***Spruance v. Commissioner, 60 T. C. 141 (1973)***

A separation agreement that transfers appreciated property to a trust for the benefit of a spouse and children can result in a taxable gift to the extent the property's value exceeds the consideration received, impacting the basis of the trust property for future tax events.

**Summary**

In Spruance v. Commissioner, the court addressed the tax implications of a 1955 separation agreement that created a trust for the benefit of the taxpayer's ex-wife and children. The agreement transferred appreciated stock to the trust, and the court held that this transfer resulted in a taxable gift to the extent the stock's value exceeded the value of the ex-wife's marital rights and child support obligations. The court also determined that the trust's basis in the stock should be increased to reflect the gain recognized by the transferor, but only for the non-gift portion of the transfer. Additionally, the court ruled that the trustee was not estopped from claiming this step-up in basis due to the transferor's individual actions, and no capital gain was recognized on the subsequent receipt of divestiture stock under section 1111 of the Internal Revenue Code.

**Facts**

In 1955, Preston Lea Spruance and his wife, Margaret, entered into a separation agreement that was later incorporated into their divorce decree. The agreement stipulated that Spruance would transfer appreciated stock into a trust, with income from the stock going partly to Margaret for her support and partly to their children while minors. The remainder interest would pass to the children upon the death of both parents. One child was already an adult at the time of the transfer. Spruance did not report any gain from the transfer or file a gift tax return. In 1962, 1964, and 1965, the trust received General Motors divestiture stock from duPont and Christiana Securities, and Spruance, as trustee, claimed a stepped-up basis for the transferred stock when reporting the income under section 1111 of the Internal Revenue Code.

**Procedural History**

The Commissioner of Internal Revenue determined deficiencies in the trust's income tax for the years 1962, 1964, and 1965, and a gift tax deficiency for Spruance for 1955. Spruance contested these deficiencies in the U. S. Tax Court, which consolidated the cases. The Delaware courts had previously ruled that the separation agreement created a trust. The Tax Court issued its decision in 1973, addressing the tax implications of the transfer and the subsequent receipt of divestiture stock.

**Issue(s)**

© 2025 SCOTUSreports.com. All rights reserved. 

1. Whether Spruance made a taxable gift when he transferred various stocks in trust for the benefit of his wife and children.
2. Whether Spruance is liable for the addition to tax under section 6651(a) for failure to file a Federal gift tax return covering the alleged gift to his children in 1955.
3. Whether Spruance, as trustee, recognized long-term capital gain in the taxable years 1962, 1964, and 1965 under section 1111 on the receipt of General Motors Corp. divestiture stock.
4. Whether the statute of limitations bars assessment and collection of any deficiency in income tax due from Spruance, as trustee, for the taxable year 1962.

**Holding**

1. Yes, because the value of the stock transferred exceeded the value of the marital and child support rights released, resulting in a taxable gift of $448,158. 37.
2. No, because Spruance relied on the advice of counsel at the time of the transfer, which constitutes reasonable cause for not filing a gift tax return.
3. No, because the trust's basis in the stock was increased to reflect the gain recognized by Spruance, and the value of the divestiture stock received did not exceed this basis.
4. Yes, because the 3-year statute of limitations under section 6501(a) bars assessment for 1962, as there was no substantial omission of income.

**Court's Reasoning**

The court applied sections 2512(b) and 2516 of the Internal Revenue Code to determine that the transfer of stock to the trust was partly a taxable gift because it exceeded the value of the marital and child support rights released. The court noted that donative intent is not necessary for a gift tax to apply. Regarding the addition to tax under section 6651(a), the court found that Spruance's reliance on counsel's advice constituted reasonable cause for not filing a gift tax return. For the capital gain issue, the court held that the trust's basis in the stock should be increased to reflect the gain recognized by Spruance, but only for the non-gift portion of the transfer. The court rejected the Commissioner's estoppel argument, stating that acts done in an individual capacity cannot estop one in a representative capacity. Finally, the court ruled that the statute of limitations barred assessment for 1962 because there was no substantial omission of income.

**Practical Implications**

This decision clarifies that transfers of appreciated property under separation agreements can result in taxable gifts to the extent they exceed the value of marital and child support rights released. Practitioners should advise clients to consider the gift tax implications of such transfers and ensure proper reporting. The ruling also establishes that a trust's basis in property transferred as part of a separation agreement can be increased to reflect the gain recognized by the transferor, but

© 2025 SCOTUSreports.com. All rights reserved. 

only for the non-gift portion of the transfer. This case may influence how similar cases are analyzed, particularly in determining the basis of property transferred to trusts in divorce settlements. Additionally, the decision reinforces the principle that actions taken in an individual capacity do not estop a person acting in a fiduciary capacity, which could impact how fiduciaries handle tax matters related to trusts.

© 2025 SCOTUSreports.com. All rights reserved. 