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A PRELIMINARY word on the scope of this review is in order. Since this was originally prepared as one of a series designed to acquaint returning veterans with legal developments during the war period, the year 1941 has been chosen as the starting point, and the review carried forward from that point through to date.[1] The review covering this period is limited to significant developments in the area of *federal taxation*, with emphasis upon the *estate*, *gift*, and *income taxes*.

The following outline indicates the pattern of the review:

I. General Survey of Revenue Legislation.

This part is intended as a panoramic but very brief survey, in chronological order, of the revenue acts for the period in question.

II. Topical Survey.

This will form the bulkiest part of the review. Here the attempt has been made to call attention to significant legislative, judicial, and administrative developments, broken down and integrated by reference to topic and subject matter. The treatment is necessarily sketchy. Nothing by way of complete analysis of these developments has been attempted. The coverage of judicial decisions is limited since the references to leading cases are confined almost entirely to decisions by the

* The writer is indebted to Mr. Milton D. Solomon of the New York Bar for his valuable assistance in the preparation of this review.

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[1] For excellent year-by-year reviews of developments in the field of federal taxation, see the chapters on "Federal Taxation" included in the ANNUAL SURVEY OF AMERICAN LAW published by New York University School of Law. The chapters for the years 1942 through 1944 were written by Professor Harry J. Rudick and for the year 1945 by Professor Gerald L. Wallace.

For a very readable and illuminating account of the revenue legislation for the war and reconversion periods, seen in the context of economic and political developments on both the domestic and international fronts, see chs. 9-17 of Book One of Randolph Paul's TAXATION FOR PROSPERITY (1947).

United States Supreme Court. Changes in administrative interpretations as reflected in the Treasury Regulations are noted only to the extent of calling attention to a few of the more conspicuous Treasury Decisions. The most the writer hopes to do in this part is to put the reader on notice and to give him the benefit of bibliographical references to which he may turn for extended treatment of the question. Indeed, this whole part may be characterized as an enlarged reference note.

III. Bibliographical Note.

IV. General Summary.

This part is designed as a critical survey of the general trends and accomplishments attributable to the period in question.

I

GENERAL SURVEY OF REVENUE LEGISLATION [2]

Revenue Act of 1941.[3] Designed to yield a net additional revenue in excess of $3,500,000, this act was limited almost entirely to changes by way of increases in the tax rate structure and the imposition of some new excises, including the extension of the retail sales tax to jewelry, furs and toilet items, the extension of the manufacturers' excise tax to cover ten new items, the imposition of a novel federal use tax on automobiles and boats, and the levying of an excise on amounts paid to carriers for the transportation of persons.

Revenue Act of 1942.[4] Acclaimed "the greatest tax bill in Ameri-

[2] The texts of the recent revenue acts are found in 26 U.S.C.A. (Internal Revenue Acts, beginning 1940).

The pamphlets on federal revenue acts prepared and distributed by Commerce Clearing House, Inc. and Prentice-Hall set forth in full the text of each of the acts and in addition incorporate helpful explanatory notes. Any student of the subject will find them very useful.

The very helpful legislative committee reports are cited in connection with the references below to each of the several revenue acts under consideration.

The best account of the revenue legislation during the war period is found in PAUL, TAXATION FOR PROSPERITY (1947), referred to in note 1, supra.

[3] Act of Sept. 20, 1941, 55 Stat. L. 687, c. 412, Pub. L. 250 (H.R. 5417), 77th Cong., 1st sess.; Rep. of House Ways and Means Comm., H. Rep. 1040; Rep. of Senate Finance Comm., S. Rep. 673; Conference Rep., H. Rep. 1203.

See PAUL, TAXATION FOR PROSPERITY 76-80 (1947).

[4] Act of Oct. 21, 1942, 56 Stat. L. 798, c. 619, Pub. L. 753 (H.R. 7378), 77th Cong., 2d sess.; Rep. of House Ways and Means Comm., H. Rep. 2333; Rep. of Senate Finance Comm., S. Rep. 1631; Conference Rep., H. Rep. 2586.

For treatments of this act, or phases of it, see the following: PAUL, TAXATION FOR PROSPERITY, c. 12 (1947); Kauper, "The Revenue Act of 1942: Federal Estate and Gift Taxation," 41 MICH. L. REV. 369 (1942); Kent, "The Revenue Act of 1942," can history," this measure was indeed one of the most important and comprehensive achievements by way of revenue legislation that this country has ever known. By the time this act was passed, the United States was deeply immersed in the war effort. Further increases in income tax, corporate excess profits tax and miscellaneous excise rates, along with a new excise on amounts paid carriers for transportation of property, reflected the imperative need for providing greater revenues and also combatting inflationary tendencies. But of even greater importance, as more enduring achievements, were the numerous code amendments, some of which were designed to change the substantive law by either broadening or limiting its reach while others were intended to clarify provisions that had created controversy and litigation. Also important were the amendments amplifying the relief provisions of the corporate excess profits tax law.

Current Tax Payment Act of 1943.[5] The raising of income-tax rates to an all-time high, coupled with the lowering of personal exemptions, added millions of new names to the federal tax lists. Problems of tax collection and of keeping the taxpayer current in his account with the government by correlating tax liability and payment with the earning of income came to the forefront. A popular movement headed by Beardsley Ruml led to the enactment of this legislation which introduced the now familiar system of withholding at the source and incorporated the unique forgiveness provision which had the effect of dropping one year out of personal income tax accounting and putting the taxpayer on a pay-as-you-go basis.

Revenue Act of 1943.[6] This act which covered a medley of matters,

43 COL. L. REV. 1 (1943); Nichols, "The Revenue Act of 1942," 23 BOST. UNIV. L. REV. 1 (1943); Rottschaefer, "The Revenue Act of 1942," 27 MINN. L. REV. 217 (1943); "Aspects of Personal Income Taxation and the 1942 Revenue Revision," 52 YALE L. J. 355 (1943); "Some Aspects of the Revenue Act of 1942," 56 HARV. L. REV. 428 (1942); "The Estate and Gift Tax Amendments: Revenue Act of 1942," 31 CAL. L. REV. 60 (1942).

[5] Act of June 9, 1943, 57 Stat. L. 126, c. 120, Pub. L. 68 (H.R. 2570), 78th Cong., 1st sess.; Rep. of House Ways and Means Comm., H. Rep. 401; Rep. of Senate Finance Comm., S. Rep. 221.

For discussion of this act, see PAUL, TAXATION FOR PROSPERITY, c. 13 (1947); Miller, "The Current Tax Payment Act," 19 IND. L. J. 99 (1944).

