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TAXATION -- TAXING INCOME FROM SHORT-TERM FAMILY TRUST TO SETTLOR

William H. Shipley
University of Michigan Law School

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TAXATION — TAXING INCOME FROM SHORT-TERM FAMILY TRUST TO SETTLOR — In 1931 a settlor executed a deed of trust and transferred securities to the trustees, who were also the settlor's lawyers. The trustees were to pay the income to the settlor's wife, children and mother-in-law. The duration of the trust was six years and sixteen days, but it was provided that the trust would terminate before that time if the settlor or his wife died. At the termination of the trust the corpus was to be returned to the settlor. The settlor reserved no power to remove the trustees or to modify or revoke the trust or to control the management of the trust property. The commissioner of internal revenue sought to tax the income of the trust for the years 1934 and 1935 as income of the settlor although the trust was not created to satisfy any legal obligations of the settlor. *Held*, the net income of the trust is taxable to the settlor under section 22(a) of the Revenue Act of 1934.[1] *Commissioner of Internal Revenue v. Barbour*, (C. C. A. 2d, 1941) 122 F. (2d) 165.

In *Helvering v. Clifford*[2] it was decided that the income of an irrevocable

[1] Section 22(a) of the Revenue Act of 1934, 48 Stat. L. 686 (1934), 26 U. S. C. (1934), § 22(a), includes within "gross income" all "gains, profits, and income derived . . . from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever." The same provision was re-enacted in 49 Stat. L. 1657 (1936); 52 Stat. L. 457 (1938); 53 Stat. L. 9 (1939), 26 U. S. C. (Supp. 1939), § 22a.

[2] Helvering v. Clifford, 309 U. S. 331, 60 S. Ct. 554 (1940).

short-term trust could be taxed to the settlor because he was the owner of the corpus within the meaning of section 22(a).[3] In the *Clifford* case the facts differed from those of the principal case in that the term of the trust was five years and that the settlor-husband was the trustee and as trustee had unrestricted power to invest, to pledge, and to mortgage the trust res. According to that case, the settlor is the owner of the corpus within the meaning of section 22(a) unless the trust effects a substantial change in the settlor's economic position and in his dominion and control of the corpus.[4] The inquiry here is whether the facts of the principal case place it within the doctrine enunciated in the *Clifford* case.[5] The difference in the years of duration of the trusts involved in the two cases is relatively insignificant. However, a ten-year trust has been held not to be within the doctrine of the *Clifford* case.[6] But a substantial difference exists between the facts of the *Clifford* case and those of the principal case in that the settlor in the present case retained no control or rights of management under the trust agreement.[7] Certainly it is much more difficult to disregard the trust and consider the settlor as the owner when he has stripped himself of all dominion over the trust res. Moreover, it is difficult to assume that the trustee will always respect the wishes of the settlor as to the management of the property merely because the property will shortly revert to the settlor. This case must therefore be regarded as an extension of the doctrine of the *Clifford* case in the taxation of short-term trusts. In the light of the *Jonas* case [8] and the principal case, it is apparent that the present emphasis is on the time element and the relationship of the settlor to the beneficiaries of the trust.[9]

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[3] Compare with Helvering v. Wood, 309 U. S. 344, 60 S. Ct. 551 (1940).

[4] "For where the head of the household has income in excess of normal needs, it may well make but little difference to him (except income-tax-wise) where portions of that income are routed—so long as it stays in the family group." Helvering v. Clifford, 309 U. S. 331 at 336, 60 S. Ct. 554 (1940).

[5] For discussions of Helvering v. Clifford, 309 U. S. 331, 60 S. Ct. 554 (1940), see 38 MICH. L. REV. 885 (1940); 53 HARV. L. REV. 1050 (1940); 49 YALE L. J. 1305 (1940); 24 MINN. L. REV. 1005 (1940); Ray, "The Income Tax on Short Term and Revocable Trusts," 53 HARV. L. REV. 1322 (1940); PAUL, STUDIES IN FEDERAL TAXATION, THIRD SERIES 194 (1941).

[6] Commissioner of Internal Revenue v. Jonas, (C. C. A. 2d, 1941) 122 F. (2d) 169.

[7] The court felt that the settlor could control the corpus, since the trustees would respect his wishes because the trustees realized that within a short time the settlor would repossess the corpus by the terms of the trust. Principal case, 122 F. (2d) 165 at 166-167.

[8] Commissioner of Internal Revenue v. Jonas, (C. C. A. 2d, 1941) 122 F. (2d) 169, held that a ten-year trust was not within the doctrine of Helvering v. Clifford, 309 U. S. 344, 60 S. Ct. 554 (1940).

[9] This emphasis on the time element may be questioned in light of the refusal of Congress to adopt legislation to tax the income of a trust for a term of years. HEARINGS ON H. R. 7835, 73d Cong., 2d sess., p. 151 (1934); H. REP. 1385, 73d Cong., 2d sess. (1934), p. 24.