NOTES

THE SEVENTH CIRCUIT V. THE CLIFFORD REGULATIONS: "DUE PROCESS" EMANCIPATES THE TAX AVOIDER*

TRUSTS are a favorite income-splitting device among taxpayers seeking to avoid the high federal tax rates on large incomes.[1] While the settlor hopes the Government will tax the income of his trust separately, he is generally reluctant to relinquish all control over, or benefit from, the trust. But by retaining such attributes of ownership, the settlor may defeat his own tax avoidance scheme. The Supreme Court holds him taxable on trust income used to discharge his legal obligations.[2] And by statute, the settlor is taxed on trust income when he, or someone without an interest substantially ad-

*Commissioner v. Clark, Commissioner v. Rutherford, 202 F.2d 94 (7th Cir. 1953). The Government has decided not to petition for certiorari. 4 P-H 1953 FED. TAX SERV. ¶ 71,096.

1. "By the creation of trusts, incomes had been so divided and subdivided as to withdraw from the Government the benefit of the graduated taxes and surtaxes applicable to income when concentrated in a single ownership. . . . One can read in the revisions of the revenue acts the record of the Government's endeavor to keep pace with the fertility of invention whereby taxpayers had contrived to keep the larger benefits of ownership and be relieved of the attendant burdens." Burnet v. Wells, 289 U.S. 670, 675-6 (1933). See also H.R. REP. No. 179, 68th Cong., 1st Sess. 21 (1924); SEN. REP. No. 398, 68th Cong., 1st Sess. 25-6 (1924). One aim of the recently added provision permitting spouses to file joint returns, INT. REV. CODE § 51(b), was to reduce the incentive to set up tax-avoiding trusts. H.R. REP. No. 1274, 80th Cong., 2d Sess. 24 (1948). But this only permits a taxpayer to split his income in half. The trust device permits splitting into many parts. See Funk v. Commissioner, 185 F.2d 127 (3d Cir. 1950).

For diverse views on the legitimacy of the trust as a hiding place in the perennial hide-and-seek game in which the tax collector is always "it," see Caplin, *Protecting a Grantor of a Short-Term Trust Against Income Taxation*, 18 TAXES 677 (1940); Kennedy, *Short-Term Trusts Today*, 30 TAXES 1006 (1952); Note, 60 YALE L.J. 1426 (1951).

2. Douglas v. Willcuts, 296 U.S. 1 (1935) (alimony payments); Helvering v. Schweitzer, 296 U.S. 551 (1935) (support of minor children). See Paul, *Five Years with Douglas v. Willcuts*, 53 HARV. L. REV. 1 (1939); Note, 52 HARV. L. REV. 804 (1939). See also Helvering v. Stuart, 317 U.S. 154 (1942), 52 YALE L.J. 662 (1943); Guterman, *The Federal Income Tax and Trusts for Support—The Stuart Case and Its Aftermath*, 57 HARV. L. REV. 479 (1944).

When the obligation is completely discharged by the initial transfer of the property, however, subsequent income from that property is no longer taxable to the obligor. Pearce v. Commissioner, 315 U.S. 543 (1942) (income from annuity for divorced wife). When there are no other grounds to support taxation, a settlor is taxable on trust income only to the extent it is actually applied to discharge the obligation. INT. REV. CODE § 167(c). By statute, income from alimony trusts is now included in the wife's gross income. INT. REV. CODE § 171.

verse to his, can revest either the corpus[3] or the income[4] in the settlor or use the income to pay insurance premiums on his life.[5] In the controversial *Clifford* case the Supreme Court attributed the income of a five-year irrevocable trust to the settlor under Section 22(a) of the Internal Revenue Code, which defines "gross income."[6] The Court held that the settlor "continued to be the owner" of the corpus for income tax purposes because no "substantial change" had occurred in his "dominion and control."[7] The circumstances which "all [led] irresistibly" to this conclusion were "the short duration of the trust, the fact that the [settlor's] wife was the beneficiary, and the retention of control over the corpus."[8] But since the Court stated that "no one fact is normally decisive,"[9] the tax status of short-term irrevocable trusts lacking one or more of the *Clifford* factors remained uncertain.

---

3. INT. REV. CODE § 166, Corliss v. Bowers, 281 U.S. 376 (1930); Reinecke v. Smith, 289 U.S. 172 (1933). Originally, the settlor was taxed only when he could revoke the trust "during the taxable year." Revenue Act of 1924, § 219(g), 43 STAT. 277 (1924). Taxpayers avoided this provision simply by suspending their right to revoke for a year and a day. *E.g.*, Langley v. Commissioner, 61 F.2d 796 (2d Cir. 1932). To prevent such evasion, Congress deleted the phrase "during the taxable year." Revenue Act of 1934, § 166, 48 STAT. 729 (1934). Section 166 applies only to "vested" powers of revocation, not to contingent rights. Commissioner v. Betts, 123 F.2d 534 (7th Cir. 1941); Corning v. Commissioner, 104 F.2d 329 (6th Cir. 1939). Presumably a settlor would not be taxable for retaining even a "vested" power when it could not be exercised until some remote date. *See* Helvering v. Dunning, 118 F.2d 341, 345 (4th Cir.), *cert. denied*, 314 U.S. 631 (1941).