[6] Act of Feb. 25, 1944, 58 Stat. L. 21, c. 63, Pub. L. 235 (H.R. 3687), 78th Cong., 2d sess.; Rep. of House Ways and Means Comm., H. Rep. 871; Rep. of Senate Finance Comm., S. Rep. 627; Conference Rep., H. Rep. 1079.

For discussions of this act, see PAUL, TAXATION FOR PROSPERITY, c. 14 (1947); Fahey, " 'Relief' Provisions in the Revenue Act of 1943," 53 YALE L. J. 459 (1944); Neuhoff, "The Revenue Act of 1943: A Quick View of Its Income and Excess Profits Tax Provisions of General Interest to Corporations," 28 MINN. L. REV. 287 (1944); Paul, "The 1943 Revenue Bill," 19 IND. L. J. 85 (1944).

stepped up the corporate excess profits tax rate to 95%, increased numerous miscellaneous excise rates, clarified and restated the code on a few matters and created tax relief and advantages for certain classes of taxpayers. Inclusion of the latter features aroused the opposition of the late President Roosevelt who denounced the bill in a blistering veto message. Congress' reaction to the President's message was to pass the bill over his veto.

Individual Income Tax Act of 1944.[7] As indicated by its title, this act was concerned with personal income taxes and was addressed to problems of tax computation and collection. Kinks that had developed in the withholding-at-source collection system were straightened out, and the taxpayer's problem in computing income taxes was simplified. The act set up a new simplified tax table for use by taxpayers in the lower income brackets, created a new uniform per capita exemption, and introduced the "optional standard deduction" and "adjusted gross income" concepts.

The Tax Adjustment Act of 1945.[8] Reflecting the end of the war with Germany and the anticipated termination of the conflict with Japan, this act was designed to improve the cash position of corporate taxpayers in order to enable them to weather more successfully the difficulties expected to arise from the liquidation of government contracts and the whole process of reconversion. To achieve this purpose the act gave corporate taxpayers the privilege of applying the post war excess profits credit against current tax liability, provided for acceleration of refunds based on carry-backs of unused excess-profits credit, again in such a way as to reduce the cash requirements in meeting current tax liability, and speeded up the processing of applications for refunds based on the reduction of tax liability as a result of accelerated amortization of emergency facilities.

The Revenue Act of 1945.[9] In this act, popularly known as the

[7] Act of May 29, 1944, 58 Stat. L. 231, c. 210, Pub. L. 315 (H.R. 4646), 78th Cong., 2d sess.; Rep. of House Ways and Means Comm., H. Rep. 1365; Rep. of Senate Finance Comm., S. Rep. 885.

For discussions of this act, see PAUL, TAXATION FOR PROSPERITY, c. 15 (1947); Rottschaefer, "The Individual Income Tax Act of 1944," 29 MINN. L. REV. 94 (1945).

[8] Act of July 31, 1945, 59 Stat. L. 517, c. 340, Pub. L. 172 (H.R. 3633), 79th Cong., 1st sess.; Rep. of House Ways and Means Comm., H. Rep. 849; Rep. of Senate Finance Comm., S. Rep. 458.

For a discussion of this act, see PAUL, TAXATION FOR PROSPERITY, c. 16 (1947).

[9] Act of November 8, 1945, 59 Stat. L. 556, c. 453, Pub. L. 214 (H.R. 4309), 79th Cong., 1st sess.; Rep. of House Ways and Means Comm., H. Rep. 1106; Rep. of Senate Finance Comm., S. Rep. 655; Conference Rep., H. Rep. 1165.

For a discussion of this act, see PAUL, TAXATION FOR PROSPERITY, c. 17 (1947).

1946 Tax Reduction Law, Congress responded to the general demand for relief from the burdensome taxes of the war years. Both normal and surtax rates on individual incomes were reduced, the wartime corporate excess profits tax was repealed for tax years commencing after December 31, 1945, but with a retention for a one-year period of the unused credit carry-back privilege, corporate surtax rates were reduced, those twin nuisances—the declared value excess profits tax and the capital stock tax—were repealed, and the excise on use of motor vehicles and boats was eliminated.

II

TOPICAL SURVEY[10]

A. *The Federal Estate Tax*

1. *The Rate Structure* (I.R.C., §§ 810, 935)

The 1941 Revenue Act[11] provided for substantial rate increases with respect to the additional estate tax imposed by section 935 of the code.

[10] The following outline will serve to indicate the division of subject matter in this part and the sequence of treatment:

A. The Federal Estate Tax
   1. The Rate Structure
   2. Gross Estate Inclusions
   3. Deductions and Credits
   4. Burden of the Tax
B. The Federal Gift Tax
   1. The Rate Structure
   2. Taxable Transfers
   3. Exclusions from Value—Exceptions
C. Federal Income Taxes
   1. Taxes on Income of Individuals
      (a) The rate structure
      (b) Withholding and collection of tax at the source
      (c) Declaration and payment of estimated tax
      (d) Tax simplification *
   2. Taxes on Corporate Income
   3. Gross Income—Inclusions and Exclusions
   4. Deductions
   5. Accounting
   6. Sales and Exchanges
   7. Corporate Distributions and Reorganizations
   8. Taxable Persons
      (a) Corporations
      (b) Husband—wife
      (c) Trusts
D. The Role of the United States Tax Court.

* The discussion of the remaining topics under TOPICAL SURVEY will appear in the May, 1947 issue of the REVIEW.

[11] Sec. 401(a), amending I.R.C., § 935(b).

The 1942 Revenue Act[12] eliminated the special $40,000 exemption for proceeds of life insurance payable to specific beneficiaries and increased the general exemption for purposes of the additional estate tax to $60,000.

2. *Gross Estate Inclusions*

(a) *Decedent's interest* [I.R.C., § 811(a)]

Helvering v. Safe Deposit & Trust Co. of Baltimore[13]—property subject to decedent's testamentary power of disposition held not included under this subsection. The specific treatment of powers under section 811(f) was found to warrant a restricted interpretation of subsection (a).

(b) *Transfers in contemplation of death* [I.R.C., § 811(c)]

See *City Bank Farmers Trust Co. v. McGowan*[14] and *Allen v. Trust Co. of Georgia*.[15] These two cases, while dealing with novel questions, added nothing essentially new to the "contemplation of death" concept.[16]

(c) *Transfers taking effect at death* [I.R.C., § 811(c)]

The ramifications of the *Hallock*[17] doctrine dominate the estate tax landscape during the period under review.[18] The Treasury carried

[12] Sec. 404(a), amending I.R.C. § 811(g), and § 414(a) amending I.R.C. § 935(c).

