3 T.C. 281 (1944)

Under California law, a voluntary trust created after 1931 is revocable by the trustor unless the trust instrument expressly states it is irrevocable, impacting the tax liability for trust income.

Summary

George and Gertrude Gaylord, California residents, created a trust in 1935 for their daughters, intending it to be irrevocable. However, the trust instrument lacked an explicit irrevocability clause. Unaware of a 1931 amendment to California Civil Code Section 2280, which made all voluntary trusts revocable unless expressly stated otherwise, the Gaylords later executed a declaration of irrevocability in 1940. The Tax Court held that the trust was revocable under California law from 1936-1939, thus the trust income was taxable to the Gaylords proportionally to their contributions to the trust corpus.

Facts

The Gaylords, intending to make gifts to their daughters, created a trust in 1935, naming themselves as trustees and contributing 7,000 shares of Marathon Paper Mills Co. stock (5,000 by George, 2,000 by Gertrude).
The trust document did not explicitly state whether it was revocable or irrevocable.
The Gaylords filed gift tax returns in 1936, reporting the trust as irrevocable.
In 1940, upon realizing the omission, they executed a separate instrument declaring the trust's intended irrevocability.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in the Gaylords' income tax for 1936-1939, arguing the trust income was taxable to them because the trust was revocable.
The Gaylords petitioned the Tax Court, contesting the Commissioner's determination.

Issue(s)

Whether the income of the Gaylord trust for the years 1936 through 1939 was taxable to the Gaylords as grantors of a revocable trust, given the absence of an explicit irrevocability clause in the original trust instrument and the presence of California Civil Code Section 2280.

Holding

No, because under California law effective during the tax years in question, the absence of an express irrevocability clause in the trust instrument rendered the trust revocable, making the grantors liable for the trust's income tax.

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Court’s Reasoning

The court relied on the 1931 amendment to California Civil Code Section 2280, which states: “Unless expressly made irrevocable by the instrument creating the trust, every voluntary trust shall be revocable by the trustor.”
The court emphasized that the Gaylord trust was created in 1935, after the amendment, and the trust instrument lacked the express declaration of irrevocability required by the statute.
The court rejected the argument that the Gaylords’ intent to create an irrevocable trust, or the subsequent declaration of irrevocability in 1940, could override the statutory requirement of an express clause in the original instrument. “To hold otherwise would in effect be a rewriting of the California statute or a making of the trust instrument something it was not. We do not possess the power to do either.”
The court also dismissed the estoppel argument, noting it was not specifically pleaded.

Practical Implications

This case underscores the importance of precise legal drafting, especially in trust instruments. It serves as a reminder that intent alone is insufficient; specific language is required to achieve the desired legal outcome.
Attorneys practicing in California (and other states with similar statutes) must ensure that trust documents explicitly state irrevocability if that is the grantor’s intention, or the trust will be deemed revocable by law.
The case highlights the retroactive impact of trust revocability on income tax liability, emphasizing the need to review existing trust arrangements in light of relevant state laws.
Later cases cite Gaylord for the principle that a trust created after the 1931 amendment to California Civil Code Section 2280 is presumed revocable unless the trust instrument explicitly states otherwise.

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