Since the *Clifford* decision, note 7 *infra*, § 166 has declined in importance. Courts have taxed the income of revocable trusts to settlors under § 22(a). *E.g.*, White v. Higgins, 116 F.2d 312 (1st Cir. 1940); Cox v. Commissioner, 110 F.2d 934 (10th Cir.), *cert. denied*, 311 U.S. 667 (1940). But a settlor-reversioner of an irrevocable trust is not taxable under § 166. Helvering v. Wood, 309 U.S. 344 (1940).

See, generally, KENNEDY, FEDERAL INCOME TAXATION OF TRUSTS AND ESTATES §§ 6.05-6.13 (1948); PAUL, STUDIES IN FEDERAL TAXATION, THIRD SERIES 165-228 (1940); Ray, *The Income Tax on Short Term and Revocable Trusts*, 53 HARV. L. REV. 1322, 1322-41 (1940).

4. INT. REV. CODE § 167(a)(1), 167(a)(2), Corliss v. Bowers, 281 U.S. 376 (1930); Altmaier v. Commissioner, 116 F.2d 162 (6th Cir. 1940), *cert. denied*, 312 U.S. 706 (1941). These sections, like § 166, note 3 *supra*, have also been eclipsed by *Clifford*, since a court can now rely on § 22(a). *E.g.*, First Nat. Bank of Chicago v. Commissioner, 110 F.2d 448 (7th Cir. 1940). See, generally, KENNEDY, *op. cit. supra* note 3, §§ 6.14-6.18.

5. INT. REV. CODE § 167(a)(3), Burnet v. Wells, 289 U.S. 670 (1933). See KENNEDY, *op. cit. supra* note 3, § 6.19; Comment, 44 YALE L.J. 1409, 1409-15 (1935).

6. Helvering v. Clifford, 309 U.S. 331 (1940), 49 YALE L.J. 1305. See also PAUL, *op. cit. supra* note 3, *passim*; Ray, *supra* note 3, at 1348-57.

Clifford recognizes the validity of the trust for non-tax purposes. Helvering v. Clifford, *supra* at 335. There were some pre-*Clifford* cases taxing settlors under § 22(a) on the theory that the trust was a complete sham. *E.g.*, DuPont v. Commissioner, 289 U.S. 685 (1933) (insurance trust; even the dissenters in *Wells*, *supra* note 5, joined the majority on this ground). See Ray, *supra* note 3, at 1341-8.

7. Helvering v. Clifford, 309 U.S. 331, 335 (1940).

8. *Ibid.*

9. *Id.* at 336. But see text at note 51 *infra*.

Amid the flood of inconsistent lower court decisions spawned by *Clifford*,[10] some authority can be found for taxing trust income to settlors with reversionary interests on the ground that the trust term is short. The Second Circuit suggested that in such a case there need be "no express reservations of control" "because the grantor will soon reacquire complete dominion. . . ."[11] But there was little agreement as to how short the term had to be.[12] Some courts attempted to confine the *Clifford* doctrine to cases, like *Clifford* itself, in which the trust benefited only the taxpayer's "intimate family group";[13] but they had difficulty delimiting that class.[14] The circuits also split over the applicability of the doctrine to charitable trusts.[15] In short, the decisions provide authority both for and against almost any conceivable rule of thumb.

---

10. *See* Kohnstamm v. Pedrick, 153 F.2d 506, 510 (2d Cir. 1945); Hyman v. Nunan, 143 F.2d 425, 427 (2d Cir. 1944). See Magill, *What Shall Be Done with the Clifford Case?*, 45 COL. L. REV. 111 (1945); Polisher, *The Family Trust—Its Income Tax Fate*, 49 DICK. L. REV. 33 (1945); Notes, 31 GEO. L.J. 477 (1943), 10 U. OF CHI. L. REV. 488 (1943).

11. Commissioner v. Buck, 120 F.2d 775, 778 (2d Cir. 1941). *See* Cushman v. Commissioner, 153 F.2d 510, 513 (2d Cir. 1946); Commissioner v. Katz, 139 F.2d 107, 109 (7th Cir. 1943); Helvering v. Elias, 122 F.2d 171, 173 (2d Cir.), *cert. denied*, 314 U.S. 692 (1941). *But cf.* Central Nat. Bank of Cleveland v. Commissioner, 141 F.2d 352, 354 (6th Cir. 1944).

12. *Taxable:* Helvering v. Elias, 122 F.2d 171 (2d Cir.), *cert. denied*, 314 U.S. 692 (1941) (6½-year term); *cf.* Commissioner v. O'Keeffe, 118 F.2d 639 (1st Cir. 1941) (15-year term; settlor one of four trustees). *Nontaxable:* Central Nat. Bank of Cleveland v. Commisioner, 141 F.2d 352 (6th Cir. 1944) (7-year term); Commisioner v. Jonas, 122 F.2d 169 (2d Cir. 1941) (10-year term). See also cases cited, *infra* notes 13, 15.