[13] 316 U.S. 56, 62 S.Ct. 925(1942), noted in 40 MICH. L. REV. 1270(1942), 21 N.C.L. REV. 99(1942), 27 MINN. L. REV. 96(1942).

[14] 323 U.S. 594, 65 S.Ct. 496(1945), noted in 43 MICH. L. REV. 1194(1945). Commissioner upheld on deficiency assessment based on inclusion in gross estate of inter vivos transfers made by court order of property owned by a person adjudicated to be incompetent, where it appeared that the transfers were made in anticipation of distribution at death.

[15] 326 U.S. 630, 66 S. Ct. 389(1946), noted in 44 MICH. L. REV. 876(1946). Here the decedent, in order to avoid estate tax, had relinquished a power to amend trusts created by him, but the relinquishment was held not taxable as a transfer in contemplation of death since the decedent at the time he originally created the trusts had no reason to believe that the reserved power would subject the transfer to estate tax liability.

[16] On the general subject see Pavenstedt, "Taxation of Transfers in Contemplation of Death: A Proposal for Abolition," 54 YALE L. J. 70 (1944). Cf. the restricted conclusive presumption recommended in 1 PAUL, FEDERAL ESTATE AND GIFT TAXATION, § 6.26(1942).

[17] Helvering v. Hallock, 309 U.S. 106, 60 S. Ct. 444(1940).

[18] On the general subject, see MONTGOMERY, FEDERAL TAXES ON ESTATES, TRUSTS AND GIFTS, 1945-1946, pp. 398-419; I PAUL, FEDERAL ESTATE AND GIFT TAXATION, § 7.23 (1942) and the valuable continuation in the 1946 Supplement

the doctrine to an extreme in taking the position that nearly every retention of any kind of a reversionary interest, however remote, subjected the corpus to inclusion in the transferor-decedent's gross estate. The Supreme Court's very important decision in *Fidelity-Philadelphia Trust Co. v. Rothensies*[19] (a *must* case) indicated that the Court had lost sight of the original rationale of the *Hallock* case.[20] The companion case of *Commissioner v. Field's Estate*[21] and the later case of *Goldstone v. United States*[22] marked further important contributions by the high court, although both these cases could be fitted into a conventional interpretation of the *Hallock* doctrine. Messrs. Paul[23] and Eisenstein[24] justify the result in the *Fidelity-Philadelphia Trust Co.* case on the ground that it marks an oblique but well warranted limitation on *May v. Heiner*.[25] Sensing the general confusion and uncertainty

under the same section number at pp. 170 et seq.; Alexander, "Possibilities of Reacquisition and the Federal Estate Tax," 1 TAX L. REV. 291(1946); Eisenstein, "The Hallock Problem: A Case Study in Administration," 58 HARV. L. REV. 1141(1945); Eisenstein, "The Hallock Problem in a Nutshell," N.Y. UNIV. FOURTH ANNUAL INST. ON FED. TAX. 205(1946); Eisenstein, "Another Glance at the Hallock Problem," 1 TAX L. REV. 430(1946); Johnson, "Estate Tax on Inter Vivos Trusts," 1 TAX L. REV. 95(1945); Nelson, "Reverters in Estate Taxation, 23 TAXES 98(1945); Nelson, "The Stinson Case," 23 TAXES 245(1945); Spencer, "The Federal Estate Tax on Inter Vivos Trusts: A Common Sense Rule for Hallock Cases," 59 HARV. L. REV. 43(1945).

[19] 324 U.S. 108, 65 S.Ct. 508(1945), noted in 45 COL. L. REV. 469 (1945), 44 MICH. L. REV. 673(1946). Decedent had retained a life estate in property transferred in trust prior to March 3, 1931. Upon termination of the life estate, the income was payable in equal amounts to the decedent's daughters. If either daughter died, that part of the corpus supporting her income was to go to her descendants. If both of the daughters died without issue, the corpus was to be paid to such persons as decedent appointed by will; if no appointment was made, the corpus was to go to certain charities. Both daughters survived the decedent, and both had issue. The entire corpus of the inter vivos trust was held taxable as part of the decedent's gross estate since the settlor by means of the reserved power of appointment had retained a reversionary interest and since the interest of the beneficiaries depended on survivorship of the decedent.

[20] The case is thoroughly discussed in the texts and articles cited in note 18, supra.

[21] 324 U.S. 113, 65 S.Ct. 511(1945). In this case the trust which had been created before March 3, 1931, was to continue for the lives of two nieces of the decedent with the income payable to the decedent during his lifetime and then to other beneficiaries. In the event the trust terminated during the decedent's lifetime, the corpus was to be paid to him, but if the trust terminated subsequent to his death, the corpus was to be paid to the other beneficiaries. The entire corpus was held taxable.

[22] 325 U.S. 687, 65 S. Ct. 1323(1945). Where decedent retained reversionary interest in life insurance and annuity policies, proceeds held taxable as part of his estate notwithstanding that wife who was named as beneficiary and who was vested with incidents on ownership in policies could at any time have exercised her powers to destroy decedent's retained interest.

[23] FEDERAL ESTATE AND GIFT TAXATION, 1946 Supp., § 7.23 at pp. 198-200.

[24] "The Hallock Problem: A Case Study in Administration," 58 HARV. L. REV. 1141 at 1168-1171 (1945).

[25] 281 U.S. 238, 50 S. Ct. 286 (1930). Held in this case that the retention by

that had developed, the Treasury, in an attempt to dispel the deepening fog, issued on May 1, 1946, its T.D. 5513, amending section 81.17 of Treasury Regulations 105 and purporting to state both in terms of general standards and by means of illustrative cases an authoritative interpretation of the *Hallock* doctrine. This Treasury Decision [26] while marking a retreat by the department from its earlier extreme position and even a voluntary relinquishment of the fruit of its victory in the *Goldstone* case, represents an attempt to synthesize the results of both the *Hallock* and the *Fidelity-Philadelphia Trust Co.* decisions. This area of the law is still heavy with obscurity, and any student of the subject must keep a close watch for further developments.

(d) *Revocable transfers* [I.R.C., § 811(d)]

Commissioner v. Holmes' Estate [27]—transfer in trust before June 22, 1936, held taxable under section 811(d) (1) where decedent had retained the power to *terminate* the trust. The importance of the case lies in its holding that the 1936 amendment was simply declaratory of existing law.

