.R.C. § 2056 (1986).

\textsuperscript{23} I.R.C. § 2056(a), (b)(1) (1986). There is an identical marital deduction for inter vivos gifts to one’s spouse. I.R.C. § 2523 (1986). The marital deduction is not available if the spouse is not a United States’ citizen, I.R.C. § 2056(d) (1986), unless the bequest is to a qualified domestic trust. I.R.C. § 2056A (1986).

\textsuperscript{24} I.R.C. § 2056(b)(1) (1986).
spouse that will be included in the surviving spouse's gross estate, unless consumed or disposed of by the surviving spouse prior to death.

Section 2056(b)(4) places several restrictions on the amount of the marital deduction. First, the calculation of the marital deduction must take into account the effect of any federal or state death tax on the net value passing to the surviving spouse.\(^{25}\) Second, the effect of encumbrances on the property passing to the surviving spouse must be considered.\(^{26}\) Finally, the effect of any obligation imposed on the surviving spouse by the decedent with respect to such property must be taken into account.\(^{27}\) The Code requires that the impact of any encumbrance or obligation "be taken into account in the same manner as if the amount of a gift to such spouse of such interest were being determined."\(^{28}\)

A decedent's estate tax liability equals the product of the taxable estate and the applicable tax rate, reduced by any available credits.\(^{29}\) Several credits are available to reduce the estate tax liability. For most estates, the credit offering the greatest benefit is the unified credit. Each individual is entitled to a unified credit which allows the individual to transfer, tax-free, $600,000 of property.\(^{30}\) In addition to the unified credit, a credit for state death taxes is available.\(^{31}\) There are also some less frequently used credits designed to prevent double taxation of the estate. These include the credit for tax on prior transfers,\(^{32}\) a credit for gift taxes paid on gifts made before the unification of the estate and gift tax system,\(^{33}\) and a credit for foreign death\(^{34}\) taxes.

\(^{25}\) I.R.C. § 2056(b)(4)(A) (1986). The term death tax refers to any federal or state estate taxes, succession taxes, legacy taxes and inheritance taxes.


\(^{27}\) Id.

\(^{28}\) Id.

\(^{29}\) I.R.C. § 2001 (1986). Because of the cumulative nature of the estate and gift tax and the graduated rate system, any adjusted taxable gifts made by the decedent must be taken into account to determine the applicable rate. I.R.C. § 2001(b). Adjusted taxable gifts are any taxable gifts made by the decedent after December 31, 1976. Id. To take account of adjusted taxable gifts, the taxable estate is increased by the amount of adjusted taxable gifts, a tentative estate tax is computed, and then, the tax applicable to the adjusted taxable gifts is subtracted from the tentative tax. Id.

\(^{30}\) I.R.C. § 2010 (1986). The amount of the unified credit is $192,800, which is equivalent to the tax applicable to the transfer of $600,000. I.R.C. § 2001 (1986). The unified credit is applicable to both inter vivos gifts and testamentary transfers; however, inter vivos transfers reduce the amount of the unified credit available at death. I.R.C. §§ 2001(c) (1986), 2010, 2505.

\(^{31}\) I.R.C. § 2013 (1986). The credit for tax on prior transfers is designed to alleviate the estate tax burden when the same property is included in the gross estate of two decedents dying within a relative short time frame.


Consequently, an estate actually pays estate tax only in those situations where
the value of the taxable estate is sufficient to prevent the available credits from
eliminating the tax liability.

B. Income Tax

For income tax purposes, an estate reports income earned by the assets
during administration of the estate. With certain exceptions, an estate
calculates its taxable income in the same manner as an individual—gross income
less allowable deductions.

Certain administration expenses are deductible for purposes of calculating
an estate's taxable income. To be deductible for income tax purposes,
admission expenses must be incurred in a trade or business, in an
investment activity, or in connection with the maintenance or management of
property held for the production of income. Although a single expenditure
may qualify as a deductible expense for both estate tax purposes and income tax
purposes, the Code prohibits deducting the same expenditure more than once.
If an administration expense qualifies as an allowable deduction for both estate
tax purposes and income tax purposes, the executor must waive the right to
deduct the expense against the taxable estate in order to claim the deduction on
the estate's income tax return. The source of payment is irrelevant to the
executor's determination; the executor is free to use the administration expenses
to reduce the taxable estate or the estate's taxable income in whatever manner
the executor chooses.

35. I.R.C. § 641(a)(3) (1986). The estate only reports the income earned by an asset during the period
that the estate holds the asset. After an asset is distributed to the intended beneficiary, the
beneficiary reports any income generated by the asset.
36. I.R.C. § 641(b). Certain deductions available to individuals are not available to estates. For
example, individuals are allowed a personal exemption. I.R.C. § 151(a) (1986). Similarly, certain
restrictions applicable to individuals do not apply to estates. For example, the amount allowable
to an individual as a charitable deduction in any given year is limited to 50% of the individual's
adjusted gross income. I.R.C. § 170(b) (1986). The 50% limitation is not applicable to an estate's
charitable deduction. Id. § 642(c)(1). Other restrictions on the amount an estate may claim as a
deduction exist. Id.
40. Id.
C. Interrelationship of the Estate Tax and the Income Tax

Because an executor is free to use those administration expenses that are allowable for both estate tax and income tax purposes in the most beneficial manner, the executor must determine whether it is more advantageous to deduct such administration expenses against the taxable estate or against the estate's taxable income. Generally speaking, because the transfer tax rate exceeds the income tax rate, the deduction is more valuable in calculating the taxable estate.\(^4^1\) This is not true, however, if the other deductions and credits available to the estate either eliminate the estate tax or make the effective tax rate for estate tax purposes less than the effective tax rate for income tax purposes. In either of those instances, it is more beneficial to claim the deduction for administration expenses against the estate's taxable income.

For example, consider two different decedents. Each decedent has a gross estate of $2 million and neither has used any of the unified credit. Each estate incurs administration expenses of $4,000, all of which may be deducted for either estate tax or income tax purposes, and earns income of $20,000 during the period of administration. Also assume, for simplicity's sake, that neither estate is entitled to any tax credits other than the unified credit.

The first decedent leaves all of her property in a manner that does not qualify for either the marital deduction or the charitable deduction. Therefore, the only deduction allowable in calculating the first decedent's taxable estate is the administration expenses. If the administration expenses are deducted on the estate tax return, the taxable estate is $1,996,000, and the estate tax liability, after reduction for the unified credit, is $586,200. The estate's taxable income is $20,000 and its income tax liability is $7,075. The total tax liability of the estate is $593,275.