Since the cases usually involve additional factors, such as the identity of the beneficiaries and retention of administrative control over the corpus, the decisions do not provide inescapable authority for taxing on the shortness of the trust term alone. The above cited decisions, however, come as close as possible to isolating the short-term factor.

13. When the beneficiaries fell outside the family group, these courts did not tax the settlor. Helvering v. Bok, 132 F.2d 365 (3d Cir. 1942) (3-year trusts for charity and individuals unrelated to settlor); Dunlevy Milbank, 41 B.T.A. 1014 (1940) (3-year trust for sister-in-law; 5-year, uncle). *See* Kraft v. Commissioner, 111 F.2d 370, 371 (3d Cir.), *cert. denied*, 311 U.S. 671 (1940). *Cf.* Farkas v. Commissioner, 170 F.2d 201 (5th Cir. 1948) (10-year trust for settlor's nieces and nephews; one judge dissented while a second concurred by analogy to the *Clifford* regulation, *infra* note 18). *Contra,* Leonard Farkas, 8 T.C. 1351 (1947) (split decision), *rev'd*, 170 F.2d 201 (5th Cir. 1948). *But see* Cushman v. Commissioner, 153 F.2d 510, 513 (2d Cir. 1946).

14. *Compare* Commissioner v. Barbour, 122 F.2d 165, 167 (2d Cir.), *cert. denied*, 314 U.S. 691 (1941) (mother-in-law living apart; settlor taxed) and Commissioner v. Woolley, 122 F.2d 167, 169 (2d Cir.), *cert. denied*, 314 U.S. 693 (1941) (nephew for whose education and maintenance settlor had paid regarded as "in the family" though not member of household) *with* Central Nat. Bank of Cleveland v. Commissioner, 141 F.2d 352, 355 (6th Cir. 1944) (adult children with own homes; settlor held non-taxable) and Farkas v. Commissioner, 170 F.2d 201 (5th Cir. 1948) (nieces and nephews; settlor held non-taxable).

15. *Taxable:* United States v. Anderson, 132 F.2d 98 (6th Cir. 1942), *cert. denied*, 318 U.S. 790 (1943) (5½-year term); Commissioner v. Lamont, 127 F.2d 875 (2d Cir.

To dispel this "uncertainty and confusion," the Treasury in 1945 issued the complex and far-reaching *Clifford* regulations.[16] They evoked severe criticism, largely because they treated each of the factors present collectively in *Clifford* as an independently sufficient ground for taxation.[17] Taxing on shortness of term alone, one of the regulations attributes trust income to a settlor when the corpus or the income will, or may reasonably be expected to, revert to him within ten years of the date of transfer.[18]

In *Commissioner v. Clark*,[19] the Seventh Circuit held this "short-term" regulation unconstitutional. Retaining no express controls, the taxpayer in 1941 deeded securities to a local charitable foundation as trustee and beneficiary for five years.[20] A year later, the term was extended to run nine years from the date of extension.[21] When the trust income was treated as part of the settlor's income, it far exceeded the allowable charitable deduction.[22] As a result, the Commissioner assessed deficiencies for 1944, 1945, and 1946, but later conceded that the settlor was not taxable for the first two years, which were not covered by the regulation.[23] A divided Tax Court held that neither the

---

1942) (1-year term, settlor retained extensive controls); Edwin C. May, 3 T.C.M. 733, 740-3 (1944) (long-term, control).

Nontaxable: United States v. Pierce, 137 F.2d 428 (8th Cir. 1943) (10-year term, split decision); Helvering v. Bok, 132 F.2d 365 (3d Cir. 1942) (3-year term); Commissioner v. Chamberlain, 121 F.2d 765 (2d Cir. 1941) (4-year educational trust). *See* Helvering v. Achelis, 112 F.2d 929, 929-30 (2d Cir. 1940) (5-year educational trust). Admitting that *Chamberlain* and *Achelis* were distinguishable on their facts, the Second Circuit nevertheless questioned their validity in the *Lamont* case, supra at 876.

16. U.S. Treas. Reg. 111, § 29.22(a)-21 (1945). See Eisenstein, *The Clifford Regulations and the Heavenly City of Legislative Intention*, 2 TAX L. REV. 327 (1947); Guterman, *The New Clifford Regulations*, 1 TAX L. REV. 379 (1946); Lynch, *The Treasury Interprets the Clifford Case*, 15 FORD L. REV. 161 (1946); Pavenstedt, *The Treasury Legislates: The Distortion of the Clifford Rule*, 2 TAX L. REV. 7 (1946); Polisher, *The New Trust Regulations Under the Clifford Doctrine*, 24 TAXES 352 (1946).

17. See KENNEDY, FEDERAL INCOME TAXATION OF TRUSTS AND ESTATES § 6.23 (1948); Lynch, Pavenstedt, *supra* note 16.

18. U.S. Treas. Reg. 111, § 29.22(a)-21(c)(1) (1945). Unless the beneficiary is a charity, the settlor also remains taxable if he retains certain administrative powers over the trust corpus and the reversion will occur with fifteen years. *Id.*, § 29.22(a)-21(c)(2).

