Stockstrom v. Commissioner, 4 T.C. 255 (1944)

A grantor is treated as the owner of a trust and taxed on its income when the grantor retains substantial control over the trust through retained powers, even if those powers are not directly related to income distribution.

Summary

The Tax Court held that the income from three trusts created by Bertha Stockstrom was taxable to her as the grantor because she retained significant powers over the trusts. Although Stockstrom did not directly control income distribution, she reserved the power to amend most provisions of the trust agreements and to remove trustees. The court reasoned that these retained powers gave her substantial control over the trusts, making her the de facto owner for tax purposes under Section 22(a) and the principles of *Helvering v. Clifford*. The court emphasized that the grantor's ability to influence the trustees' actions was tantamount to direct control.

Facts

Bertha Stockstrom created three trusts in 1939, primarily for the benefit of her children and grandchildren. The trusts were funded with shares of American Stove Co. common stock. The trust agreements named Louis Stockstrom (Bertha's husband) and M.E. Turner as trustees. Bertha retained the power to amend most provisions of the trust agreements, except for those relating to income and principal distribution (Items Two, Three, and Four). Louis Stockstrom had the power to remove M.E. Turner as trustee. The trust income was primarily distributed to Bertha's children. Bertha filed a gift tax return for the transfer of stock to the trusts and paid the corresponding tax.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in Bertha Stockstrom's income tax for 1939, 1940, and 1941, arguing that the trust income was taxable to her. After Bertha Stockstrom died, the Commissioner pursued the deficiencies against her estate's transferees. The Tax Court reviewed the Commissioner's determination.

Issue(s)

Whether the income of the three trusts created by the decedent is taxable to her as the grantor under Section 166 of the Internal Revenue Code (regarding revocable trusts) or under Section 22(a) and the principles of *Helvering v. Clifford* (regarding grantor control).

Holding

Yes, because the grantor retained significant powers over the trusts, including the

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power to amend most trust provisions and to effectively remove and replace trustees, giving her substantial control over the trust assets and income, making her the de facto owner for tax purposes.

Court's Reasoning

The Tax Court reasoned that Bertha Stockstrom's retained powers gave her substantial control over the trusts, even though she didn't directly control income distribution. The court noted that she could amend the trust agreements to influence the trustees' discretionary actions and could effectively remove and replace trustees, potentially appointing herself. The court analogized the situation to *Louis Stockstrom, 3 T.C. 255*, where the grantor was also the trustee and had broad powers over income distribution. The court cited *Commissioner v. Buck, 120 F.2d 775*, and *Ellis H. Warren, 45 B.T.A. 379*, aff'd, *133 F.2d 312*, emphasizing that such powers, combined with broad administrative powers, amounted to substantial ownership. The court emphasized that Item Two, while unamendable, still granted the trustees discretion over income distribution. The court concluded that these powers brought the case in line with *Helvering v. Clifford, 309 U.S. 331*, requiring the trust income to be taxed to the grantor. The court stated, "We find nothing in the unamendable items two, three, and four of the trust agreements which can be said to constitute a complete and irrevocable gift to any of the beneficiaries of the trusts."

Practical Implications

This case reinforces the grantor trust rules, highlighting that retained powers, even if seemingly indirect, can cause a grantor to be taxed on trust income. Attorneys drafting trust agreements must carefully consider the scope of any retained powers, as they can trigger grantor trust status. The case serves as a reminder that the IRS and courts will look beyond the formal structure of a trust to assess the grantor's actual control. Later cases cite this ruling for the principle that the power to influence trustee actions, even without direct control over distributions, can lead to grantor trust treatment. This case emphasizes that the totality of the circumstances, not just isolated provisions, determines taxability.

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