If, instead, the executor deducts the administration expenses against the estate's taxable income, the taxable estate is $2 million and the estate tax liability, after reduction for the unified credit, is $588,000. The estate's taxable income is $16,000\(^4^2\) and its income tax liability is $5,491. If this option is chosen, the total tax liability of the estate is $593,491. Clearly, in this situation the more advantageous option is to deduct the administration expenses on the estate tax return.

Now consider the second decedent, who leaves $600,000 to her children and the balance, charged with the obligation of paying the administration

\(^{41}\) The maximum estate tax rate is 55 percent. I.R.C. § 2001 (1986). The maximum income tax rate is only 39.6 percent. I.R.C. § 1 (1986).

\(^{42}\) Gross income of $20,000 less administration expenses of $4,000.
expenses, to her surviving spouse in a manner that qualifies for the marital deduction. If the executor chooses to deduct the administration expenses on the estate tax return, the second decedent's taxable estate is $600,000 and the estate tax liability, after reduction by the unified credit, is zero. The estate's taxable income is $20,000 and its income tax liability, and total tax liability, is $7,075.

If, however, the executor chooses to deduct the administration expenses on the fiduciary return rather than on the estate tax return, the taxable estate is $604,000, which results in an estate tax liability of $1,480, after taking into account the unified credit. The estate's taxable income is $16,000 and its income tax liability is $5,491. Under this option, the total tax liability is $6,971.

In this example, the marital deduction reduces the value of the taxable estate to such an extent that the effective tax rate applicable for estate tax purposes is less than the effective rate applicable for income tax purposes. As a result, it is more advantageous to deduct the administration expenses against the estate's taxable income.

III. THE CONFLICT BETWEEN THE CIRCUITS: STREET AND HUBERT

The holdings in Street and Hubert conflict with respect to the question of whether an executor can preserve the value of the marital deduction by charging administration expenses to post mortem income. The factual situation giving rise to the conflict can be easily summarized. Decedent's will devises the residue of decedent's estate in a manner that qualifies for the marital deduction; decedent dies in a jurisdiction that permits the will to allocate payment of administration expenses, including any interest expense, to either estate principal or income. In accordance with an authorization included in decedent's will, decedent's executor allocates a portion of the administration expenses to the income earned by the residue during the period of administration of the estate; that is, to the post mortem income earned by the

43. Gross estate of $2,000,000 less (1) administration expenses of $4,000 and (2) marital deduction of $1,396,000. Because the marital share bears the burden of paying the administration expenses, the marital deduction is reduced by the administration expenses. I.R.C. § 2056(b)(4)(B) (1986).

44. Because the administration expenses are charged to the marital share, the amount of the marital deduction must be reduced by the amount of the administration expenses, even though the administration expenses are deducted on the fiduciary return instead of the estate tax return.

The executor deducts the administration expenses allocated to the income on the estate's fiduciary return, rather than on its estate tax return, and does not reduce the marital deduction to reflect the administration expenses paid from estate income.

The tax advantages of this approach can be demonstrated by reconsidering the tax liability of decedent number two in the above example. In the above example, the decedent dies with a gross estate of $2 million, leaving $600,000 to her children and the balance, charged with the burden of paying the $4,000 of administration expenses, to her surviving spouse. The minimum aggregate tax liability for decedent's estate is $6,971. Now, assume that pursuant to state law, decedent's will allows her executor to allocate administration expenses to income or principal and that the executor allocates the $4,000 to income earned by the marital share during administration of the estate. The executor deducts the $4,000 of administration expenses on the fiduciary return, but unlike the prior example, because the administration expenses are allocated to income rather than principle, the executor does not reduce the marital deduction. In this situation, decedent's taxable estate is $600,000 and the estate tax liability, after reduction for the unified credit, is zero. The estate's taxable income is $16,000 and its income tax, and total tax liability, is $5,491, a savings of $1,480.

This approach allows the executor to disregard the question of whether it is more advantageous to claim the administration expenses for estate tax purposes or for income tax purposes. The value of the taxable estate remains the same regardless of the executor's decision, thereby making it always more advantageous to deduct the administration expenses against the estate's income.

An obvious criticism of this approach is that it circumvents the prohibition in section 642(g) against deducting the same expense for both estate tax purposes and for income tax purposes. The Hubert court rejected this criticism by limiting the prohibition to deductions claimed under section 2053, administration expenses, and not to deductions claimed under section 2055, the

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46. For obvious reasons, the issue of whether expenses allocated to income affect the marital deduction arises only with respect to expenses allocated to the income that is earned by the portion of the residue passing to the surviving spouse. If a third party shares in the devise of the residue, any expenses paid from that portion of the residue have no effect on the marital deductions.

47. Gross estate of $2 million less marital deduction of $1,400,000.

48. Except for the difference resulting from the reduction of the estate's aggregate tax liability, the surviving spouse receives the same amount in each example: the residue of $1,400,000 less the administration expenses of $4,000 increased by the $20,000 of income and reduced by the estate's aggregate tax liability. In effect, the executor no longer needs to consider the impact of the election on the taxable estate; the value of the taxable estate remains the same regardless of the executor's decision.
marital deduction. 49 The Hubert court distinguished claiming a section 2053 deduction for administration expenses that have been deducted against the state’s taxable income and failing to reduce the marital deduction by the amount of administration expenses deducted against the state’s taxable income, even though the Code would require the marital deduction to be reduced if the administration expenses were deducted against the taxable estate instead of the taxable income from claiming a deduction in section 2053 for administration expenses that have also been claimed on the estate’s income tax return. At best, this distinction appears to follow the letter but not the intent of section 642(g).