(e) *Joint and community interests* [I.R.C., § 811(e)]

The 1942 Revenue Act [28] amended this subsection to require inclusion in the decedent's estate of community property except such part thereof as may be shown to have been received as compensation for personal services actually rendered by the surviving spouse or originally derived from such compensation or from separate property of the surviving spouse. In any event there is required to be included in the deceased spouse's gross estate the value of such part of the community property as was subject to the decedent's power of testamentary disposition. The general effect of this amendment was to place community property in the same category as joint interests and estates by the entireties for estate tax purposes.[29] Constitutional objections were urged,

the decedent of a life estate was not sufficient to make the inter vivos transfer taxable as one intended to take effect in possession or enjoyment at or after death. See Gillette, "A Re-examination of May v. Heiner," 24 TAXES 821 (1946).

[26] See Nelson, "The New Reverters Regulations," 24 TAXES 848 (1946); Platt, "The New Hallock Regulation," 2 TAX L. REV. 94 (1946).

[27] 326 U.S. 480, 66 S. Ct. 257 (1946), noted 45 MICH. L. REV. 236 (1946). On the general subject see James, "Family Trusts and Federal Taxes," 9 UNIV. CHI. L. REV. 427 (1942).

[28] Sec. 402(b), amending I.R.C., § 811(e).

[29] For discussions of the 1942 amendments, see Freeman and Mueller, "Federal Taxation of Community Property," 34 CAL. L. REV. 398 (1946); Jackson, "The New Federal Estate and Gift Taxes on Community Property," 21 TAXES 535 (1943); "The Estate and Gift Tax Amendments: Revenue Act of 1942," 31 CAL. L. REV. 60

as was to be expected, but the Supreme Court promptly and completely disposed of them in the case of *Fernandez v. Wiener.*[80]

(f) *Powers of appointment* [I.R.C., § 811(f)]

For decisions under the law prior to the 1942 amendments, see *Helvering v. Safe Deposit & Trust Co. of Baltimore*[81] and *Rogers' Estate v. Commissioner.*[82] In the former the Court gave effect to a compromise agreement in determining the applicability of the powers subsection. The decision in the *Rogers* case indicated a limitation on the doctrine of *Grinnell v. Helvering,*[83] respecting the effect of an exercise of a power in favor of persons otherwise taking by default.

The 1942 Revenue Act[84] resulted in complete revision of the powers subsection. Whereas the law formerly[85] required inclusion in the gross estate only of property passing by an exercise of a general power of appointment, the law as amended[86] now requires inclusion in the

(1942); Pedersen, "Application of Federal Income, Estate and Gift Tax Laws to Community Property," 45 MICH. L. REV. 409 (1947); Taylor, "Comments on the Federal Estate and Gift Tax Provisions Re Community Property," 19 CAL. S.B.J. 106 (1944); Winstead, "Constitutionality of Federal Taxation of Community Property," 24 TEX. L. REV. 34 (1945).

For earlier discussion, see Mitchell, "Federal Taxation in Recent Contact with California Community Property," 14 So. CAL. L. REV. 390 (1941); Ray, "Proposed Changes in Federal Taxation of Community Property: Estate and Gift Taxes," 30 CAL. L. REV. 527 (1942).

[80] 326 U.S. 340, 66 S. Ct. 178 (1945), noted in 44 MICH. L. REV. 671 (1946). See de Funiak, "Community Property and Law Schools," 20 CAL. S.B.J. 398 (1945); Freeman and Mueller, "Federal Taxation of Community Property," 34 CAL. L. REV. 398 (1946); Friedland, "Community Estates—Problems Raised by the Decision in Wiener and Herbst," 24 TAXES 194 (1946); Pedersen, "Application of Federal Income, Estate and Gift Tax Laws to Community Property," 45 MICH. L. REV. 409 (1947); Winstead, "Aftermath of Herbst and Wiener Decisions," 24 TEX. L. REV. 439 (1946).

[81] 316 U.S. 56, 62 S. Ct. 925 (1942), noted in 40 MICH. L. REV. 1270 (1942), 27 MINN. L. REV. 96 (1942), 21 N.C. L. REV. 99 (1942). See Paul's discussion of the case which he characterizes as one "unusually conspicuous for its yield of obscurity" in his FEDERAL ESTATE AND GIFT TAXATION, 1946 Supp., § 9.16 at pp. 225-229.

[82] 320 U.S. 410, 64 S. Ct. 172 (1943), noted in 53 YALE L. J. 572 (1942).

[83] 294 U.S. 153, 55 S. Ct. 354 (1935).

[84] Sec. 403(a), amending code § 811(f).

[85] For treatment of questions under the earlier law, see 1 PAUL, FEDERAL ESTATE AND GIFT TAXATION, §§ 9.01 through 9.27 (1942), and the 1946 Supp. under the same section numbers; Angell, "The Impact of the Law of Powers Upon our Internal Revenue Laws," 39 MICH. L. REV. 1269 (1941); Griswold, "Powers of Appointment and the Federal Estate Tax," 52 HARV. L. REV. 929 (1939); Schuyler, "Powers of Appointment and Especially Special Powers: The Estate Taxpayer's Last Stand," 33 ILL. L. REV. 771 (1939); Thompson, "State Death Taxes and Powers of Appointment," 26 IOWA L. REV. 549 (1941); "Taxation—Inheritance and Estate Taxes—Powers of Appointment," 39 MICH. L. REV. 302 (1940).

[86] For a discussion of the 1942 Amendments see PAUL, FEDERAL ESTATE AND

gross estate of all property with respect to which the decedent has at the time of his death "a power of appointment."[37] The "passing" and "exercise" requirements are eliminated. Power of appointment is defined to exclude two specifically defined classes of special powers.[38] Effective date provisions detailed by the 1942 act,[39] together with a provision permitting a tax-free release of certain powers within a limited period,[40] served to preclude a harsh retroactive effect of the amendment.

(g) *Proceeds of life insurance* [I.R.C., § 811(g)]

Capitalizing on the memorable decisions of the Court of Claims in the thrice argued *Bailey* case,[41] the Treasury Department by T.D. 5032,[42] issued January 10, 1941, amending the then current Estate Tax Regulations, reverted to its position taken in earlier years in stating the rule that life insurance payable to specific beneficiaries was "taken out" by the decedent and hence taxable as part of his gross estate under the language of the earlier law, to the extent that the decedent had paid the premiums therefor.[43] To avoid retroactive application of this interpretation, the amended Regulations were made to turn on January 10,

GIFT TAXATION, 1946 Supp. §§ 9.28 et seq.; Alexander, "Taxation of Powers of Appointment under the Revenue Act of 1942," 56 HARV. L. REV. 742 (1943); Austin, "Taxing Appointive Property," 30 IOWA L. REV. 17 (1944); Eisenstein, "Powers of Appointment and Estate Taxes," 52 YALE L. J. 296, 494 (1943); Kauper, "The Revenue Act of 1942: Estate and Gift Tax Amendments," 41 MICH. L. REV. 369 at 374-379 (1942).

