2 T.C. 159 (1943)

Trust income is taxable to the beneficiary unless it is demonstrably used to discharge the grantor's legal obligation, such as support for minor children, and the burden of proof lies with the beneficiary to show the extent of such use.

Summary

Katharine Ketcham received income from trusts established by her former husband, Francis duPont, in contemplation of divorce. The IRS assessed deficiencies, arguing the trust income was taxable to her. Ketcham contested, arguing it was for alimony or child support, and that the statute of limitations barred some assessments. The Tax Court held that the trust income was taxable to Ketcham, except to the extent proven to be used for child support, which remained the husband's obligation. The court also found that the statute of limitations did not bar the deficiencies due to the omission of income exceeding 25% of her gross income and reliance on the mitigation provisions.

Facts

Katharine Ketcham (formerly duPont) divorced Francis duPont. Prior to the divorce, duPont established two trusts with income payable to Katharine for life. An agreement stipulated Katharine would provide clothing and medical care for the children from the trust income, while duPont retained legal custody and provided for their education and support. The divorce decree approved the trust agreements. A later compromise agreement guaranteed Katharine a minimum income of $25,000 per year from the trusts and duPont's personal funds.

Procedural History

The Commissioner determined deficiencies in Ketcham's income tax for 1933, 1935, 1936, 1937, 1938, and 1939. DuPont previously challenged the taxability of the trust income to him, and the Board of Tax Appeals ruled the income was not taxable to him except to the extent it was used for child support. Ketcham then received a deficiency notice. She petitioned the Tax Court, arguing the trust income was not taxable to her and that the statute of limitations barred some deficiencies.

Issue(s)

1. Whether the income from trusts established by a former husband for the benefit of his divorced wife and minor children is taxable to the wife.

2. Whether the deficiency assessment for 1933 is barred by the statute of limitations.

3. Whether the deficiencies for 1935 and 1936 are barred by the statute of limitations.

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Holding

1. No, the trust income is taxable to the wife only to the extent it was not used for the support and maintenance of the minor children, which remained the legal obligation of the former husband.

2. No, the deficiency for 1933 is not barred because the assessment was made within one year of the Board of Tax Appeals decision holding the trust income was not taxable to the grantor, and the mitigation provisions of the tax code apply.

3. No, the deficiencies for 1935 and 1936 are not barred because the taxpayer omitted income exceeding 25% of her reported gross income, extending the statute of limitations to five years, and the deficiency notice was timely.

Court’s Reasoning

The court reasoned that the trust income was generally taxable to the beneficiary (Ketcham), as per Revenue Act of 1932, sec. 162 (b). However, to the extent that the trust income was used to discharge the husband’s legal obligation to support his minor children, it was taxable to him, citing *Helvering v. Stuart, 317 U.S. 154*. The court emphasized that the taxpayer (Ketcham) bore the burden of proving how much of the trust income was used for child support. General household expenses were not excludable from the wife’s income without specific evidence allocating them to the children’s support. The court stated, “The taxpayer here can avoid the deficiency only to the extent that she proves the amount which is not attributable to her but to the discharge of the father’s obligation to the children.” The court further noted that the 1936 agreement guaranteeing a minimum income did not alter the taxability of the trust income to the wife. Regarding the statute of limitations, the court applied section 820 of the Revenue Act of 1938 (now <span normalizedcite=

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