19. 202 F.2d 94 (7th Cir. 1953). The opinion involves two cases dealing with identical trusts set up by two sisters. Both the Tax Court and the Court of Appeals considered the cases together. For simplicity, reference to the taxpayers in this Note is in the singular.

20. *Id.* at 95. The powers of the charity as trustee were limited only in that the corpus upon reversion was to contain stock equivalent to that transferred. *Ibid.*

21. *Ibid.* The taxpayer also set up another trust, with a ten-year term, in 1943. *Id.* at 96.

22. Taxpayer Clark returned a net taxable income of $13,585.83 for 1946; Rutherford, $14,903.92. The trusts set up by each taxpayer earned $42,750.00. *Id.* at 96. Individuals, at that time, could deduct charitable contributions only up to 15% of their adjusted gross income. INT. REV. CODE § 23(o). See amendments effective through 1944 in P-H CUM. CH. SERV. pp. 14-A - 14-C.

23. Commissioner v. Clark, 202 F.2d 94, 96 (7th Cir. 1953). Taxability of trust

Clifford doctrine nor the regulation was applicable to charitable trusts.[24] On appeal, the Seventh Circuit passed over the charitable nature of the trust to give its wholesale endorsement to every objection raised by the taxpayer.[25] The court agreed that the regulation could not be applied "retroactively" to a trust already in existence and, further, that the trust term was not nine but ten years.[26] But what was "[m]ore important" in the eyes of the court, the regulation "creates a conclusive or irrebutable presumption" "that even Congress [is] without power to create" because it violates due process.[27] Furthermore, under Section 22(a), "the question as to whether the income from the trust was that of [the settlor] was one of fact" requiring a judicial hearing in each case.[28] Finally, the case law did not, according to the court, support taxation of the settlor on the facts of this case.[29]

Precedent does not support the court's cursory acceptance of the taxpayer's contention based on the "retroactive" application of the regulation. The court disposes of "retroactivity" with two sentences: the regulation cannot be applied to trusts in existence prior to its promulgation; and it cannot create taxable income where there was none previously.[30] Underlying both assertions is an assumption that the settlor would not have been taxable prior to the regulation. Even if the court could conclusively support this proposition,[31] a person has

---

income for years prior to January 1, 1946 is to be determined without reference to the *Clifford* regulations. U.S. Treas. Reg. 111, § 29.22(a)-21(f) (1945).

It is not clear why the Commissioner abandoned his claim for 1944 and 1945. He may have thought that the generally pro-taxpayer Seventh Circuit would decide that the case law did not support taxation for 1944 and 1945, and that such a decision would in turn undermine his chances for success under the regulation. Whereas, were the court to consider the regulation alone, attention would presumably be focused on its reasonableness rather than on how the court itself would have decided the case in the absence of any regulation.

24. Ruth S. Clark, Hazel S. Rutherford, 17 T.C. 1357 (1952). Three judges dissented. The majority chose its precedents judiciously, citing *Bok*, *Pierce*, *Chamberlain*, and *Achelis* to support its result, distinguishing *Lamont* on its facts, and ignoring *Anderson*, the *Lamont* dictum, and its own decision in *May* (a more recent case than the precedent it cites here). Above cases cited, *supra* note 15. See also note 74 *infra*.

25. Commissioner v. Clark, 202 F.2d 94, 98 (7th Cir. 1953).

26. *Ibid.*

27. *Id.* at 98, 99, 100.

28. *Id.* at 98.

29. "The regulation is in conflict with . . . all adjudicated cases." *Id.* at 99.

30. *Id.* at 98.

31. By adept choice of precedent, a court can support almost any desired result in this field. For an example, see the Tax Court majority opinion in *Clark*, 17 T.C. 1357 (1952), discussed, note 24 *supra*. The jumble of cases is outlined in notes 11-15 *supra*. In any event, the decisions provide no justification for the Seventh Circuit's *unsupported* assertion that "[t]he regulation is in conflict with . . . all adjudicated cases." Commissioner v. Clark, 202 F.2d 94, 99 (7th Cir. 1953). Further, it seems that the decisions contrary to the regulation are out of step with the Supreme Court's views, see p. 1244 *infra*.

no vested right of non-taxability.[32] The Supreme Court has held that even a prior *adjudication* holding an assignor non-taxable on assigned income does not preclude taxing him on later income under the same assignment.[33]

In addition, the Seventh Circuit's "thought" that the *Clark* trust ran for ten years, and therefore fell outside the regulation, contravenes both practice and policy. The regulation and the court decisions measure the term for tax purposes from the date of extension, not from that of the original trust deed.[34] Thus the Tax Court viewed the *Clark* trust as running for nine years.[35] And, in fact, the settlor had at no time surrendered control for more than nine years. Under the Seventh Circuit's theory, a settlor who surrenders his power of disposition for only short periods of time could eventually gain tax exemption through successive extensions of the trust term.[36]

Although the court's facile disposition of these two issues turns out to be legerdemain, it could provide other judges with convenient grounds for distinguishing *Clark*. But in view of the abbreviated treatment accorded these contentions, there can be little doubt that the real basis for the Seventh Circuit's decision lies elsewhere.[37]

The court erred in holding that even Congress would deny due process by erecting the conclusive presumption which the Treasury created in the "short-term" regulation. As a practical matter, this view invites a renascence of litigation at least until there remain no untried variations on the short-term trust.[38] The history of the *Clifford* doctrine indicates not only that the possible

32. Reinecke v. Smith, 289 U.S. 172 (1933). "[T]he subject of the tax is not the creation of trusts or transfer of the corpus from the grantor to the trustees, but the income of the trusts which accrued after . . . the effective date of the Revenue Act. . . ." *Id.* at 175. Also, *see* Burnet v. Wells, 670, 682-3 (1933).