[37] I.R.C., § 811(f) (1).

[38] I.R.C., § 811(f) (2).

[39] Sec. 403(d) (1) and (2).

[40] Sec. 403(d) (3). The crucial date of January 1, 1943, specified by the 1942 act was thereafter successively extended by various acts of Congress to July 1, 1947. See Nossaman, "Release of Powers of Appointment," 56 HARV. L. REV. 757 (1943); Simes, "Trusts and Estates—Trends in the Law: 1941-1945," 44 MICH. L. REV. 833 at 834-835 (1946).

[41] Bailey v. United States, (Ct. Cl. 1939) 27 F. Supp. 617, rehearing (Ct. Cl. 1939) 30 F. Supp. 184, second rehearing (Ct. Cl. 1940) 31 F. Supp. 778.

[42] 1941: 1 CUM. BULL. 427.

[43] For a thorough discussion of the law prior to the 1942 amendments see 1 PAUL, FEDERAL ESTATE AND GIFT TAXATION, §§ 10.01 through 10.29 (1942) and 1946 Supp. under the same section numbers. Also see the following comments: "Federal Estate Tax—Inclusion of Proceeds of Life Insurance Policies in Gross Estate," 24 MINN. L. REV. 963 (1940); "Federal Estate Taxation of Life Insurance—Effect of Treasury Decision 5032 Amending Articles 25 and 27 of the Estate Tax Regulations," 40 MICH. L. REV. 1221 (1942); "Insurance: Estate Taxation: The Bailey Case," 25 CORN. L. Q. 605 (1940); "Life Insurance and the Federal Estate Tax," 40 COL. L. REV. 86 (1940).

1941, as the pivotal date so that where the insured had divested himself of all incidents of ownership before that date, the proceeds were taxable upon his death only to the extent of premiums paid after January 10, 1941. The validity of this amendment has been sustained in the well-reasoned opinion of the federal district court in the case of *Colonial Trust Co. v. Kraemer.*[44]

Less than two years had elapsed after the issuance of T.D. 5032 before Congress, by means of amendments included in the 1942 Revenue Act,[45] completely overhauled the insurance subsection and thus discharged a task long overdue.[46] As amended the law now requires inclusion of life insurance proceeds payable to specific beneficiaries either (1) if the decedent paid the premiums directly or indirectly and in proportion to the amounts so paid, or (2) if the decedent at his death possessed any of the incidents of ownership (excluding, however, a reversionary interest).[47] It will be seen that the law as amended goes further than T.D. 5032 which discarded the incident of ownership test and made taxability hinge upon payment of premiums by the decedent. While the amendment was made applicable to estates of person's dying after the enactment date of the 1942 act (October 21, 1942), special provision was made to limit the applicability of the new law to policies taken out at an earlier date in such a way as to avoid any harsh retroactivity.[48] For this purpose an interesting use is made of the January 10, 1941 date which occupied such a crucial place in T.D. 5032.

3. *Deductions and Credits*

(a) *Claims* [I.R.C., §812(b)]

The 1942 Revenue Act[49] amended this subsection to allow a deduction for amounts paid by executors in discharge of unpaid pledges to charities made by decedent during his life, thereby correcting the inequitable result of the *Taft*[50] case which had held that such a claim was not founded on adequate consideration in money or money's worth.

[44] (D.C. Conn. 1945) 63 F. Supp. 866.

[45] Sec. 404(a), amending I.R.C., § 811(g). See Kauper, "The Revenue Act of 1942: Estate and Gift Tax Amendments," 41 MICH. L. REV. 369 at 379-384 (1942).

[46] For a thorough treatment of the law as amended, see PAUL, FEDERAL ESTATE AND GIFT TAXATION, 1946 Supp., § 10.30 et seq.

[47] I.R.C., § 811(g).

[48] Revenue Act of 1942, § 404(c).

[49] Sec. 406(a), amending I.R.C., § 812(b).

[50] Taft v. Commissioner, 304 U.S. 351, 58 S. Ct. 891 (1938), noted in 37 MICH. L. REV. 152 (1938), 16 TEX. L. REV. 427 (1938), 24 VA. L. REV. 453 (1938), 47 YALE L. J. 494 (1938).

This same subsection was further amended by the 1942 act[51] to bar the deductibility of claims to the extent that they exceed the value of property subject to payment of claims, thereby correcting the anomalous result under the earlier law whereby the gross estate determined by reference to inter vivos transfers and life insurance proceeds was reduced by the face amount of claims not actually paid in full.[52]

(b) *Property previously taxed* [I.R.C., § 812(c)]

The 1942 Revenue Act[53] amended the complex provisions of this subsection to correct technical defects in the earlier law.[54]

(c) *Transfers for public, charitable and religious uses* [I.R.C., § 812(c)]

Merchants National Bank v. Commissioner[55]—remainder to charity held not deductible where trustee given discretionary power to invade corpus "for the comfort, support, maintenance and/or happiness" of the life tenant.

Harrison v. Northern Trust Co.[56]—where decedent made bequest of residuary estate to charity, deduction held limited to actual amount of such bequest after payment of the federal estate tax.

The 1942 Revenue Act[57] extended deductions for transfers to charity to include any interest falling into the transfer as the result of an irrevocable disclaimer of a bequest, legacy, etc.

(d) *Credit for state death taxes* [I.R.C., § 813(b)]

The 1942 Revenue Act[58] amended this subsection to permit a credit for state death to the extent of 80% of the full basic estate tax *unreduced by gift tax credit.*

[51] Sec. 405(a), amending I.R.C., § 812(b).

[52] See, for instance, Commissioner v. Windrow, (C.C.A. 5th, 1937) 89 F. (2d) 69, and the discussions in 14 MINN. L. REV. 428 (1930), 5 UNIV. CHI. L. REV. 154 (1937), 76 UNIV. PA. L. REV. 989 (1928).

[53] Sec. 407(a) (1) (2), amending I.R.C., § 812(c).

[54] For explanation of the changes, see the committee reports: H. Rep. 2333, 77th Cong., 2d sess. (1942), pp. 165-166, and S. Rep. 1631, 77th Cong., 2d sess. (1942), pp. 238-240.

