The New York Non-Resident Estate Tax: A Tax That Can Be Less Than it Seems to Be
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The de-coupling of the federal and New York estate taxes has raised a number of questions with regard to the calculation of the New York estate tax. One of these involves the proper amount of the tax on the estate of a U.S. citizen who died domiciled in a jurisdiction that does not impose a state death tax and owned property that is taxable in New York. On its face, New York would seem to impose a tax equal to the full amount of the credit for state death taxes calculated on the decedent’s entire federal taxable estate, less only the amount of tax levied by other states. In other words, New York would seem to take for itself any portion of the full potential credit for state death taxes that is not absorbed by other state taxes. However, in a recent unreported case, the State Tax Commission has determined that this is not the case. The difference in tax was dramatic. The decedent owned approximately $50,000 of property that was taxable in New York. Following the instructions to Form ET-706, after subtracting state death taxes payable to other states, the State Tax Commission initially proposed a New York estate tax of over $400,000. After consideration of the position set forth below, the New York tax was finally determined to be about $3,000.

The taxation of the estate of a non-resident is governed by Section 960 of the New York State Tax Law (the “Tax Law”). Section 960(a) imposes a tax on the transfer by a non-resident “of real and tangible personal property having an actual situs in New York State” which is includible in his federal gross estate (emphasis added). Pursuant to Section 960(b) of the Tax Law, with an exception not relevant here, the tax due on the estate of a non-resident is the same as the tax due on a New York State resident under Section 952(a) of the Tax Law. Section 952(a) of the Tax Law imposes a tax on the estate of a New York State resident in “an amount equal to the maximum amount allowable” against the federal estate tax as a credit for state death taxes under Section 2011 of the Internal Revenue Code (emphasis added). (Under Section 951(a) of the Tax Law, the Internal Revenue Code is defined to mean the Internal Revenue Code of 1986, with all amendments enacted on or prior to July 22, 1998 [the “Code”].) Section 952(b) of the Tax Law reduces the amount of the New York estate tax in situations where the estate of a deceased resident is subject to a tax imposed by another state with respect to which credit is allowed under Section 2011 of the Code by the lesser of (a) the amount of the death tax paid to the other state that is allowable as a credit for state death taxes and (b) the fraction of that credit that is attributable to non-New York property.

Since the maximum amount of New York estate tax imposed by Section 952 is the “maximum amount allowable against the Federal estate tax as a credit for state death taxes under Section 2011 of the Code,” the initial inquiry must be to determine the amount of the credit for state death taxes that would be allowed in determining the federal estate tax on the decedent’s estate under the Code.

There is a basic United States constitutional proposition that a state has no power to tax the transfer of a decedent’s intangible personal property that lies outside its jurisdiction. And a state may not do indirectly, by taking the whole of a decedent’s estate as the basis for measuring the tax on the portion that lies within its jurisdiction, that which it may not do directly. The Internal Revenue Service applied these principles in Revenue Ruling 56-230, 1956-1 C.B. 660 in determining the amount of credit allowable for state death taxes in a situation very similar to the situation here under discussion.

Revenue Ruling 56-230 involved the estate of a non-resident non-citizen of the United States who owned real property in one state of the United States and intangible personal property situated in another state, all of which was included in his gross estate for federal estate tax purposes. Like New York, the state in which the intangible personal property was situated did not impose an estate tax on the intangible personal property of a non-domiciliary. The state in which the real property was situated imposed an estate tax on that real property and, in addition, sought to impose an additional estate tax (a “Sop Tax”) in an amount sufficient to avail itself of the full credit for state death taxes allowable under then-Sec- tion 813(b) of the Internal Revenue Code of 1939 (the predecessor to Section 2011 of the Code). The estate advised the Internal Revenue Service that it was prepared to pay this additional Sop Tax if it would get a credit against the federal estate tax for the amount of the payment.
Citing the aforecited Supreme Court cases for the proposition that a state “has no power to tax the transfer of intangible personal property of the decedent’s estate which lies outside its jurisdiction,” and that a state, being without the power to tax directly the transfer of property outside its jurisdiction, “cannot accomplish the same thing indirectly by taking the whole of the decedent’s estate as the basis for measuring the tax on the transfer of that part of the estate which lies within its jurisdiction,” the Internal Revenue Service ruled that the credit for state death taxes would be “limited in the instant case and will be limited in all other similar cases to the proportion of the full Federal credit allowable to the estate which is attributable to that part of the gross estate situated in State A” (i.e., the state seeking to impose the Sop Tax) (emphasis added).