Charging administration expenses to post mortem income raises the issue of whether those administration expenses reduce the amount of the marital deduction. 50 Estate of Street v. Commissioner holds that the marital deduction must be reduced. 51 Estate of Hubert v. Commissioner holds that the marital deduction is not affected. 52

A. Evolution of the Current Judicial Opinion

The tax court first considered the question of whether administration expenses paid from estate income reduce the marital deduction in Estate of Roney v. Commissioner. 53 Mr. Roney, a resident of Florida, left the residue of his estate to his wife in such a manner that the entire bequest qualified for the marital deduction. 54 Mr. Roney’s will was silent regarding the source of payment of administration expenses, and, therefore, under state law the administration expenses were chargeable to the residue. 55 The executrix elected to deduct the administration expenses on the estate’s fiduciary tax return rather than on its estate tax return. 56 The executrix did not reduce the marital

49. 63 F.3d at 1085.
50. Administration expenses allocated to the principal balance of the marital share reduce the marital deduction. I.R.C. § 2056(b)(4)(B) (1986). Additionally, administration expenses allocated to the income earned by the marital share reduce the marital deduction where such allocation is not authorized by state law. Estate of Roney v. Commissioner, 33 T.C. 801 (1960).
52. Estate of Hubert v. Commissioner, 63 F.3d 1083 (11th Cir. 1995), cert. granted, 64 U.S.L.W. 3726 (U.S. Apr. 26, 1996) (No. 95-12-965).
53. 33 T.C. 801 (1960).
54. Id. at 802-03.
55. Id. at 801, 804. The will did address the source for payment of death taxes, which were to be paid from property that did not qualify for the marital deduction. Id. at 802.
56. Id. at 802.
deduction to account for the administration expenses deducted against the estate's taxable income. 57

The tax court held that the administration expenses reduced the marital deduction because the value of the marital deduction is limited to the "net value of the bequest to the wife." 58 The court found that the net value limitation requires that the value of a bequest to the surviving spouse be reduced by debts for which the bequest is liable. 59 Because the surviving spouse received the residue, which under state law was chargeable with payment of all expenses, the net value passing to the surviving spouse was the value of the residue reduced by the administration expenses. 60 The court found it irrelevant that the administration expenses were "charged . . . against income of the estate and deducted . . . on the fiduciary income tax returns." 61 The tax court also found it irrelevant, albeit fortuitous, that the estate generated sufficient income to pay the expenses. 62 Because state law charged the administration expenses to estate principal, the administration expenses reduced the value of the property passing to the surviving spouse, and, hence, reduced the marital deduction, regardless of whether the expenses were paid from income or principal. 63

Courts consistently followed the Roney approach 64 until Estate of Richardson v. Commissioner. 65 In Richardson, the decedent's will devised a portion of the residue to his widow 66 and directed the executors to pay the administration expenses out of the residue. 67 The will also authorized the executors to allocate expenses between income and principal. 68 The Internal

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57. Id. at 801-02.
58. Id. at 802-03 (citing Thompson v. Wiseman, 233 F.2d 734 (10th Cir. 1956)).
59. Id. at 804. The tax court simply extended its previous holding regarding the calculation of the charitable deduction when administration expenses are paid out of income to the calculation of the marital deduction. Estate of Luehrmann, 33 T.C. 277 (1959) aff'd 287 F.2d 10 (8th cir. 1961) (holding that where state law charged administration expenses to estate principal, such expenses reduced the charitable deduction even though paid out of estate income).
60. Estate of Roney, 33 T.C. at 804.
61. Id.
62. Id. (citing Estate of Luehrmann, 33 T.C. 277 (1959) aff'd 287 F.2d 10 (8th cir. 1961)).
63. Id. Ironically, the tax court supports its holding by pointing to the exact portion of the legislative history of the marital deduction it would later reject in Estate of Hubert. Id. at 805. See, infra, text accompanying notes 109, 121-22.
64. See, e.g., Ballantine v. Tomlinson, 293 F.2d 311 (5th Cir. 1961); Estate of Wycoff v. Commissioner, 59 T.C. 617 (1973); Estate of Horne v. Commissioner, 91 T.C. 100 (1988).
66. Id. at 1194.
67. Id. There was no restriction on what part of the residue could be used to pay the administration expenses, however, death taxes could only be paid out of that portion of the residue that did not qualify for the marital deduction. Id.
68. Id. at 1195.
Revenue Service audited the estate tax return and assessed a deficiency, which caused the estate to incur interest expense. The executor allocated the interest expense to the income generated by the marital share during administration and deducted the interest expense on the estate's income tax return. The estate maintained that the interest expense did not affect the value of the marital deduction because the allocation to income preserved the amount of estate principal that passed to the surviving spouse. The Internal Revenue Service challenged this, asserting that the interest expense was chargeable to the estate principal.

The tax court's opinion in *Estate of Richardson* begs the question by assuming "[i]f the interest is chargeable against income it will not reduce the value of the interest in the estate that passes to the surviving spouse under the will, and consequently will not reduce the amount of the marital deduction." The tax court concluded that state law and the terms of the decedent's will control whether an expenditure is charged to income or principal. Because Tennessee law did not require expenses to be charged to either income or principal, the tax court looked to the testator's intent. The tax court found that the will clearly indicated that the testator's intent was to maximize the marital deduction. Because it concluded that charging the interest expense to estate principal would defeat this intent, the tax court found that the decedent intended to charge the interest expense to estate income.

The tax court distinguished its holding in *Estate of Richardson* from that of *Estate of Roney* based on the fact that the expenses involved in *Roney* were "administration expenses which are usually charged against the principal of an estate." The tax court also noted that the emphasis in *Roney* appeared to be on timing. Noting that the value of the gross estate is determined at death, the tax court concluded that because the interest expense accrued after death and was paid out of post-death income, there was no affect on the value of the gross estate.

69. Id. at 1196.
70. Id. Apparently, the non-marital portion of the residue was consumed by other charges to it because the income from the marital share bore the entire burden for the interest.
71. Id. at 1198.
72. Id. at 1199.
73. Id. at 1200.
74. Id. at 1201.
75. Id.
76. Id. at 1203.
77. Id.
78. Id. at 1204.
79. Id.
80. Id. at 1205.
B. Richardson's Progeny: *Street* and *Hubert*

The tax court next faced the issue of the impact of administration expenses allocated to post mortem income upon the calculation of the marital deduction in *Estate of Street*. In *Estate of Street* the decedent's will devised a sufficient amount of his estate to his children to utilize his available unified credit and the remainder to his surviving spouse. Mr. Street's will, in accordance with state law, granted his executor the ability to allocate income and expenses between principal and income as necessary to protect the marital deduction. The executor allocated the administration expenses and the interest expense to the income earned by the residue; that is, the income earned by the marital share, and deducted these expenses on the estate's fiduciary return. The executor did not reduce the marital deduction to reflect either the administration expenses or the interest expense allocated to income.