33. Commissioner v. Sunnen, 333 U.S. 591 (1948). The Court reached this result on the ground that its intervening decisions had changed the "legal climate." *Id.* at 606-07. While a regulation promulgated to clarify muddied case law may not have the force of Supreme Court decisions, it does seem to affect the "legal climate."

34. U.S. Treas. Reg. 111, § 29.22(a)-21(c) (1945). See Commissioner v. Lamont, 127 F.2d 875 (2d Cir. 1942); Commissioner v. Barbour, 122 F.2d 165 (2d Cir.), *cert. denied*, 314 U.S. 691 (1941).

35. "The question . . . is whether the settlor-petitioners should be taxed . . . solely because the duration of the trust is 9 instead of 10 years. . . ." Ruth S. Clark, 17 T.C. 1357, 1361 (1952).

36. For example, the settlor of a five-year trust who, at the expiration of the trust, extended the term for another five years would not be taxed on the trust income for the second five years under the *Clark* rationale. And, apparently, any later extensions, however short, would not lead to taxability.

37. Having devoted a sum total of three sentences to "retroactivity" and the length of the trust term, the court turns to an extensive discussion of issues it labels "[m]ore important." Commissioner v. Clark, 202 F.2d 94, 98 (7th Cir. 1953). The former rulings appear to be the thirteenth bun in the baker's dozen the Seventh Circuit insisted on giving the taxpayer.

38. Subsequent to the promulgation of the *Clifford* regulations, litigation in the field declined markedly, while hundreds of cases had flooded the courts in the five years after *Clifford*. Although the regulations were expressly made inapplicable to prior years, see

variations are infinite but also that, in this area, case by case determinations do not produce inescapable rules of law.[39] Fortunately, the Constitution does not command *ad hoc* decisions; conclusive presumptions are valid if reasonable.[40] Two of the decisions cited by *Clark* struck down presumptions that all gifts within a certain period prior to death were made in contemplation thereof.[41] There a state of mind was inferred from the subsequent occurrence of an unpredictable event;[42] the regulation challenged here bases "ownership" on the terms of the trust deed. The *Hoeper* case, *Clark*'s third "controlling precedent," declared unconstitutional a state statute taxing husbands on their wives' income.[43] There the question was whether someone else's earnings could be merged with the taxpayer's; here it is whether he has in reality parted with the trust corpus.[44] The Supreme Court distinguished *Hoeper* on this very ground in upholding taxation of settlors on the income of revocable trusts.[45] Thus *Clark* ignored the closest possible precedent, to invalidate the regulation on the basis of earlier, clearly distinguishable decisions. Moreover, the high Court had on more than one occasion invited Congress and the Treasury to clean up the *Clifford* mess.[46] Since it is clear that a "conclusive

---

note 23 *supra*, many taxpayers who might otherwise have contested deficiency assessments apparently did not.

39. "[I]f [the *Clifford* doctrine] is to be continually refined by successive distinctions, each trifling in itself, we shall end in a morass from which there will be no escape; and the spate of decisions already poured upon us will be the earnest of eventual utter confusion. Perhaps it is best not to approach the issue dialectically at all, but merely by fiat. . . ." L. Hand, J., in Kohnstamm v. Pedrick, 153 F.2d 506, 510 (2d Cir. 1945). For illustrations of the inconsistency among decisions, see notes 11-15 *supra*.

40. "The question is whether [the standard] is one that an enlightened legislator might act upon without affront to justice. Even administrative convenience, the practical necessities of an efficient system of taxation, will have heed and recognition within reasonable limits. . . . A margin must be allowed for the play of legislative judgment. To overcome this [enactment] the taxpayers must show that . . . the lawmakers have done a wholly arbitrary thing, have found equivalence where there was none nor anything approaching it, and laid a burden unrelated to privilege or benefit." Burnet v. Wells, 289 U.S. 670, 678-9 (1933). See also Reinecke v. Smith, 289 U.S. 172, 178 (1933).

41. Heiner v. Donnan, 285 U.S. 312 (1932); Schlesinger v. Wisconsin, 270 U.S. 230 (1926).

42. "The young man in abounding health, bereft of life by a stroke of lightning within two years after making a gift, is conclusively presumed to have acted under the inducement of the thought of death. . . ." Heiner v. Donnan, 285 U.S. 312, 327 (1932).

43. Hoeper v. Tax Commission of Wisconsin, 284 U.S. 206 (1931).

44. *See* Helvering v. Clifford, 309 U.S. 331, 334 (1940). See note 56 *infra*.

