4 T.C. 850 (1945)

When trust income is used to pay premiums on life insurance policies for the grantor's benefit, that income is taxable to the grantor, even if structured as a loan from the trust.

Summary

Rom created five family trusts and one insurance trust. The family trusts' income was used to pay premiums on life insurance policies held in the insurance trust, insuring Rom's life. Rom argued this was a loan, not an application of income, and therefore not taxable to him. The Tax Court held that because the trustees used the family trusts' income to pay the premiums, the income was taxable to Rom under Section 167(a)(3) of the Internal Revenue Code, regardless of whether it was nominally labeled a loan. The court emphasized that the beneficiaries did not control the income, and the arrangement served to circumvent tax law.

Facts

- Petitioner, Rom, created an insurance trust intended to hold life insurance policies on his life. He initially planned to fund it with securities.
- Instead of funding the insurance trust, Rom created five family trusts and transferred income-producing securities (preferred stock of M. Rom & Sons Co.) to them.
- The income from these family trusts was used to pay the premiums on the life insurance policies held by the insurance trust.
- The trustees of all trusts were the same three individuals.
- After a revenue agent's examination, the trustees made book entries to reflect these premium payments as 'loans' from the family trusts.

Procedural History

The Commissioner of Internal Revenue determined that the income from the family trusts used to pay the life insurance premiums was taxable to Rom. Rom petitioned the Tax Court for review.

Issue(s)

Whether the income from family trusts, used to pay premiums on life insurance policies on the grantor's (Rom's) life, is taxable to the grantor under Section 167(a)(3) of the Internal Revenue Code, when the payments are characterized as loans from the family trusts.

Holding

Yes, because the income of the family trusts was in fact used to pay the premiums on the policies of insurance on the grantor's life, and the grantor predetermined the

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plan.

Court’s Reasoning

The court focused on the statutory language of Section 167(a)(3), which taxes the grantor when trust income “is…applied to the payment of premiums upon policies of insurance on the life of the grantor.” The court reasoned that the actual use of the income was the determining factor, not the label attached to the transaction. The court dismissed the

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