[55] 320 U.S. 256, 64 S. Ct. 108 (1943), noted in 42 MICH. L. REV. 1142 (1944). On the general subject of charitable deductions see the comments in 30 CAL. L. REV. 556 (1942), 29 IOWA L. REV. 611 (1944), 28 VA. L. REV. 387 (1942).

[56] 317 U.S. 476, 63 S. Ct. 361 (1943), noted in 41 MICH. L. REV. 1001 (1943).

[57] Sec. 408(a), amending I.R.C., § 812(d).

[58] Sec. 410, amending I.R.C., § 813.

4. *Burden of the Tax*

The 1942 Revenue Act[59] amended section 826(c), relating to the executor's right to recover from life insurance beneficiaries an aliquot part of the estate tax, unless decedent directs otherwise in his will, and added subsection (d) to section 826 to state the same general rule with respect to appointive property included in the gross estate.

Riggs v. Del Drago[60]—New York statute providing that, except as otherwise directed by decedent's will, the burden of any federal death taxes paid by executor or administrator shall be spread proportionately among the distributees or beneficiaries of the estate, held constitutional.

B. *The Federal Gift Tax*

1. *The Rate Structure* [I.R.C., §§ 1001, 1003, 1004]

The 1941 Revenue Act[61] substantially increased the rates.

The 1942 Revenue Act[62] reduced the specific exemption from $40,000 to $30,000 and also[63] reduced from $4,000 to $3,000 the amount of the exclusion from value of gifts to individual donees in a calendar year.

2. *Taxable Transfers*

(a) *What is a gift?—Relevancy of donative intent and nature of consideration* [I.R.C., §§ 1000 and 1002]

Wemyss v. Commissioner[64]—transfer in consideration of transferee's promise to marry, where by remarriage transferee forfeited income from testamentary trust created by her former husband, held taxable in its entirety as transfer by gift. Both the Regulations excluding donative intent as a controlling element and the Tax Court's findings on nature and value of consideration were sustained.

Merrill v. Fahs[65]—transfer in consideration of transferee-wife's relinquishment of dower rights held taxable in its entirety as transfer by gift. This case is significant on the question of correlation of the estate and gift taxes.

[59] Secs. 404(b) and 403(c).

[60] 317 U.S. 95, 63 S. Ct. 109 (1942). On the subject generally see Karch, "Apportionment of Death Taxes," 54 HARV. L. REV. 10 (1940); Comments, 27 CORN. L. Q. 280 (1942), 51 YALE L. J. 1202 (1942), 40 COL. L. REV. 690 (1940).

[61] Sec. 402(a), amending I.R.C., § 1001.

[62] Sec. 455, amending I.R.C., § 1004.

[63] Sec. 454, adding I.R.C., § 1003(b) (3).

[64] See Wolfe, "Something New in Gift and Estate Taxes," 25 TAXES 217 (1947); 324 U.S. 303, 65 S. Ct. 652 (1945), noted in 1 TAX L. REV. 107 (1945).

[65] 324 U.S. 308, 65 S. Ct. 655 (1945). See Rand, "What is a Gift," 34 KY. L. J. 99 (1946).

(b) *Types of transfers*

(1) *Powers of appointment* [I.R.C., § 1000(c)]

The 1942 Revenue Act[66] added subsection (c) to section 1000 to tax the exercise or release of a power of appointment as a transfer of the appointive property. This amendment served to correlate the gift tax treatment of appointive property with the treatment under the estate tax law as amended by the same act.[67]

(2) *Community property* [I.R.C., § 1000(d)]

The 1942 Revenue Act[68] added subsection (d) to section 1000 to state the rule that transfers of community property shall be considered transfers of the husband's property except to the extent that the property transferred is derived from the wife's earnings or from her separate property. This amendment served to correlate the gift tax treatment of appointive property with the treatment under the estate tax law as amended by the same act.[69]

(3) *Life insurance policies*

Guggenheim v. Rasquin[70]—in the case of single premium insurance policies transferred at time of issuance, cost rather than cash surrender value held to determine their value for gift tax purposes.

United States v. Ryerson[71]—where policies transferred subsequent to issuance, value for gift tax purpose held determined by replacement value.

(c) *Completeness of gift*

(1) *Retention of reversionary interest.*[72] *Smith v. Shaughnessy*—where transferor retained a reversionary interest such as would bring the transfer into gross estate under the *Hallock* rule, transfer held nevertheless taxable as a completed gift subject to allowance of deduction for ascertainable value of reversionary interest; theory of mutual

[66] Sec. 452(a), amending I.R.C., § 1000.

[67] See the discussion in PAUL, FEDERAL ESTATE AND GIFT TAXATION, 1946 Supp., §§ 9.40 et seq., and also the articles on the 1942 amendments cited in note 35, supra.

[68] Sec. 453, amending I.R.C., § 1000.

[69] See the discussion in PAUL, FEDERAL ESTATE AND GIFT TAXATION, 1946 Supp., § 16.17, beginning at p. 718. Also see Altman, "Community Property and the Gift Tax," 21 TAXES 429 (1943) and the articles cited in note 28, supra.

[70] 312 U.S. 254, 61 S. Ct. 507 (1941).

[71] 312 U.S. 260, 61 S. Ct. 479 (1941).

[72] 318 U.S. 176, 63 S. Ct. 545 (1943), noted in 56 HARV. L. REV. 1010 (1943). See also the companion case, Robinette v. Helvering, 318 U.S. 184, 63 S. Ct. 540 (1943), where the Court found that the retained reversionary interest had no ascertainable value and hence allowed no deduction for the same.

exclusiveness of estate and gift taxes, as suggested by the *Sanford's Estate* case rejected, and gift tax in case like this viewed as partial prepayment of estate tax.[73]

(2) *Revocable transfer.* The 1943 Revenue Act[74] added subsection (e) to section 1000 in order to mitigate possibly harsh consequences of the decision in the *Sanford's Estate* case;[75] this amendment has the effect of relieving from further gift tax liability a final inter vivos relinquishment of control in respect to a transfer on which a gift tax was paid at an earlier date.[76]

3. *Exclusions From Value—Exceptions* [I.R.C., § 1003]

(a) *Transfers in trust.* The 1942 Revenue Act[77] repealed the limitation inserted in section 1003 by the 1938 Revenue Act denying the benefit of the exclusion from value provision to gifts in trust. This repeal has the effect of reinstating the rule of the *Hutchings* case[78] that value exclusions may be claimed in the case of a transfer in trust by reference to the gifts of each of the beneficial interests in the trust (subject to the limitation governing future interests).

