Richards v. Commissioner, 19 T.C. 366 (1952)

A settlor is taxable on trust income when they retain substantial control and economic benefit over the trust corpus, even if legal title is nominally transferred to a trust.

Summary

The Tax Court addressed whether income from trusts created by Richards for his children should be included in his and his wife's taxable income under Section 22(a) of the Internal Revenue Code. Richards, seeking to shift income while maintaining control over his business interests, created trusts funded with stock but retained significant rights, including voting rights and control over stock disposition. The court held that because Richards retained substantial ownership attributes and the full legal title to the stock, the trust income was taxable to him, except for income derived from reinvestments made by the trustees.

Facts

Richards, associated with Paramount in operating Paramount-Richards and Enterprises, formed nine trusts for his children, funding them with a "beneficial interest" in certain shares of stock. However, Richards retained full legal title to the stock, including voting rights, the right to receive stock dividends, and the power to dispose of the stock (subject to Paramount's option). Paramount consented to the transfer of the beneficial interest to the trustees only after Richards assured them that they would not have to recognize the trustees as owners of any interest in the stock and that he would retain all rights and powers associated with the stock.

Procedural History

The Commissioner of Internal Revenue determined that the income from the trusts was taxable to Richards and his wife. Richards and his wife petitioned the Tax Court for a redetermination. The Tax Court upheld the Commissioner's determination in part, finding that the dividend income was taxable to Richards, but not the income from the trustees' reinvestments.

Issue(s)

1. Whether the dividend income from the stock held in trust is taxable to the settlor, Richards, under Section 22(a) of the Internal Revenue Code, given his retained control and economic benefit.
2. Whether the income generated by the trustees' reinvestment of undistributed trust income is taxable to the settlor.

Holding

1. Yes, because Richards retained substantial ownership rights and control over

the stock, including voting rights and the power to dispose of the stock, thus maintaining a significant economic interest.
2. No, because once the trusts received dividend income and reinvested it, Richards no longer had control over that income, and it became part of the trust corpus.

Court’s Reasoning

The court reasoned that Richards, despite transferring a

