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IN THE DISTRICT COURT OF LANCASTER COUNTY, NEBRASKA

NATIONAL BANK OF SOUTH DAKOTA )  
and JOHN H. LITZELMAN, Personal )  
Representative of the Estate )  
of Burl A. Litzelman, Deceased, )  
and DAVID DEROUCHÉY, )  
Plaintiffs )

Docket 370 Page 289

Dept. of Justice

vs.

AUG 1 1986

THE NEBRASKA DEPARTMENT OF )  
REVENUE and DONNA KARNES, )  
The Nebraska State Tax )  
Commissioner, )  
Defendants. )

State of Nebraska

A hearing was held in this matter on June 17, 1986 and briefs have now been received.

This action arises out of the determination of inheritance tax in the estate of Burl A. Litzelman, who died on August 5, 1981. Plaintiff David DeRouchéy, a beneficiary of the estate of Burl A. Litzelman, received a remainder interest in certain real estate which was subject to Nebraska inheritance tax. Plaintiffs brought this suit for declaratory judgment under Neb. Rev. Stat. §84-911 (Reissue 1981), contending that the six percent (6%) interest rate contained in regulations and tables adopted by the State Tax Commissioner in effect at that time to discount the remainder interest in the estate to present value for Nebraska inheritance tax purposes was in excess of the statutory authority granted the Commissioner under Neb. Rev. Stat. §77-2008 (Reissue 1981).

Section 77-2008, which pertains to the determination of inheritance tax for life estates and remainder interests, provides, in pertinent part:

The portion thereof allocable to the temporary estate and the portion thereof allocable to the vested remainder estate shall be computed in accordance with such regulations with respect thereto as the State Tax Commissioner, from time to time, shall promulgate and adopt, and the Tax Commissioner is hereby directed to promulgate and adopt, from time to time, and to furnish to each county judge regulations and tables with respect thereto, based upon sound actuarial principles and prevailing interest rates. (Emphasis added).

The thrust of the plaintiffs' argument focuses exclusively on the language in §77-2008 pertaining to the use of "prevailing interest rates". "Prevailing" has been generally defined in terms such as "generally current", "most frequent", "of wide circulation". If "prevailing use" was the only term of the test, perhaps the six percent rate was not the prevailing rate in 1981; however, the statute also requires that the rate must be based on sound actuarial principles.

Section 77-2008 provides the Tax Commissioner shall, "from time to time", adopt the regulations in tables specified therein. This language provides discretion on the Tax Commissioner's part as to the determination of when a change in such tables is warranted. As Mr. Luckner, the actuary, testified, the determination as to when it would be sound

actuarial practice to move from one interest rate to another rests on a determination that, based on the professional judgment of the actuary, a permanent, long-term trend at a particular level of interest rates has been firmly established. Conditions which reflect temporary, short-term effects in a highly volatile market, resulting in artificially inflated interest rates, cannot form the basis for establishing the appropriate interest rate for long-term tables of this nature. The plaintiffs' witness, Jim Turner, conceded that interest rates were highly volatile in the early 1980's, and that various factors relating to economic conditions and monetary policy at that time, principally the high rate of inflation, created a situation where certain market interest rates were temporarily elevated to extremely high levels during that period.

The evidence demonstrates that the Tax Commissioner has, consistent with the requirements of §77-2008, promulgated the regulations with regard to life estates and remainder interests for inheritance tax purposes in accordance with the law. This is reflected in the amendments adopted by the Tax Commissioner in 1984, which adopted the rate in effect at that time established by the Internal Revenue Service under federal estate tax regulations, resulting in a change from the six percent interest rate to a ten percent interest rate for Nebraska inheritance tax

purposes. The Internal Revenue Service moved from a six percent interest rate in the federal estate tax tables to a ten percent interest rate effective for decedent's dying after November 30, 1983. The Internal Revenue Service continued to employ a six percent interest rate for this purpose for interests transferred after December 31, 1970, and before December 1, 1983. The fact that the federal government continued to employ a six percent interest rate in 1981 for federal estate tax purposes, and did not raise the interest rate under federal regulations to ten percent until 1983, is evidence that the Tax Commissioner, in acting in 1984 to move to the ten percent interest rate employed at that time by the Internal Revenue Service, did timely exercise her duties under §77-2008. In establishing an interest rate for the valuation of annuities, life estates, and remainder interests for use in actuarial tables, it is simply not consistent with sound actuarial theory or practice to attempt to establish an interest rate based on a particular rate of interest in effect on a specific date, or, for that matter, on an average of a particular rate of interest for a specific year. Rather, as Mr. Luckner stated, it is necessary to examine historical trends and make assumptions reflecting long-term interest rate trends.

The plaintiffs have not presented any evidence relating to

the actuarial soundness of the interest rate employed by the Tax Commissioner at the relevant time. Jim Turner, the witness relied upon by the plaintiffs, is not an actuary. While Mr. Turner may well be qualified to state what particular interest rates were in effect in certain financial markets at specific times, there is nothing which establishes any relevancy in his testimony to the issue involved in this particular case with respect to the appropriateness of an interest rate for use regarding the limited purpose of adopting tables for the valuation of life estates and remainder interests.

Mr. Luckner testified that, based on his background and experience as an actuary, the various factors and data he reviewed in assessing the appropriateness of the interest rate factor in effect under Nebraska Law in 1981 for the valuation of life estates and remainder interests for inheritance tax purposes, it was his opinion that the six percent interest rate in effect at that time was not unreasonable and was consistent with sound actuarial practice and prevailing interest rates.


Considering all of the evidence, the Court finds that the regulations of the Tax Commissioner adopting a rate of six percent, were based on sound actuarial principles and prevailing interest rates, The language in McMurtry v. Commissioner, 203 F. 2d 659 (1st Cir. 1953) is appropriate although dealing with a somewhat different issue.

"The whole problem of valuing individual life interests by resort to mortality tables is at best a matter of educated guesswork. The courts cannot demand perfection in an area so fraught with speculation and uncertainty. The fact is also not to be disregarded that as late as 1952 - ten years after the agreed valuation date of the interests here in question - approximately three-fourths of the states were still using for state inheritance tax purposes the same actuarial table used by the Commissioner, or else the American Experience Table compiled in 1968, which is not much better from petitioners' point of view. See I Prentice-Hall, Inheritance and Transfer Tax Service, p. 801 (1952). We think, therefore, that tables which have enjoyed such widespread and long-standing use should not be rejected as wholly unreasonable, even though they may perhaps be susceptible of minor improvements in particular respects. Such discrepancies as may exist will no doubt average out in the long run; and while this may sometimes prove to be unfortunate for individual taxpayers, the discrepancies may have to be suffered in the interest of a simplified overall administration of the tax laws.

We do not think that the Tax Court erred in accepting the 4 percent interest factor used by the Commissioner. The evidence indicated that virtually all the states in 1942 used an interest factor of 4 percent or even higher for inheritance tax purposes.

THE COURT FINDS that the regulations and tables promulgated and adopted by the Tax Commissioner pursuant to Neb. Rev. Stat. &77-2008 (Reissue 1981) were not in excess of statutory authority and it is ordered that plaintiffs' petition be and it is hereby dismissed at plaintiffs' costs.

Dated this 30 day of July, 1986.

  
District Judge