30 T.C. 335 (1958)

A beneficiary cannot deduct trustee fees on their personal income tax return when those fees were properly a charge against the trust corpus.

Summary

The Commissioner of Internal Revenue determined a deficiency in the income tax of the Estates of James B. Drew and Mary S. Drew. The issue was whether a trustee's fee, paid in 1953 by Mary, the beneficiary of a trust that terminated in 1947, was deductible on the joint income tax return for 1953. The Tax Court held that the fee, which was properly chargeable to the trust corpus, could not be deducted by Mary, even though she paid it from her personal funds after the trust terminated. The court reasoned that the fee was an expense of the trust and not of the beneficiary, and therefore, not deductible by the beneficiary.

Facts

William P. Snyder established the "Mary Snyder (Drew) Trust No. 6835" in 1917, with Mary as both income and principal beneficiary, and Pittsburgh Trust Company as trustee. The trust's term was 30 years. The trust instrument stipulated that the trustee would collect income, deduct charges and expenses, and distribute the surplus to Mary. Upon termination, the trustee was to receive its balance of compensation from the corpus. The trust terminated on February 2, 1947. At termination, the trustee was owed $7,470 in fees. The trustee-bank suggested Mary leave the corpus in an agency account to defer fee collection. Mary and the bank executed an agency agreement in May 1947. In 1953, Mary terminated the agency and paid the $7,470 fee. This fee was claimed as a deduction on Mary's 1953 joint income tax return with her deceased husband James. The Commissioner disallowed the deduction.

Procedural History

The Commissioner of Internal Revenue disallowed the deduction of trustee fees on the joint income tax return of Mary and James Drew. The petitioners, the Estates of James B. Drew and Mary S. Drew, contested this disallowance in the United States Tax Court.

Issue(s)

Whether the trustee's fee of $7,470, paid by Mary in 1953 after the trust terminated, is properly deductible on the joint income tax return of Mary and James Drew for the year 1953.

Holding

No, because the trustee's fee was earned during the term of the trust and was a

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proper charge against the trust corpus, and is not deductible by the beneficiary.

Court’s Reasoning

The court focused on the nature of the trustee’s fee. It determined the fee was earned during the trust’s operation and was, according to the trust instrument, a charge against the corpus. The court emphasized that the trust and its beneficiaries are separate taxable entities. The fact that Mary, rather than the trust, actually paid the fee did not change the nature of the expense. The court stated, “Mary may not deduct the expenses of another.” The court distinguished the case from scenarios where a beneficiary could deduct taxes assessed against the trust property because in those cases the payment was necessary to preserve the trust property. Because Mary would have received the same net benefit whether the fee was paid by the trust or by her, the payment was not deductible.

Practical Implications

This case highlights the importance of distinguishing between the tax liabilities of trusts and their beneficiaries. Legal practitioners should consider whether the expense is properly a charge of the trust or the beneficiary. The case reinforces the principle that a beneficiary generally cannot deduct expenses that are the responsibility of the trust. Furthermore, any agreement between the trustee and beneficiary that shifts the responsibility for payment of the fees does not change the underlying tax consequences. This case can be cited in similar situations where beneficiaries seek to deduct expenses incurred by a trust. The court also reinforces the general rule that expenses are deductible by the party who incurred the expense.

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