45. Reinecke v. Smith, 289 U.S. 172, 178 (1933). *Cf.* Burnet v. Wells, 289 U.S. 670, 677-9 (1933).

46. *See* Harrison v. Schaffner, 312 U.S. 579, 583 (1941); Helvering v. Clifford, 309 U.S. 331, 334-5, 338 (1940). See also Helvering v. Stuart, 317 U.S. 154, 167 (1942).

Since Congress has the power "to carve out of § 22(a) a defined group of cases [like revocable trusts under § 166] to which a rule of thumb [will] be applied," Helvering v. Clifford, *supra* at 337-8, it seems clear that that prerogative can be delegated to the Treasury. Brushaber v. Union Pac. R.R., 240 U.S. 1, 26 (1916). And such power has been delegated. See note 48 *infra*.

presumption" based on the terms of the trust instrument can be constitutionally created, the "short-term" regulation is void only if it is unreasonable or fails to conform with the pertinent statute.[47]

Clark also strayed in holding that, under Section 22(a), a hearing is necessary in each case to determine whether a settlor is the owner of the trust income for tax purposes. Since there is no explicit statutory provision to that effect,[48] the court sought precedent in the case law. Misapplying *Hormel v. Helvering*[49] to gain support, *Clark* quoted *Clifford* as saying that a hearing on the facts is required.[50] But the Seventh Circuit failed to note that the *"absence of more precise standards or guides supplied by statute or appropriate regulations"* forced the Supreme Court to scrutinize "all the circumstances" in *Clifford*.[51] And the Court reiterated this plea for a nonjudicial statement of the *Clifford* doctrine two weeks after it decided *Hormel*.[52]

In the last analysis, the validity of the "short-term" regulation must turn on the question *Clark* treated so cavalierly—whether a trust term of less than ten years in itself provides a reasonable ground for taxing a settlor on trust income. This standard must be reasonable in the constitutional sense and also as a construction of Section 22(a) as interpreted by the courts.[53] Although

47. *See, e.g.*, Commissioner v. South Texas Lumber Co., 333 U.S. 496, 501 (1948). Also, *see* Estate of Sanford v. Commissioner, 308 U.S. 39, 52 (1939); Manhattan General Equipment Co. v. Commissioner, 297 U.S. 129, 134 (1936). Insofar as not inconsistent with express statutory provisions, regulations have the force and effect of law. Maryland Casualty Co. v. United States, 251 U.S. 342, 349 (1920). See, generally, Eisenstein, *Some Iconoclastic Reflections on Tax Administration*, 58 HARV. L. REV. 477, 509-47 (1945); Griswold, *A Summary of the Regulations Problem*, 54 HARV. L. REV. 398 (1941).

48. In fact, the power to promulgate regulations for all sections of the Code has been delegated without reservation. INT. REV. CODE §§ 61, 62, Brushaber v. Union Pac. R.R., 240 U.S. 1, 26 (1916).

49. 312 U.S. 552 (1941). There the Commissioner had argued §§ 166 and 167 before the Board of Tax Appeals. While an appeal was pending from the Board's decision, the Supreme Court decided *Clifford.* Thereupon the Commissioner in the court of appeals switched to § 22(a) via the *Clifford* doctrine and won. "Under these circumstances" the Supreme Court remanded the case to the Board to enable the taxpayer to present *any additional facts* which might "take his case out of the *Clifford* rule." *Id.* at 560. In view of its context—the absence of any applicable regulation and the collector's introduction of a new theory on appeal—*Hormel* hardly seems controlling here.

50. Commissioner v. Clark, 202 F.2d 94, 99 (7th Cir. 1953).

51. Helvering v. Clifford, 309 U.S. 331, 334-5 (1940) (emphasis added).

52. *See* Harrison v. Schaffner, 312 U.S. 579, 583 (1941). See also Helvering v. Stuart, 317 U.S. 154, 167 (1942) and note 48 *supra*.

53. Granting that the Treasury can constitutionally promulgate a regulation inferring "ownership" from the terms of the trust instrument, see notes 45-7 *supra*, the question remains whether the particular regulation created meets the constitutional standard of reasonableness. Under the statute, the question is whether the regulation reasonably effectuates the congressional intent. See note 47 *supra* and accompanying text. And since "[t]he broad sweep of [the] language [of section 22(a)] indicates the purpose of Congress to use the full measure of its taxing power," Helvering v. Clifford, 309 U.S. 331, 334 (1940), the question of reasonableness is, for all practical purposes, the same under the Constitution and under Section 22(a).

admitting the existence of "some confusion" in the field, the Seventh Circuit found it unnecessary to analyze the case law because the decisions "all in the main employ [all] the factors enumerated in Clifford."[54] In fact, the Commissioner "concede[d] that his determination of the deficiencies [for the pre-regulation years] was erroneous."[55] Thus *Clark*'s holding that the regulation was unreasonable as applied rests merely on the court's abrupt dismissal of previous decisions and on the Commissioner's perhaps mistaken concession regarding tax years prior to the regulation.