In *Estate of Street*, the tax court reiterated its position that interest expense, if chargeable to estate income, does not reduce the marital deduction. In addition, the tax court extended its holding in *Estate of Richardson* to administration expenses chargeable to estate income. The tax court's opinion in *Estate of Street* teaches us little aside from the fact that the tax court believes that expenses chargeable to the income of an estate do not reduce the marital deduction. The tax court framed the issue as whether the administration expenses and the interest expense were chargeable to income or to principal.

The court concluded, without discussion or authority, that to the extent the administration expenses and the interest expense were chargeable to income "they do not reduce the amount of principal passing to the surviving spouse and hence qualifying for the marital deduction." The tax court relied on *Estate of Richardson* as authority for the proposition that state law determines whether an expense is charged to principal or income. Once the tax court concluded

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82. *Estate of Street*, 56 T.C.M. at 775.
83. Id. at 777.
84. Id.
85. *Street* arose before the Internal Revenue Service conceded that interest expense chargeable to income does not reduce the marital deduction. Therefore, the effect on the marital deduction of the interest expense allocated to estate income was an issue in *Street*.
86. Id. at 776.
87. Id.
88. Id. at 777
89. Id.
90. Id. at 776.
that the expenses before it were chargeable to income under state law and
determined that interest expense was considered an administration expense
under state law, the court found it "not illogical to extend the treatment afforded
interest in Estate of Richardson v. Commissioner . . . to other administration
expenses." 91

On appeal, the Court of Appeals for the Sixth Circuit affirmed the tax
court's decision with respect to the interest expense but reversed its decision
with respect to the administration expenses. 92 The court of appeals held that
administration expenses, even though chargeable to estate income, reduce the
marital deduction. 93 The court reasoned that because the value of the property
actually distributed to, or for the benefit of, the surviving spouse limits the
amount of the marital deduction, 94 the necessary inquiry is whether the
administration expenses reduce the net value of the assets received by the
surviving spouse. 95

The court of appeals found section 20.2056(b)-4(a) 96 of the Treasury
Regulations dispositive of the issue whether administrative expenses chargeable
to income reduce the marital deduction and chided the tax court for failing to
consider this Regulation. 97 The appellate court determined that section
20.2056(b)-4(a) "controls the tax treatment of administrative expenses paid
from income regardless of state law or the dictates of a decedent's will." 98
The court also found support for its conclusion in the legislative history to section
2056. 99 Finally, the court distinguished administration expenses from interest
expense based on the conclusion that administration expenses accrue at death,
whereas interest expense accrues "sometime after death." 100

91. Id. at 777.
93. Id. at 729.
94. Id. at 726 (citing United States v. Stapf, 375 U.S. 118 (1963)).
95. Id.
96. See infra text accompanying notes 105, 110-11.
97. Estate of Street v. Commissioner, 974 F.2d at 727.
98. Id. at 728. The court concluded "for federal tax purposes, whether the marital deduction must be
reduced to reflect a payment of expenses is a question of federal law, and cannot depend on the
whim of the state courts or legislatures." Id.
99. Id. at 728.
100. Id. at 729. With respect to the interest expense, the court of appeals for the sixth circuit declined
to read Regulation 20.2056(b)-4(a) expansively. Id. at 728. Although the sixth circuit found that
the Regulation clearly requires that the marital deduction be reduced by administrative expenses
paid from estate income, the court concluded that interest on death taxes "must be accorded
different treatment." Id. at 729. Relying on the distinction between administration expenses and
interest expense made by the tax court in Estate of Richardson, the court of appeals found that the
Regulation's failure to specifically mention interest expense made it inapplicable to interest
expense. Id.
The question of the impact on the marital deduction of administration expenses chargeable to income came before the tax court again in *Estate of Hubert v. Commissioner*.

In an opinion that criticized the appellate court's opinion in *Estate of Street*, the tax court reiterated its position that administration expenses do not reduce the marital deduction if chargeable to the income of the estate.

In a reviewed opinion with fifteen of the seventeen judges concurring, the tax court rejected the reasoning advanced by the appellate court in *Estate of Street*. The tax court also addressed the criticisms raised by the court of appeals with respect to the tax court's decision in *Estate of Street* and repudiated the appellate court's distinction between administration expenses and interest expense.

The Court of Appeals for the Eleventh Circuit wholeheartedly affirmed the holding of the tax court, incorporating the majority opinion as its own.

The Internal Revenue Service advanced two arguments in *Estate of Hubert*. First, section 20.2056(b)-4(a) is dispositive of the issue because (1) it requires that the value of the property passing to the surviving spouse be determined by taking into account any material limitation on the surviving spouse's right to income from the property, and (2) the payment of administration expenses from income earned by the marital share during administration of the estate is a material limitation.

Second, the legislative history of section 2056 requires that the marital deduction be reduced by the amount of administration expenses paid from estate income. The Internal Revenue Service based its second argument on a provision in the legislative history.

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102. *Estate of Hubert*, 63 F.3d 1083. Interest expense was not an issue in *Estate of Hubert* because the Internal Revenue Service ruled prior to the tax court's consideration of *Hubert* that it would no longer contest the issue. Rev. Rul. 93-48, 1993-2 C.B. 271.
103. *Id.*
104. *Id.*
105. *Id.*
106. Regulation 20.2056(b)-4(a) provides in pertinent part:

> Marital deduction; valuation of interest passing to surviving spouse.-(a) In general . . .
> The marital deduction may be taken only with respect to the net value of any deductible interest which passed from the decedent to his surviving spouse, the same principles being applicable as if the amount of a gift to the spouse were being determined. In determining the value of the interest in property passing to the spouse account must be taken of the effect of any material limitations upon her right to income from the property. An example of a case in which this rule may be applied is a bequest of property in trust for the benefit of the decedent's spouse but the income from the property from the date of decedent's death until distribution of the property to the trustee is to be used to pay expenses incurred in the administration of the estate.

107. *Estate of Hubert*, 63 F.3d at 1085.
108. *Id.* at 1086.
history, which speaks to the effect on the marital deduction of claims against the estate that are paid from post mortem income. The legislative history addresses the situation in which the surviving spouse is devised the residue and either the surviving spouse pays, or the estate income is used to pay, claims against the estate. In this situation, the marital deduction must be reduced by the amount of any claim paid by the surviving spouse or from the estate income because such payment increases the residue and "such increase in the residue is acquired by purchase and not by bequest."  