Following the principles set forth in Revenue Ruling 56-230, the State Tax Commission determined that the only property with respect to which a credit for state death taxes would be allowable under Section 2011 of the Code is property within the jurisdiction of states of the United States the transfer of which was constitutionally subject to tax by those states and that the New York tax would be its pro-rata share of that credit.3

Accordingly, the first step required to calculate the amount of the New York estate tax was to determine the value of the decedent’s property situated in states of the United States which could constitutionally be subject to tax. This property consisted of his real and tangible personal property located within those states and, in the case of the states that exercised their jurisdiction under Utah v. Aldrich4 to tax certain intangible personal property, such as the stocks of corporations formed or headquartered within their bounds, also the value of that property. 5

Since the credit under Section 2011 of the Code is calculated as a fraction of “the adjusted taxable estate,” it was next necessary to determine what the adjusted taxable estate would be in a situation where the gross estate for the purpose of determining the credit for state death taxes (the “State Death Tax Gross Estate”) was not the same as the gross estate for determining the federal estate tax. The term “adjusted taxable estate” is defined in Section 2011(b)(3) of the Code as the “taxable estate reduced by $60,000.” The term “taxable estate” is defined in Section 2051 of the Code as the value of the gross estate, less the deductions provided for in Part IV of Subchapter A of Chapter 11 (namely, after deductions for administration expenses, indebtedness and taxes under Section 2053 of the Code, losses under Section 2054 of the Code, transfers for public, charitable or religious uses under Section 2055 of the Code and bequests to a surviving spouse under Section 2056 of the Code). In determining the adjusted taxable estate for the purpose of calculating the credit for state death taxes, the State Tax Commission allowed deductions from the State Death Tax Gross Estate for expenses, such as ancillary probate fees, appraisal costs and fees of attorneys situated in the states where the taxable property was located that were directly related to the administration of the taxable property and granted a marital deduction for such of that property as passed to the decedent’s spouse. No deduction was claimed or granted for a pro-rata portion of the total of the decedent’s debts and the expenses of administering the estate. The credit for state death taxes allowable to the decedent’s estate was then determined by applying Section 2011(b) of the Code to this adjusted taxable estate.6

Pursuant to Revenue Ruling 56-230, the New York state death tax was limited to the portion of the credit for state death taxes which was attributable to that part of the adjusted taxable estate that was situated in New York. The numerator of that fraction, therefore, was the portion of the above-calculated adjusted taxable estate that was situated in New York and the denominator of the fraction was the total of the above-calculated adjusted taxable gross estate.7

The case discussed in this article involved a decedent whose estate was subject to a United States estate tax and who died domiciled in a jurisdiction that did not impose any estate or inheritance tax and, therefore, none that qualified for the federal credit for state death taxes. However, the principles announced in Revenue Ruling 56-230 would be equally applicable to the estate of a non-resident of New York who dies in a Sop Tax state which has not de-coupled its estate tax from the federal estate tax and who also owned property taxable in New York. In such a situation, New York should not be able to gain any additional tax simply because the decedent’s domiciliary state imposes a lesser tax because of the reductions required by Section 2011(b)(2) of the current Code than its full share of the credit for state death taxes calculated under Section 2011(b)(1) of the current Code. In such cases, depending upon the amount of the estate tax actually payable to New York and other states which do not have a Sop Tax conformed to the federal tax, the credit for state death taxes under Section 2011 of the current Code might not be subject to the limitations imposed by Section 2011(b)(1) of the current Code. Each case will require a separate calculation.
Endnotes
3. If one were to construe Sections 960 and 952 of the Tax Law as measuring the New York estate tax on the estate of a non-domiciliary on a decedent’s entire gross estate, the Sections would be unconstitutional. Treichler v. Wisconsin, supra.
5. Section 3 of Article 16 of the New York State Constitution provides that intangible personal property shall be deemed located at the domicile of the owner for purposes of taxation.
6. This methodology was approved by the Internal Revenue Service in determining the credit for state death taxes to be allowed for federal estate tax purposes.
7. The correct result for a non-resident cannot be obtained by following the instructions for Form ET-706. It is suggested that the correct tax be shown on the face of the return and that the basis for its calculation be set forth in detail, including a reference to Revenue Ruling 56-230, in a rider to the return.

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