Actually, it seems quite reasonable to tax settlors on trust income solely because the corpus will revert within ten years. The basic question, as posed by *Clifford* and subsequent Supreme Court decisions, is whether the settlor has *in economic reality* parted with the corpus.[56] When the term is short, it is doubtful that control has in fact been relinquished.[57] The trustee is under a duty to the settlor as reversioner to preserve the corpus;[58] and few trustees would not manage the property according to reasonable suggestions from a settlor soon to reacquire possession.[59] Moreover, the creator of a short-term irrevocable trust seldom effects any change in his economic status or relationships.[60] Rather he intends simply to save taxes while disposing of his income

54. Commissioner v. Clark, 202 F.2d 94, 97 (7th Cir. 1953). The cases do not support this sweeping generalization. See notes 11-15 *supra*.

55. Commissioner v. Clark, 202 F.2d 94, 97 (7th Cir. 1953). See note 23 *supra*.

56. Helvering v. Clifford, 309 U.S. 331, 334 (1940). The high Court starts with the basic premise that the revenue laws are not to be avoided by "legal niceties" of property law. In order to embrace as many as possible of the infinite number of income-splitting devices, the Court has sketched its theory in broad outline, going far beyond what was necessary to decide most of the cases before it. A grantor remains taxable when he continues to exercise control over income-producing property or the income therefrom. Helvering v. Stuart, 317 U.S. 154 (1942); Helvering v. Clifford, *supra*. And even though his control may be suspended, a donor who derives economic benefits, even "non-material satisfactions," from the returns on income-producing property remains taxable on that income unless he has for all practical purposes parted with the property forever. Harrison v. Schaffner, 312 U.S. 579 (1941); Helvering v. Horst, 311 U.S. 112 (1940); Helvering v. Eubank, 311 U.S. 122 (1940). See generally, Pavenstedt, *The Broadened Scope of Section 22(a): The Evolution of the Clifford Doctrine*, 51 YALE L.J. 213 (1941); Note, 10 U. OF CHI L. REV. 488 (1943).

57. See note 11 *supra* and accompanying text.

58. 2 SCOTT, TRUSTS §§ 232-41 (1939).

59. *See* Helvering v. Bok, 132 F.2d 365, 366-7 (3d Cir. 1942); Commissioner v. Lamont, 127 F.2d 875, 876 (2d Cir. 1942); McKnight v. Commissioner, 123 F.2d 240, 242 (8th Cir. 1941); Helvering v. Elias, 122 F.2d 171, 173 (2d Cir.), *cert. denied*, 314 U.S. 692 (1941).

60. *See* Helvering v. Clifford, 309 U.S. 331, 335-6 (1940); cases cited, *supra* note 59. Examination of the facts in *Clark* leads to a like conclusion. Apparently, securities comprised the principal, if not the sole, source of the taxpayer's independent income. The trust in dispute was set up on the eve of United States entry into World War II. By virtue of increased dividends with the end of the depression and the beginning of the mobilization effort, the securities probably provided, and would for some time continue to provide, more income than the taxpayer desired in order to maintain her standard of

to the same beneficiaries who enjoyed it before.[61] He would not, of course, remain taxable if he parted with the corpus forever or postponed the reversion for a considerable period.[62] But he desires the opportunity to recapture the corpus within a few years because he may then need the income himself or have changed his mind as to suitable objects for his beneficence.[63] Furthermore, should the settlor retain a power to revoke after a term of years instead of a reversion, he would be taxable under a specific provision of the Code.[64] It is unreasonable to allow the taxpayer to circumvent the policy of that provision merely by juggling technical concepts of property law. True, drawing the line at ten years, as the Treasury did, is arbitrary—in the same sense that any dividing line is arbitrary. But the economic factors discussed above appear to support taxation of trust income to settlors to whom the corpus will revert within ten years.[65]

---

living. Taxes had also increased and could be expected to remain high for several years. Under these circumstances, and presumably to "save" taxes, the taxpayer was willing to commit part of her income to a charitable cause, managed by relatives, to which it would probably have gone anyway. But since either dividends or taxes, or both, could also be expected to decrease at some time in the future, the taxpayer retained a reversion in anticipation of a time when changed conditions might cause her to reconsider.

61. *See* Commissioner v. Lamont, 127 F.2d 875 (2d Cir. 1942); Leonard Farkas, 8 T.C. 1351, 1357 (1947), *rev'd*, 170 F.2d 201 (5th Cir. 1948). *See* Farkas v. Commissioner, 170 F.2d 201, 205 (5th Cir. 1948); United States v. Pierce, 137 F.2d 428, 433 (8th Cir. 1943) (dissenting opinions).

Even if the taxpayer does shunt his income in new directions, as appears to be the case in *Clark*, there is still no justification for permitting him to escape the full impact of the income tax. The choice of the short-term trust as the mechanism of transfer in itself suggests the intent to avoid taxes. See Kennedy, *Short-Term Trusts Today*, 30 TAXES 1006 (1952). And the taxpayer still retains the reversionary string, permitting him to retrieve the corpus before too much time has passed.