With respect to the first argument, the Hubert court examined section 20.2056(b)-(a)'s requirement that "the effect of any material limitations upon [the surviving spouse's] right to income from the property" must be taken into account. Notwithstanding the fact that the Regulation provides, as an example of a material limitation, a bequest of property in trust if the income from the property is to be used to pay expenses incurred in the administration of the estate, the court found that the Regulation did not mandate a reduction of the marital deduction for administrative expenses charged to the estate's income. The court held that the Regulation "is merely a valuation provision which requires material limitations on the right to receive income to be taken into account when valuing the property interest passing to the surviving spouse." The court also held that the use of income to pay administrative expenses is not automatically a material limitation on the surviving spouse's right to the income.

To determine whether payment of the administration expenses from the income earned by the marital share constitutes a material limitation, the court looked to section 2523(e), which allows a marital deduction for gifts in trust if the spouse has a general power of appointment over the remainder interest

109. Id.

The interest passing to the surviving spouse from the decedent is only such interest as the decedent can give. If the decedent by his will leaves the residue of his estate to the surviving spouse and she pays, or if the estate income is used to pay, claims against the estate so as to increase the residue, such increase in the residue is acquired by purchase and not by bequest. Accordingly, the value of any such additional part of the residue passing to the surviving spouse cannot be included in the amount of the marital deduction.

Id.

111. Estate of Hubert, 63 F.3d at 1086.
113. Estate of Hubert, 63 F.3d at 1086.
114. Id.
115. Id.
116. Id.
and is "entitled to all of the income from the trust." 117 The Regulations interpreting section 2523 provide that a "spouse is considered to receive all of the income from a trust even if 'trustees' commissions, and other charges' are paid out of the income, provided the spouse is not deprived of substantial beneficial enjoyment." 118 The Hubert court found this Regulation to be comparable to the Regulations interpreting section 2056(b)(5), the estate tax counterpart of section 2523(e). 119 Because the Internal Revenue Service has ruled that a similar power to allocate executors' and trustees' fees between income and principal "does not result in the disallowance or diminution of the marital deduction" under section 2056(b)(5), 120 the Hubert court found that the executor's power to allocate administration expenses between income and principal was not a material limitation upon the surviving spouse's right to the income. 121 Finally, the court concluded that when compared to the income that would be paid to the surviving spouse during her life, the income spent on administrative expenses was immaterial. 122

With regard to the argument that the legislative history of section 2056 mandates decreasing the marital deduction for administration expenses paid from estate income, the Hubert court found the provision of the legislative history on which the Internal Revenue Service based its argument inapplicable. 123 The Hubert court found the provision inapplicable because it only refers to claims against the estate, which the court found distinguishable from administration expenses. 124 The court distinguished claims against the estate from administration expenses because claims against the estate are "in existence at the date of death; therefore, by their very nature, claims against the estate relate to corpus and must be charged thereto. By contrast, administration expenses come into existence only after the death of the decedent and may relate to both income and corpus." 125

119. Estate of Hubert, 63 F.3d at 1086. Section 2056(b)(5) is identical to section 2523(e) and serves the same purpose-to permit the marital deduction for transfers that give the surviving spouse a power of appointment over property rather than an actual interest in the property.
120. Estate of Hubert, 63 F.3d at 1086 (citing Rev. Rul. 69-56, 1969-1 C.B. 224).
121. Id. Because the statute requires the spouse to be entitled to all of the income from the property in order for the donor spouse to enjoy the marital deduction, the Hubert court concluded that the surviving spouse was not denied "substantial beneficial enjoyment" and, therefore, under 25.2523(e)-1(f)(3) would be treated as "having received all of the income from the trust." Id.
122. Id.
123. Id. at 1087.
124. Id.
125. Id.
Having rejected the Sixth Circuit's reasoning, the Hubert court fell back on Estate of Richardson and the tax court's opinion in Estate of Street to support its conclusion that administration expenses, like interest expense, do not reduce the marital deduction if charged to the estate's income.\textsuperscript{126} To reach this conclusion, the Hubert court rejected the distinction drawn by the Sixth Circuit between administration expenses and interest expense.\textsuperscript{127} According to the Hubert court, administration expenses, as well as interest expense, accrue after death.\textsuperscript{128} The court concluded that administration expenses do not accrue at death because of the impossibility of determining at the date of death the amount necessary to administer a particular estate.\textsuperscript{129} Based on its conclusion that both administration expenses and interest expense accrue after death, the Hubert court concluded that the holding in Estate of Richardson, that interest expense does not reduce the marital deduction, was equally applicable to administration expenses.\textsuperscript{130}

IV. ANALYZING THE CONCLUSIONS OF THE HUBERT COURT

When a surviving spouse receives property subject to an obligation imposed by the decedent, section 2056(b)(4)(B) requires that the effect of such obligation on the marital deduction be determined "as if the amount of a gift to such spouse of such interest were being determined."\textsuperscript{131} The Regulations interpreting section 2056(b)(4)(B) clarify this provision by stating that the amount of the marital deduction is limited to the net value of the property passing to the surviving spouse.\textsuperscript{132} In determining the net value of property passing to the surviving spouse, material limitations upon the surviving spouse's right to income from such property must be taken into account.\textsuperscript{133} The Regulations give, as an example of a material limitation, a bequest in trust where the income from the trust is to be used to pay the estate administration expenses.\textsuperscript{134}

\textsuperscript{126} Id. at 1088.
\textsuperscript{127} Id. at 1089.
\textsuperscript{128} Id. at 1088. The Sixth Circuit distinguished administration expenses from interest expense based on its conclusion that administration expenses accrue at death and interest expense does not. Estate of Street, 974 F.2d at 727.
\textsuperscript{129} Id.
\textsuperscript{130} Id.
\textsuperscript{131} I.R.C. § 2056(b)(4)(B) (1986).
\textsuperscript{132} Treas. Reg. § 20-2056(b)-4(a) (1986).
\textsuperscript{133} Id.
\textsuperscript{134} Id.
A. The Court Improperly Construes Section 20.2056(b)-(4)(a)

The Hubert court found that section 20.2056(b)-4(a) does not mandate a reduction of the marital deduction. In interpreting the Regulation, the Hubert court erroneously looked to section 2523(e) and the corresponding sections. Section 2523 sets forth the gift tax marital deduction, which is almost identical to the estate tax deduction. Section 2523 grants an unlimited marital deduction for any inter vivos transfer by gift to the donor's spouse of "an interest in property," provided such interest is not a terminable interest. Section 2523(e) addresses a transfer of property, in trust or otherwise, where the terms of the transfer make the donee spouse the sole beneficiary of a life estate in the income from the property and gives the donee spouse a general power of appointment over the remainder, which the donor spouse either retains or gives to someone other than the donee spouse. Without the special provisions of section 2523(e), such a transfer does not qualify for the marital deduction. Section 2523(e) allows the donor spouse to claim the marital deduction for the value of the property transferred, including the value of the remainder interest, because, based on the terms of such transfer, the donee spouse "is the virtual owner of the property." The Hubert court concluded that because a power to charge executors' and trustees' commissions to income does not preclude the surviving spouse from being considered the sole income beneficiary, such a power is not a material limitation on the spouse's income and, therefore, does not effect the amount of the marital deduction.