(b) *Future interests in property.* See the following cases: *United States v. Pelzer;*[79] *Ryerson v. United States;*[80] *Fondren v. Commissioner;*[81] *Commissioner v. Disston.*[82] All these cases indicate clearly that the term "future interests in property," as used in the code to deny the benefit of the value exclusion to gifts of such interests, is not to be construed by reference to common law conceptions that may turn on the distinction between vested and contingent interests. On the contrary, this term assumes a broader significance as covering any interest which is limited or may be limited to commence in actual possession or enjoyment at a future date. Apparently any limitation, however tenuous, on

[73] See the discussion in PAUL, FEDERAL ESTATE AND GIFT TAXATION, 1946 Supp., § 17.15.

[74] Sec. 502(a), amending I.R.C., § 1000.

[75] 308 U.S. 39, 60 S. Ct. 51 (1939).

[76] See the discussion in PAUL, FEDERAL ESTATE AND GIFT TAXATION, 1946 Supp., § 17.07A.

[77] Sec. 454, amending I.R.C., § 1003(b) (2).

[78] Helvering v. Hutchings, 312 U.S. 393, 61 S. Ct. 653 (1941), noted in 39 MICH. L. REV. 1441 (1941), 25 MINN. L. REV. 803 (1941), 15 SO. CAL. L. REV. 122 (1941).

[79] 312 U.S. 399, 61 S. Ct. 659 (1941).

[80] 312 U.S. 405, 61 S. Ct. 656 (1941).

[81] 324 U.S. 18, 65 S. Ct. 499 (1945).

[82] 325 U.S. 442, 65 S. Ct. 1328 (1945).

For a discussion of these and related cases, see Bizar, "Future Interests—Gift Taxes," 24 TAXES 621 (1946).

present enjoyment, is a sufficient basis for denying the benefit of the exclusion.

C. *Federal Income Taxes*

1. *Taxes on Income of Individuals*

(a) *The Rate Structure* [I.R.C., §§11 and 12]. The 1941 Revenue Act[83] while retaining the normal tax rate of 4% moderately increased the surtax so that the rates ranged from 6% on income in the $2000 bracket to 77% on the part of income in excess of $5,000,000. Actually the impact of surtaxes became heavier than the rate changes indicated since the new rates were made applicable to the first dollar of surtax net income whereas the earlier law had recognized a $4000 cushion, i.e., the first $4000 of surtax net income had been nontaxable. Under the 1941 act[84] personal exemptions were reduced to $750 in the case of single persons and $1500 in the case of married persons and heads of families.

The 1942 Revenue Act increased the normal tax rate to 6%,[85] added the victory tax of 5% on "Victory tax net income"[86] and drastically increased the surtax rates.[87] The new surtax rates ranged from 13% on $2,000 of surtax net income to 82% on the part of such income in excess of $200,000. Simultaneously exemptions were reduced to $500 for single persons and to $1200 for husband and wife and heads of families,[88] while the exemption for dependents was reduced from $400 to $350.[89] The effect of these changes was to make the income tax bear much more heavily on persons in the lower income group.

The 1943 Revenue Act reduced the victory tax rate to 3%.[90] This law also repealed the earned income credit.[91]

The Individual Income Tax Act of 1944 resulted in extensive changes. The victory tax was repealed[92] but in effect was carried forward in the normal tax which was reduced to 3%[93] The former normal tax rate was absorbed by the surtax rates which were increased and

[83] Sec. 101, amending I.R.C., § 12(b).

[84] Sec. 111, amending I.R.C., § 25(b) (1).

[85] Sec. 102, amending I.R.C., § 11.

[86] Sec. 172, amending the code by inserting the new subchapter D at the end of chapter 1.

[87] Sec. 103, amending I.R.C., § 12(b).

[88] Sec. 131(a) (1), amending I.R.C., § 25(b) (1).

[89] Sec. 131(b), amending I.R.C., § 25(b) (2) (A).

[90] Sec. 106(a), amending I.R.C., § 450.

[91] Sec. 107(a), repealing I.R.C., § 25(a) (3) and (4) and §§185 and 47(d).

[92] Sec. 6(a), repealing I.R.C., subchapter D of chapter 1.

[93] Sec. 3, amending I.R.C., § 11.

which, as thus increased, ranged from 20% on the first $2000 of income to 91% on the part of income in excess of $200,000.[94] Personal exemptions were also revised. For normal tax purposes an exemption of $500 was allowed for a single person, $500 for head of family, and $500 for a married person with a further provision for an additional exemption for the spouse in case a joint return was filed but not to exceed $500 or the amount of the spouse's separate income whichever was lower; no normal tax exemption was allowed for dependents.[95] In regard to surtaxes the 1944 act introduced the system of a uniform per capita exemption; under it each taxpayer was allowed an exemption of $500 plus added exemptions in like amount for his or her spouse and for each person defined as a dependent.[96]

The 1945 Revenue Act, effective with the calendar year 1946, signalized the first step in the post-war tax reduction program. Surtax rates were reduced three points in each bracket with the result that the new rates ranged from 17% on the first $2000 to 88% on surtax net income in excess of $200,000.[97] In addition to these rate reductions the law also provided for a flat 5% reduction of both normal and surtaxes.[98] For all practical purposes, therefore, the normal tax rate was reduced to 2.85% and the surtax rates to a minimum of 16.15% and a maximum of 83.6%. Moreover the uniform per capita exemption of $500 was made fully applicable to normal tax as well as surtax.[99] The net effect of all these changes was to write the special wartime victory tax out of the income tax rate structure.

By way of summary of developments in the rate structure during the period under review, it may prove interesting to compare the 1940 and the 1945 Revenue Acts. Under the 1940 act the normal tax rate was 4% as compared with the effective 2.85% under the present law. Surtax rates under the 1940 act ranged from 4% on surtax net income in the $4000 to $6000 bracket (the first $4000 were exempt from surtax) to 75% on the part of surtax net income in excess of $5,000,000. Under the 1945 act the surtax rates range from 17% on the first $2000 to 88% on the excess over $200,000, subject however to the 5% reduction referred to above. In place of the exemptions allowed under the 1940 act in the amount of $800 for a single person and

[94] Sec. 4(a), amending I.R.C., § 12(b).
[95] Sec. 10(a), amending I.R.C., § 25(a).
[96] Sec. 10(b), amending I.R.C., § 25(b).
[97] Sec. 101(b), amending I.R.C., § 12(b).
[98] Sec. 101(a), amending I.R.C., § 11, and § 101(b), amending code § 12 (b).
[99] Sec. 102, amending I.R.C., § 25(b).

$2000 for married persons and heads of families, together with $400 for each dependent, the law now authorizes a uniform $500 per capita exemption; however, the earned income credit which served the same purpose as an added exemption and which was still effective under the 1940 act is no longer authorized under the present law.

