

The Constitutional Limits of the Massachusetts Estate Tax

By Andrew D. Rothstein

It has been nearly five years since Massachusetts enacted its current version of the estate tax. During that time Massachusetts trusts and estates lawyers have become more familiar with the law and how it works. The experience developed during that time has led to the discovery that, in at least one respect, the Massachusetts estate tax may reach beyond the constitutional limits on the commonwealth's jurisdiction to tax. Those limits only permit Massachusetts to impose its estate tax on real and tangible personal property located within the commonwealth. See, *Frick v. Pennsylvania*, 268 U.S. 473, 498 (1925). However, in certain circumstances Massachusetts imposes its estate tax on real or tangible personal property that is located outside of Massachusetts.

Under the current Massachusetts estate tax, the amount of the tax payable by the estate of a resident decedent is equal to the amount of the credit for state death taxes that would have been allowable by the resident decedent's estate computed under Internal Revenue Code §2011, as in effect on Dec. 31, 2000. M.G.L. ch. 65C, §2A(a).

The starting point for the calculation of the credit for state death taxes is the federal gross estate. See, Form M-706 Massachusetts Resident Estate Tax Return Instructions. This includes all property, real and personal, whether the property is located within Massachusetts or outside of Massachusetts.

For example, a Massachusetts resident decedent who owned Massachusetts real estate valued at \$5,000,000 and Florida real estate valued at \$5,000,000, calculates his estate tax starting with a gross estate of \$10,000,000. Assuming no deductions, the Massachusetts estate tax is calculated as follows:

Taxable Estate	\$ 10,000,000
Less: \$60,000 per IRC § 2011(b)(3)	<u>(60,000)</u>
Adjusted Taxable Estate	\$ 9,940,000
Times: Effective Tax Rate	<u>10.74%</u>
Total Massachusetts Estate Tax	\$ 1,067,600

Part 2 of the M-706 provides a further computation for a resident decedent with property located in another state. Under the Massachusetts approach, the estate is given credit for tax actually paid in the other jurisdiction. However, as a result of decoupling, there is no Florida estate tax payable by the decedent in the example above, and therefore no credit will be given on the Massachusetts return. As a result, the decedent's estate will pay a Massachusetts estate tax attributable to the real property located in Florida.

While the Massachusetts credit for tax paid in another jurisdiction appears to prevent multiple state death taxes from being imposed on the property of a Massachusetts resident decedent, it does not prevent Massachusetts from effectively taxing a resident decedent's property located outside of Massachusetts.

Massachusetts taxes a nonresident decedent's estate differently than a resident decedent's estate. If the decedent in the example above was a Florida resident instead of a Massachusetts resident, the credit for state death taxes (as figured above) would still be the starting point. The credit for state death taxes would then be apportioned based on the ratio of Massachusetts property to the total estate. M.G.L. ch. 65C, §2A(b). Thus, the nonresident decedent's estate would only be subject to Massachusetts estate tax on property located in the commonwealth. The statute makes no distinction as to whether the nonresident lives in a state that imposes a death tax or not. In this example, the nonresident decedent's estate would owe only \$533,800 – one-half the amount it would owe if the decedent was a Massachusetts resident.

There is legal authority that indicates that the disparity in the Massachusetts estate taxation of a resident decedent and a nonresident decedent may be problematic from a constitutional law perspective.

In *Frick v. Pennsylvania*, 268 U.S. 473, 498 (1925) the United States Supreme Court held that a Pennsylvania estate tax statute, "in so far as it attempts to tax the transfer of tangible personalty having an actual situs in other States, contravenes the due process of law clause of the Fourteenth Amendment and is invalid." In its deci-

sion the Supreme Court noted “[i]ndeed, we know of no case where a legislature has assumed to impose a tax upon land within the jurisdiction of another state, much less where such action has been defended in any court.” *Id.* at 490 quoting Union Refrigerator Transit Co. v. Kentucky, 199 U.S. 194 (1905).

The United States Supreme Court reached a similar result in Treichler v. Wisconsin, 338 U.S. 251 (1949). There the Court held a Wisconsin estate tax statute “invalid insofar as it is measured by tangible personal property outside of Wisconsin.” *Id.* at 257. In that case, the Wisconsin tax was measured by portions of the federal death tax credit that were attributable to tangible personal property located outside of Wisconsin.

Because the Massachusetts estate tax for a resident decedent is determined in part based on the value of real property located outside of Massachusetts, it is possible that the statute results in the application of the Massachusetts estate tax beyond the constitution’s jurisdictional limits that allow the tax to be imposed only on real and tangible personal property located within the commonwealth.

The California Supreme Court dealt with a similar issue in Cory v. Fasken, 563 P.2d 832, 842 (1977). In that case the California Supreme Court found that constitutional limits on the state’s jurisdiction to impose its estate tax prevented California from “picking-up” any part of the federal credit for state death taxes that was not apportioned to property within the state. In reaching its decision, the Court reasoned that California’s entitlement to a portion of the credit

“...should not depend on how one or more of the other states with a right to levy inheritance or pick-up taxes proceed to do so. Should, for instance, a sister state with some portion of estate property located within its borders elect not to assert its claim for a share of the federal credit, California’s entitlement should not thereby be enlarged or otherwise affected as any increased apportionment in California’s favor would extend its jurisdictional reach to the sister state’s property.”

Based on the cited authorities, it is possible that the Massachusetts estate tax, to the extent that it applies to a resident decedent’s property with a situs outside of the commonwealth, may be subject to a constitutional challenge.

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