The Hubert court's reliance on section 2523(e) is

135. Estate of Hubert, 63 F.3d at 1086.
137. I.R.C. § 2523(a),(b).
139. Absent 2523(e), neither the life estate nor the remainder interest meets the requirements necessary to qualify for the marital deduction. The donee spouse's life estate does not qualify for the marital deduction because it violates the terminable interest rule. I.R.C. § 2523(b)(1). The transfer of the remainder interest does not qualify for the marital deduction because all the donee spouse receives is a general power of appointment over the remainder interest, and "a power of appointment is not an 'interest in property.'" S.Rep. No. 1013, at 1223. See infra text accompanying notes 23-24 for a discussion of the terminable interest rule. For gift tax purposes, the transfer of a property interest to a donor's spouse also violates the terminable interest rule if, instead of transferring an interest in the property to a third person, the donor retains either an interest in the property or a power of appointment over the property. I.R.C. § 2523(b)(1),(2).
141. Estate of Hubert, 63 F.3d at 1086.
misplaced. Section 2523(e) is not a valuation provision. Its purpose is to enable a donor spouse to claim the marital deduction for property transferred in the prescribed manner, not to determine the value of such property. Just because a transfer qualifies for the marital deduction does not mean that the transfer escapes the valuation rules of section 2056(b)(4).

B. The Court's Interpretation of Section 2056(b)(4)(B) Does Not Accord with the Statutory Language

The Regulations interpreting section 2056(b)(4)(B) state that material limitations on the surviving spouse's right to income affect the value of the marital deduction. The Hubert court compared the income used to pay administration expenses with the total income the surviving spouse would receive from the property during life in order to determine whether the impact on the surviving spouse's right to income was material.\(^{142}\) The Hubert court's approach effectively concludes that no use of the income earned by the marital share to pay administration expenses will constitute a material limitation.\(^{143}\) If the standard of materiality requires a comparison of the income used to pay expenses with the surviving spouse's lifetime income interest, as a practical matter, the surviving spouse's right to income will never be materially limited.\(^{144}\) Consequently, the Hubert court's approach renders the word "material" meaningless.

The Hubert court construed section 20.2056(b)-4(a) in a manner that contradicts the clear language of the statute. Section 2056(b)(4)(B) provides that "any obligation imposed by the decedent" be taken into account. The statute contains no exception for immaterial obligations. Instead, section 2056(b)(4)(B) clearly states that any obligation, immaterial as well as material, imposed by the decedent, affects the value of the marital deduction.\(^{145}\) If, as the

\(^{142}\) Id.
\(^{143}\) On the other hand, the approach adopted by Streat suggests that any use of income to pay administration expenses always constitutes a material limitation.
\(^{144}\) Using the standard adopted by the Hubert court, materiality will depend on how long the surviving spouse outlives the decedent. If this standard is adopted, using income earned by the marital share to pay administration expenses is likely to be a material limitation only when the surviving spouse dies shortly after the decedent.
\(^{145}\) Obviously, it is more convenient for the Internal Revenue Service if only those obligations that materially affect the value of the property interest passing to the surviving spouse must be taken into account. The question, however, is whether administrative convenience justifies an interpretation that departs from the plain language of the statute; does administrative convenience justify construing "any obligation" to mean only those that materially affect the value of the property.
plain language of the statute seems to imply, any obligation imposed by the
decedent must be taken into account, an obligation affects the value of the
marital deduction regardless of whether the impact of such obligation on the
source of payment, in this case the surviving spouse's right to income, is
material or immaterial.146 The pertinent question is whether the payment of
administration expenses from post mortem income is an obligation imposed by
the decedent on the surviving spouse.

V. THE INTERPRETATION ADVANCED BY UNITED STATES V.
STAPF

The analysis adopted by the Hubert court does not accord with the
interpretation of the predecessor to section 2056(b)(4)(B), sections 812(e)(1)(A)
and 812(e)(1)(E)(ii) of the Internal Revenue Code of 1939, adopted by the
Supreme Court in United States v. Stapf.147

A. The Interpretation Advanced in United States v. Stapf

Mr. Stapf died a resident of Texas, a community property state.148 His will
gave his widow the option of keeping her one-half of the community property
and receiving nothing under the will or contributing her share of community
property to a trust created by Mr. Stapf and benefiting under the will.149 Mrs.
Stapf elected to take under the will, which meant that, after reduction for certain
specific bequests, she was entitled to one-third of her husband's separate
property and one-third of the combined community property.150 As a result, she
received property valued at $106,268 and surrendered property having a value
of $111,443.151 The executors of Mr. Stapf's estate deducted, as the marital
deduction, the entire value of property passing to Mrs. Stapf under the will.152
The Internal Revenue Service challenged the deduction, asserting that sections
812(e)(1)(A) and 812(e)(1)(E)(ii) of the Internal Revenue Code of 1939 dictated

146. The materiality of the obligation's impact on the source of payment is relevant in determining the
    effect of the obligation. The greater the impact, the greater the effect on the value of the marital
deduction.
147. 375 U.S. 118 (1963). The language of section 2056(b)(4)(B) is identical to that of section
    812(e)(1)(A) and 812(e)(1)(E)(ii).
148. Stapf, at 120.
149. Id. The trust created by Mr. Stapf's will was for the benefit of the couple's children. Id.
150. Id.
151. Id. at 122.
152. Id. at 122.
that the marital deduction be reduced by the value of the community property surrendered by Mrs. Stapf. 153

