6 T.C. 77 (1946)

A settlor-trustee is not taxable on trust income under Section 22(a) of the Internal Revenue Code merely because of broad management powers, provided they do not derive economic gain and the trust mandates eventual distribution of income and principal to the beneficiary.

Summary

Alma M. Myer created a trust for her son, serving as trustee with broad managerial powers, including the discretion to distribute or accumulate income until he turned 30, at which point all assets would be distributed to him. The Commissioner of Internal Revenue argued that the trust income should be taxable to Myer under Section 22(a) of the Internal Revenue Code. The Tax Court ruled in favor of Myer, holding that the broad managerial powers did not warrant taxing the income to her, as the trust mandated eventual distribution to the beneficiary, and she derived no economic benefit.

Facts

In 1932, Alma M. Myer created an irrevocable trust for the benefit of her son, Leo A. Drey. The trust agreement, formalized in writing in 1934, included cash, securities, and various bonds contributed by Myer, her parents, and her son's aunt. Myer, as trustee, possessed broad powers, including managing and controlling trust property, selling or exchanging assets, investing proceeds, and borrowing money for trust purposes. The trust allowed her to expend net income for her son's benefit at her discretion, accumulating any unexpended income. The trust was to terminate when Leo reached 30, at which point all assets would be distributed to him. Myer's personal net worth was approximately $1,000,000, with an annual income exceeding $35,000.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in Myer's income tax for the years 1938-1941, attributing a portion of the trust income to her under Section 22(a) of the Internal Revenue Code. Myer petitioned the Tax Court for a redetermination of these deficiencies.

Issue(s)

Whether the income of a trust, derived from property contributed by the settlor-trustee, is taxable to the settlor-trustee under Section 22(a) of the Internal Revenue Code, where the settlor-trustee has broad managerial powers but no direct economic benefit, and the trust mandates eventual distribution of income and principal to the beneficiary.

Holding

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No, because the settlor-trustee did not enjoy significant attributes of ownership warranting taxation of the trust income, as the broad managerial powers did not result in economic gain, and the trust instrument fixed a time for payment of the income and distribution of the principal which permitted of no variation by the trustee.

Court's Reasoning

The Tax Court distinguished this case from *Helvering v. Clifford*, 309 U.S. 331 (1940), stating that Myer did not retain enough control to warrant taxing the trust income to her. The court highlighted that the trust mandated eventual distribution of income and principal to the beneficiary, Leo, at age 30. Unlike cases where the settlor-trustee could indefinitely withhold income, Myer's discretion was limited by the fixed date of distribution. The court relied on precedent such as *J.M. Leonard, 4 T.C. 1271*, and *Alice Ogden Smith, 4 T.C. 573*, where settlor-trustees were not taxed on trust income due to similar limitations on their control. The court emphasized that mere managerial powers, without economic benefit, are insufficient to justify taxing the settlor-trustee. Judge Opper dissented, arguing that Myer retained significant control over the trust, including the power to accumulate income and potentially benefit from the trust through insurance transactions and the possibility of inheriting the trust assets if her son died intestate before age 30.

Practical Implications

This case clarifies the limits of the *Clifford* doctrine in the context of settlor-trustees. It establishes that broad managerial powers alone are not sufficient to tax trust income to the settlor. Crucially, the trust must provide for eventual distribution of income and principal to the beneficiary. Drafting attorneys must consider the degree of control retained by the settlor, the duration of the trust, and the mandatory or discretionary nature of income distribution. This decision emphasizes the importance of a fixed distribution date to avoid the settlor being taxed on trust income. Later cases have cited *Myer* to distinguish situations where the settlor retained greater control or economic benefit, leading to different tax consequences.

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