Mather v. Commissioner, 5 T.C. 1001 (1945)

A grantor is taxed on trust income when they retain substantial control over the trust, including the power to direct investments and to use income for the maintenance and education of dependents.

Summary

Rathbun Fuller Mather created trusts for his children, naming a bank as trustee. The trust agreements gave Mather broad powers, including directing trust investments and potentially using income for the children's maintenance and education. The IRS argued that Mather should be taxed on the trust income under Sections 22(a), 166, and 167 of the Internal Revenue Code. The Tax Court agreed, holding that Mather's retained powers made him the substantial owner of the trusts, thus taxable on the income, because he could direct investments and potentially benefit from the income being used to satisfy his legal obligation to support his children.

Facts

Rathbun Fuller Mather established four identical trusts, one for each of his minor children. The Summit Trust Co. was named as trustee. The trust agreements granted the trustee broad administrative powers, including the power to invest and reinvest trust funds, either in legal trust investments or as directed in writing by Mather. Mather retained the right to direct the trustee to make loans, sales, and purchases. Mather was financially able to support his children and did so from his own funds. The trust instruments stated that Mather "retains the right to elect at any time to have all or any part of the net income used for the maintenance and education of his said son".

Procedural History

The Commissioner of Internal Revenue determined income tax deficiencies against Mather for 1940 and 1941, arguing that the income from the trusts should be included in Mather's gross income. Mather challenged the Commissioner's determination in the Tax Court.

Issue(s)

Whether the grantor of a trust is taxable on the trust's income under Sections 22(a), 166, or 167 of the Internal Revenue Code, where the grantor retained the power to direct trust investments and the potential to use trust income to satisfy his legal obligation to support his minor children.

Holding

Yes, because the grantor retained substantial control over the trust assets, including the power to direct investments and the potential to use the income to satisfy his legal obligation to support his children, making him the substantial owner of the trust for tax purposes.

Court’s Reasoning

The Tax Court relied on several factors to conclude that Mather was taxable on the trust income. First, Mather retained the right to direct the trustee to make loans, sales, and purchases. The court reasoned this right was essentially a power to revoke the trust, citing *Estate of William J. Garland, 42 B. T. A. 324*. The court stated,