In United States v. Stapf, the Supreme Court interpreted two provisions of sections 812(e)(1)(A) and 812(e)(1)(E)(ii), which remain intact in section 2056(b)(4): “(1) the introductory phrase ‘any obligation imposed by the decedent with respect to the passing of such interest;’ and (2) the concluding provision that ‘such . . . obligation shall be taken into account in the same manner as if the amount of a gift to such spouse of such interest were being determined.’” 154 Reading the statutory provision as a whole, the Supreme Court reached several conclusions. First, the marital deduction exists only for bequests or devises that pass to the surviving spouse. 155 The Supreme Court found that “[t]he gift-to-the-surviving-spouse terminology reflects concern with the status of the actual recipient . . . .” 156 Consequently, the Supreme Court concluded that “[t]he appropriate reference . . . is not to the value of the gift moving from the deceased spouse but to the net value of the gift received by the surviving spouse.” 157 Second, the Supreme Court determined that the statutory direction requiring consideration of any obligation imposed by the decedent “relates the gift-amount determination to the net economic interest received by the surviving spouse.” 158

The Supreme Court found its interpretation supported by the legislative history of the marital deduction. 159 In particular, the Court found the following example in the legislative history persuasive:

If the decedent bequeaths certain property to his surviving spouse subject, however, to her agreement, or a charge on the property, for payment of $1,000 to X, the value of the bequest (and, accordingly, the value of the interest passing to the surviving spouse) is the value, reduced by $1,000, of such property.” 160

Based upon legislative history, the Treasury Regulations, and its interpretation of the statute, the Supreme Court concluded “that the governing principle, approved by Congress and embodied in the Treasury Regulation, must be that

153. Id. at 123. Because the value of the property surrendered by Mrs. Stapf exceeded the value of the property she received under the will, the Internal Revenue Service took the position that Mr. Stapf’s estate was not entitled to a marital deduction. Id.
154. Id. at 124.
155. Id. at 125.
156. Id.
157. Id.
158. Id. at 126.
159. Id.
160. Id. (quoting S.Rep. No. 1013 (Part II), 80th Cong., 2d Sess. 1228 (1948)).
a marital deduction is allowable only to the extent that the property bequeathed to the surviving spouse exceeds in value the property such spouse is required to relinquish.\textsuperscript{161}

B. Applying \textit{Stapf} to the Facts Posed in \textit{Hubert}

The Supreme Court's analysis in \textit{Stapf} is apposite to the factual situation faced in \textit{Estate of Hubert}. Under the analysis adopted in \textit{Stapf}, if the decedent leaves property valued at $10,000 to the surviving spouse, subject to the decedent's direction that the surviving spouse pay the decedent's attorney $1,000 to administer the decedent's estate, the value of the marital deduction equals $9,000, the net economic benefit to the surviving spouse.\textsuperscript{162}

The factual situation encountered in \textit{Hubert} is indistinguishable from the situation in which the decedent explicitly directs the surviving spouse to pay the decedent's administration expenses. In the situation found in \textit{Hubert}, the decedent allows the executor to allocate administration expenses to the income earned by the marital share, income which is the property of the surviving spouse.\textsuperscript{163} By allowing the executor to charge the administration expenses to the surviving spouse's income, the decedent, in effect, conditions receipt of the marital share upon the surviving spouse's payment of the administration expenses. Because receipt of the marital share is conditioned upon the surviving spouse's payment to a third party, the "net economic benefit" to the surviving spouse and, hence, the value of the marital deduction equals the value of the property devised to the surviving spouse less the amount of administration expenses paid from her share of estate income.

In \textit{Stapf}, the lower court noted that a donor spouse who gives property to the donee spouse on the condition that the donee spouse give something to the children is subject to gift tax on the full value of property transferred by the donor spouse.\textsuperscript{164} Therefore, the lower court concluded that the value to the

\begin{footnotesize}
\begin{enumerate}
\item[161.] \textit{Id.} at 127.
\item[162.] Notwithstanding the \textit{Hubert} court's conclusion that under state law the administration expenses were chargeable to estate income, the estate principal remained liable for payment of the administration expenses. Most states have a statute charging a decedent's estate with the expenses of administration. \textit{See}, e.g., \textit{GA. CODE ANN.} \textsection 53-7-90 (1995). Nothing in the statutory provision examined by the \textit{Hubert} court indicates that the estate principal is relieved from liability for the administration expenses if the income should prove inadequate. The implication is that the principal of the estate remains liable; charging the expenses to income simply creates another source of payment.
\item[163.] The surviving spouse, as residuary legatee, is entitled to all income earned by the residue. \textsc{Thomas E. Atkinson, Law of Wills} 753 (1953).
\item[164.] \textit{Stapf}, 375 U.S. at 124.
\end{enumerate}
\end{footnotesize}
donee spouse equals the amount transferred by the donor spouse; there is no reduction for detriment to the donee spouse.\textsuperscript{165}

The Supreme Court found that the lower court’s conclusion was not supported by the statute.\textsuperscript{166} Because the effect of the donor spouse’s direction was to transfer wealth to someone other than the donee spouse, the value of the gift to the spouse was limited to the net amount received by the donee spouse.\textsuperscript{167} The same conclusion applies to the facts set forth in \textit{Hubert}.\textsuperscript{168} By directing the executor to charge the administration expenses to the income earned by the marital share, the decedent diverts a portion of the property given to the donee spouse to someone other than the donee spouse. Therefore, the value of the marital deduction must be reduced by the amount of administration expenses charged to the income earned by the marital share.\textsuperscript{169}

Analyzing a decedent’s direction that administration expenses be charged to the income earned by the marital share using the principles enunciated in \textit{United States v. Stapf}, it is clear that such direction imposes an obligation on the surviving spouse that reduces the surviving spouse’s net benefit from the marital share. It is equally clear that the principles enumerated in \textit{United States v. Stapf} dictate that the current Court either hold that the marital deduction must be reduced by administration expenses charged to post mortem income or limit, explicitly or implicitly, the holding of \textit{United States v. Stapf}.\textsuperscript{169}