(b) *Withholding and collection of tax at the source* [I.R.C., §§ 1621-1627]. A large scale system of collecting income tax at the source was inaugurated under the 1942 Revenue Act which levied the special 5% victory tax, in addition to other income taxes, and required employers to withhold the victory tax at the source on wages paid on or after January 1, 1943.[100] Thereafter a popular campaign was instituted to extend collection at the source and the pay-as-you-go system to make it applicable to individual income taxes generally. In response to this campaign Congress enacted the Current Tax Payment Act of 1943 pursuant to which employees were required to make a 20% withholding beginning July 1, 1943.[101] Since the federal income tax had traditionally rested on a system of reporting and accounting whereby taxpayers were always a year in arrears in discharge of accrued tax liability, any attempt at correlation of withholding at source with the pay-as-you-go idea necessitated either double tax payment in the year when withholding first became effective (a program that would have entailed considerable hardship for taxpayers) or, in the alternative, an arrangement for forgiving in the year when withholding became effective the liability accrued for the previous year. Congress chose the latter alternative. Subject to limitations not necessary to develop in this review, the effect of section 6 of the 1943 Current Tax Payment Act was to forgive taxpayers their 1942 income tax liability. Instalments paid by taxpayers prior to July 1, 1943 on their 1942 liability, together with income tax withheld at the source beginning July 1, 1943, on the new 20% withholding basis, were applied against the current 1943 liability for which a final accounting was then required on or before March 15, 1944.

The 20% withholding required under the 1943 act was not completely satisfactory since the collection at the source authorized thereunder was not accurately geared to individual income tax liability. This was particularly the case with respect to persons in the higher

[100] Sec. 172(a), amending code by inserting the new subchapter D at end of chapter 1. The code sections dealing with the collection of the victory tax at source on wages were included under Part II of the new subchapter and began with § 465.

[101] Sec. 2(a), amending I.R.C. by inserting at end of chapter 9 the new subchapters D and E, comprising I.R.C., §§ 1621 through 1632.

salary brackets, since the applicable surtax rates exceeded 20% so that such taxpayers were still required to account for a substantial amount of unpaid income tax in their final accounting for the year in question. To correct this and other weaknesses in the withholding system Congress in the 1944 Individual Income Tax Act substantially revised the withholding system and set up a new schedule of withholding rates,[102] the general effect of which was to assure collection at the source of the entire income tax liability in cases of persons deriving all their income from service and not earning in excess of $5000. Under the 1945 Revenue Act the withholding rates were again revised,[103] this time downwards, to reflect the reduction in income tax rates.

(c) *Declaration and payment of estimated tax.* Inauguration of the tax withholding system did not eliminate the necessity of a final tax accounting for any given year. It simply required a current collection and payment by way of credit against the tax liability as ultimately determined on the final accounting by March 15th of the following year. Moreover, viewed as a collection and credit mechanism, collection of wages at the source does not establish a pay-as-you-go status for all taxpayers. Even with the 1944 modifications the withholding rates do not absorb the tax liability of salary earners in the high brackets. Furthermore, withholding at the source does not reach income other than salaries and wages. It was therefore a necessary part of any pay-as-you-go system to complement wage withholding with a requirement that taxpayers account directly to the collector for payment of current tax liability to the extent not accounted for by withholding. The 1943 Current Tax Payment Act achieved this related purpose in its provisions[104] requiring taxpayers on or before March 15th each year to file a return declaring estimated tax liability for the current year and showing the amount thereof remaining after subtracting estimated withholding during the year. This excess of estimated current liability is then required to be paid in four equal instalments of which the first is due when the estimate is filed. Penalties are provided to take care of taxpayers who underestimate in a substantial amount.[105]

(d) *Tax simplification* (I.R.C., §§ 400-404). Changes made in

[102] Sec. 22(b), amending I.R.C. § 1622(a) and (b) (1), and § 22(c), amending I.R.C., § 1622(c) (1).

[103] Sec. 104(a), amending I.R.C., § 1622(a), and § 104(b), amending I.R.C., § 1622(c) (1).

[104] Sec. 5(a), amending I.R.C. by striking out §§ 58, 59, and 60 and inserting new sections in lieu thereof.

[105] See the present I.R.C., § 294(d) (2).

the tax structure have added to the federal tax rolls millions of taxpayers in the lower income brackets. This, coupled with the ever increasing complexity of the income tax law, created a demand for some simplification of income tax returns and tax computations on the part of the average taxpayer. The 1941 Revenue Act[106] introduced the use of the simple optional rate schedule limited in its use to taxpayers whose gross income was $3000 or less and was derived solely from compensation for personal services, dividends, interest, rents, annuities or royalties. In preparation of this schedule allowance was made for an assumed standard deduction to cover such items as interest on indebtedness, taxes and contributions so that the taxpayer could easily determine his income tax liability by referring to the bracket in the tax table appropriate to his gross income and personal status. The 1942 Revenue Act[107] limited the optional tax privilege to cash-basis, calendar-year taxpayers and denied its use to taxpayers having gross income by way of rents or royalties. The 1943 Revenue Act[108] prescribed a new set of tables which reflected repeal of the earned income credit and eliminated the need for a separate computation of the victory tax. These tables carried the process of simplification still further through the use of a series of columns showing variations depending on the number of dependency credits claimed by the taxpayer. Further important changes were effected by the 1944 Individual Income Tax Act. It authorized a new simplified tax table for use by taxpayers with adjusted gross incomes of less than $5000, regardless of the nature of the income.[109] Furthermore, in connection with the introduction into the code of the "adjusted gross income" concept, this act gave taxpayers with adjusted gross income in excess of $5000 or more the privilege of electing to claim a "standard deduction" of $500 in lieu of actual deductions permitted under the code.[110] Taxpayers with adjusted gross income of less than $5000 receive the benefit of the standard deduction only if they elected to use the simplified tax table.

Under the Revenue Act of 1945 the optional simplified tax table was again revised to reflect the reduction in income tax rates.[111]

(To be continued.)

[106] Sec. 102(a), amending the I.R.C. by inserting after § 396 the new Supplement T comprising I.R.C., §§ 400 through 404.

[107] Sec. 104, amending I.R.C., §§ 400, 401 and 404.

[108] Sec. 102(a), amending I.R.C., § 400.

[109] Sec. 5(a), amending I.R.C., supplement T of chapter 1.

[110] Sec. 9(a), amending I.R.C., § 23 by adding the new subsection (aa).

[111] Sec. 103(a), amending I.R.C., § 400.