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August 10, 1971

DEPARTMENT OF LAW OPINION NO. 71-32 (R-77)

REQUESTED BY: GERALDINE C. SWIFT
Estate Tax Commissioner

QUESTION: If a decedent, a resident of another state, dies with an interest in real property in the State of Arizona which is encumbered with a mortgage and other liens which exceed the value of the property, may an estate tax be due the State of Arizona?

ANSWER: Yes.

The State of Arizona imposes an estate tax upon the transfer of the net estate of every decedent whether a resident or nonresident of this state. A.R.S. § 42-1509. The tax is determined by application of an appropriate rate against the net estate. A.R.S. § 42-1510. The net estate is computed by ascertaining the gross estate as provided in A.R.S. § 42-1511 less certain deductions and exemptions provided in A.R.S. § 42-1512.

In the case of a nonresident the net estate is computed by ascertaining the value of the Arizona property in which the decedent has an interest less a proportion of certain deductions, such as funeral expenses and claims against the estate and a \$100,000.00 exemption, in the ratio which the gross estate in Arizona bears to the value of the entire gross estate, wherever located, and less other enumerated exemptions. A.R.S. §§ 42-1512.C, 42-1512.D and 42-1512.E. Although a nonresident decedent's property in Arizona may be encumbered by a mortgage and other liens which exceed the value of the property, under the statutory definition of net estate, that nonresident decedent may have left a net estate in Arizona subject to the Arizona estate tax.

In considering the constitutionality of the Arizona estate tax law in the case of nonresidents, it is necessary to consider the nature of the law. As are all other estate tax laws, the tax is levied on the right to transfer property on death. In re Estate of Garcia, 9 Ariz.App. 587, 455 P.2d 269 (1969). The right to this tax exists in the state because the owner of the property needs the aid of

the state, its laws and courts to acquire and enforce his rights to his property. The state may demand a "quid pro quo" in return for its functions. Kelly v. Bastedo, 70 Ariz. 371, 220 P.2d 1069 (1950). The tax is levied upon the right to transfer property, and not on the property itself. It is an excise tax, not a property tax. Minot v. Winthrop, 162 Mass. 113, 38 N.E. 512, 26 L.R.A. 259 (1894); Cooley on Taxation, §§ 1721, 1722, 1723 and 1724.

In 1919 the United States Supreme Court was confronted with a situation in which the State of New Jersey based its tax on the proportion of a decedent's property located within that state to the entire estate. In Maxwell v. Bugbee, 250 U.S. 525, 40 S.Ct. 2, 263 L.Ed. 1124, the United States Supreme Court, in upholding that scheme, stated:

"It is not to be disputed that, consistently with the Federal Constitution, a State may not tax property beyond its territorial jurisdiction, but the subject-matter here regulated is a privilege to succeed to property which is within the jurisdiction of the State. When the State levies taxes within its authority, property not in itself taxable by the State may be used as a measure of the tax imposed. * * * In the present case the State imposes a privilege tax, clearly within its authority, and it has adopted as a measure of that tax the proportion which the specified local property bears to the entire estate of the decedent. That it may do so within limitations which do not really make the tax one upon property beyond its jurisdiction, the decisions to which we have referred clearly establish. The transfer of certain property within the State is taxed by a rule which considers the entire estate in arriving at the amount of the tax. It is in no just sense a tax upon the foreign property, real or personal. It is only in instances where the State exceeds its authority in imposing a tax upon a subject-matter within its jurisdiction in such a way as to really amount to taxing that which is beyond its authority, that such exercise of power by the State is held void. . . ." (Emphasis added.)

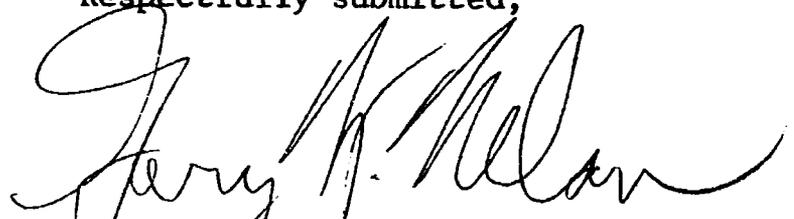
Opinion No. 71-32
(R-77)
August 10, 1971
Page Three

The Court of Appeals of North Carolina recently upheld the constitutionality of the North Carolina inheritance tax law which provided that all of the decedent's property, wherever located, is to be used in establishing the rate at which the decedent's estate is to be taxed. In that case, the North Carolina court, noting that at least ten other states use a similar scheme, traced the history of Maxwell v. Bugbee and several succeeding United States Supreme Court cases, which concerned the same or similar issues. It concluded the Maxwell case to still be the law. Rigby v. Clayton, 2 N.C.App. 57, 162 S.E.2d 682 (1968); aff'd 274 N.C. 465, 164 S.E.2d 7 (1968).

It is obvious under the Maxwell v. Bugbee doctrine that the Arizona statutory scheme for taxing the estates of non-residents is constitutional. But, even if Maxwell v. Bugbee were not the law, we must recognize that the Arizona tax is not measured by the value of property in other states. Instead, the value of property in other states is used to proportion the debts and other deductions to be deducted from the gross estate.

The state has the right to demand a "quid pro quo" from an estate, even one which may be fully encumbered. Mere consideration of the costs of the superior court in the administration of a decedent's estate, whether solvent or not, is enough to establish the right to a "quid pro quo". Therefore, it is our opinion that an estate tax may be due the State of Arizona in the case of a nonresident decedent who had an interest in real property in Arizona which is encumbered with a mortgage and other liens which exceed the value of the property.

Respectfully submitted,



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The Attorney General

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