\begin{footnotes}
\footnote{165. \textit{Id.}}
\footnote{166. \textit{Stapf}, 375 U.S. at 124. The taxpayers relied on \textit{Commissioner v. Wemyss}, 324 U.S. 303 (1945) as support for the proposition that detriment to the surviving spouse does not reduce the amount of the marital deduction. \textit{Stapf}, 375 U.S. at 124, note 8. \textit{Wemyss} held that detriment to incurred by a transferee does not constitute consideration for purposes of the gift tax, and, therefore, does not reduce the amount of a gift. \textit{Id.} The court found the taxpayer’s reliance on \textit{Wemyss} misplaced because \textit{Wemyss} did not address who was the recipient of the gift or the value of the gift. \textit{Id.}}
\footnote{167. \textit{Stapf}, 375 U.S. at 125.}
\footnote{168. As in \textit{Stapf}, the important question in this situation is who is the intended recipient of the decedent’s property. Only property interests that pass from the decedent to the surviving spouse qualify for the marital deduction. I.R.C. §2056(a) (1986).}
\footnote{169. This conclusion is further supported by the principles used for gift tax purposes to value property gratuitously transferred subject to an obligation. When a donor spouse transfers property to a donee spouse subject to the condition that the donee assume a liability of the donor spouse, the amount of the gift equals the value of the property transferred to the donee spouse less the amount of the donor’s liability that the donee spouse undertakes. \textit{Jackman v. Commissioner}, 44 B.T.A. 704 (1941) (holding that the value of a gift to the spouse was reduced by the amount of the donor’s indebtedness encumbering the property). Similarly, whenever a donor transfers property subject to a condition, either explicit or implicit, that the donee undertake an obligation of the donor, the amount of the gift equals the value of the transferred property reduced by the amount of the obligation undertaken by the donee. \textit{E.g., Harrison v. Commissioner}, 17 T.C. 1350 (1952); \textit{Lingo v. Commissioner}, 13 T.C.M. (CCH) 436 (1954).}
\end{footnotes}
C. The Impact of *Stapf* on Interest Expense Chargeable to Income

*Richardson Street* and their progeny agree that interest expense chargeable to income of an estate does not affect the marital deduction because interest "accrues" sometime after death.\(^{170}\) The courts appear to agree on two points. One, an expense charged to income automatically affects the marital deduction, if the expense is in existence at death. Two, an expense charged to income does not automatically affect the marital deduction if not in existence at death.\(^{171}\)

This approach ignores the holding of *Stapf* that the amount of the marital deduction is limited to the net economic benefit received by the surviving spouse, not the value of the property "moving from the deceased spouse."\(^{172}\) *Stapf* teaches us that in order to determine the value received by the surviving spouse, the value of the property passing from the decedent must be reduced by the value of all obligations imposed on surviving spouse, not just those in existence at the date of the decedent’s death.

Additionally, by focusing on the time an expense accrues, the courts ignore the fundamental purpose of the estate tax—to tax the value of property transferred from a decedent to the beneficiaries of an estate.\(^{173}\) Congress has defined the value of property subject to estate tax, the taxable estate, as the gross estate less allowable deductions.\(^{174}\) The Supreme Court in *Stapf* held that the value of the marital deduction is similarly limited to the value of the property that the decedent can give to the surviving spouse, not the value moving from the decedent.\(^{175}\) A decedent can transfer, or "give away," only that property that remains after payment of all debts and claims chargeable to the estate. Therefore, in determining whether an expense must be taken into account in calculating the taxable estate, the relevant question is not when the expense accrues, but when the property is transferred from the decedent.

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170. The courts refer to whether the expense "accrues" at death as the determinative factor but fail to define what they mean by "accrue," however, from reading the case law, it is clear that the courts agree that an expense in existence at death "accrues" at death.

171. With respect to administration expenses, the courts differ with respect to when administration expenses accrue.


173. *Id.* at 131.

174. The deductions allowable by sections 2053 and 2054 support the conclusion that Congress intended to tax only the value of the property that a decedent could transfer to the beneficiaries. Section 2053 recognizes that the value of property that a decedent can "give away" is reduced by the decedent’s outstanding debts, by the cost of the decedent’s funeral and by the costs associated with making the testamentary gift, i.e., the administration expenses. Similarly, section 2054 recognizes that a decedent cannot "give away" property that is destroyed during the administration of decedent’s estate.

175. *Stapf*, 375 U.S. at 125.
expense accrues, but whether the expense is one that reduces the value of property available to make the testamentary gift.

When the value of the marital deduction is determined by reference to the property available to the decedent to make a testamentary gift, it is clear that interest expense, as well as administration expenses, reduce the amount of property that the decedent can give away. Based on the interpretation of the marital deduction enunciated in Stapf, the value of the marital deduction is reduced by both administration expenses and interest expense allocated to post mortem income earned by the marital share.

VI. SOUND POLICY REASONS EXIST FOR FOLLOWING STAPF

Acceptance of the interpretation of section 2056(b)(4)(B) adopted by Estate of Hubert, that the value of the marital deduction is not reduced by expenses chargeable to post mortem income, would circumvent the purpose of section 642(g). Section 642(g) permits an executor to deduct an expense otherwise allowable under sections 2053 or 2054 against the estate's taxable income only if the executor agrees to forgo the estate tax deduction allowed by those sections. The clear purpose of section 642(g) is to limit the benefits available from a section 2053 or section 2054 deduction. Such deductions may benefit an estate only once and the cost of choosing to use a section 2053 or section 2054 deduction to reduce the taxable estate means that the estate's taxable income will be greater than if the deduction were used to reduce taxable income and vice versa.

In fact, section 642(g) presumes that the taxable estate will be reduced by the administration expenses unless the executor agrees to remove such expenses from the calculation of the taxable estate in order to include them in the calculation of the estate's taxable income. Consequently, an election to deduct administration expenses against the estate's income necessarily implies that there will be a corresponding increase in the taxable estate. Adoption of the Hubert approach allows the executor to relinquish a section 2053 or section 2054 deduction without suffering the consequences demanded by section 642(g)—there is no corresponding increase in the taxable estate. The approach adopted by United States v. Stapf, on the other hand, prevents evasion of section 642(g). If the marital deduction is reduced to reflect the obligation imposed on the surviving spouse, the value of the marital deduction cannot offset the increase in the taxable estate caused by the election to deduct the administration expenses against taxable income.
VII. CONCLUSION

Section 2056(b)(4)(B) requires the value of the marital deduction to be reduced by the amount of any obligation imposed on the surviving spouse by the decedent. The interpretation of the marital deduction adopted by *United States v. Stapf* construes this requirement to limit the amount of the marital deduction to the net economic benefit received by the surviving spouse. A surviving spouse's net economic benefit equals the value of the property received from the decedent reduced by any amount that the surviving spouse is obligated to pay to a third party. A direction in the decedent's will that results in charging administration expenses, interest expenses, or any other expense to the income earned by the marital share is equivalent to subjecting the surviving spouse to an obligation to pay such expenses. Consequently, the value of the marital deduction is reduced by the amount of any expenses charged to the income earned by the marital share.