62. *E.g.*, Cushman v. Commissioner, 153 F.2d 510 (2d Cir. 1946); Jones v. Norris, 122 F.2d 6 (10th Cir. 1941); Commissioner v. Branch, 114 F.2d 985 (1st Cir. 1940). But where extensive controls have been retained by the settlor, many courts taxed him on that factor alone when there was no possibility, except subject to extensive contingencies, that the property would ever revert. *E.g.*, Littel v. Commissioner, 154 F.2d 922 (2d Cir. 1946); Byerly v. Commissioner, 154 F.2d 879 (6th Cir.), *cert. denied*, 329 U.S. 727 (1946); Foerderer v. Commissioner, 141 F.2d 53 (3d Cir. 1944).

63. See note 60 *supra*.

64. INT. REV. CODE § 166. See note 3 *supra* and accompanying text. Even there a settlor who has a "vested" power of revocation but can exercise it only after a long term of years would presumably be held non-taxable. *See* Helvering v. Dunning, 118 F.2d 341, 345 (4th Cir.), *cert. denied*, 314 U.S. 631 (1941). But no decision has as yet found a term long enough.

65. It would appear that the *Clifford* regulations have the tacit approval of Congress. "Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially re-enacted statutes, are deemed to have received congressional approval and have the effect of law." Helvering v. Winmill, 305 U.S. 79, 83 (1938). In recent years, Congress has been quick to act when distressed by non-congressional developments in this area of tax law. *E.g.*, INT. REV. CODE § 167(c) over-

The fact that the beneficiary falls outside the settlor's "intimate family group" should not preclude taxation. Many lower courts thought that the *Clifford* doctrine was so limited.[66] But the Supreme Court had merely stated that this circumstance called for "*special* scrutiny of the arrangement."[67] If taxability were to turn on where trust income goes, the logical line of demarcation would lie between discharge of legal obligations and other uses. But tax liability is thus limited only when the discharge of a legal obligation is the *sole* ground for taxation.[68] Granting that a settlor may remain taxable on income of a gratuitous irrevocable trust, his liability should not depend on the identity of the beneficiaries. Congress made no distinction between intra- and extra-family dispositions in taxing the income of revocable trusts to settlors.[69] And the Supreme Court, in a similar situation, could see no difference between a campaign or community chest contribution and a gift to the taxpayer's son.[70] If the settlor's purpose "can be [achieved] only by the expenditure of money or property," the identity of the beneficiary provides no rational basis for a tax distinction between settlors of otherwise identical trusts.[71]

The fact that the beneficiary of a short-term trust is a charity should provide the settlor with no income tax saving beyond the allowable deduction for charitable contributions. The Tax Court in *Clark*, however, held that neither the regulation nor the *Clifford* doctrine was applicable to charitable trusts.[72] Since the Treasury explicitly excluded charitable trusts from other sections of the *Clifford* regulations,[73] the lack of similar language in the ten-year provision indicates that no exemption was intended there. Nor do the decisions cited by the Tax Court provide sound authority for such a result.[74]

---

ruled Helvering v. Stuart, 317 U.S. 154 (1942); INT. REV. CODE §§ 191, 3797(a)(2) changed the rule of Commissioner v. Culbertson, 337 U.S. 733 (1949). It can scarcely be contended that Congress is unaware of the existence of the *Clifford* regulations.

66. See note 13 *supra*.

67. Helvering v. Clifford, 309 U.S. 331, 335 (1940) (emphasis added).

68. INT. REV. CODE § 167(c). See Guterman, *The Federal Income Tax and Trusts for Support—The Stuart Case and Its Aftermath*, 57 HARV. L. REV. 479 (1944).

69. INT. REV. CODE § 166, discussed *supra* note 3. See Elsie A. Drexler, 25 B.T.A. 79 (1932), *appeal dismisssed*, 65 F.2d 1015 (9th Cir. 1933) (charitable beneficiaries).

70. *See* Helvering v. Horst, 311 U.S. 112, 117 (1940) (assigned income).

71. *Ibid. See* United States v. Anderson, 132 F.2d 98, 101 (6th Cir. 1941), *cert. denied*, 318 U.S. 790 (1943).

72. Ruth S. Clark, 17 T.C. 1357 (1952).

73. U.S. Treas. Reg. 111, §§ 29.22(a)-21(c)(2), 29.22(a)-21(d)(2) (1945).

74. Helvering v. Bok, 132 F.2d 365 (3d Cir. 1942), relies heavily on the family circle rationale. *Id.* at 367. But see notes 67-71 *supra* and accompanying text. In United States v. Pierce, 137 F.2d 428 (8th Cir. 1943), the fact that the term was ten years, which would take it outside the present regulation, was regarded as significant. *Id.* at 432. Both Commissioner v. Chamberlain, 121 F.2d 765 (2d Cir. 1941) and Helvering v. Achelis, 112 F.2d 929, 929-30 (2d Cir. 1940), which distinguished charitable trusts, have been specifically questioned by the court that decided them. Commissioner v. Lamont, 127 F.2d 875, 876 (2d Cir. 1942). Moreover, the statements in *Achelis* are dicta.

Furthermore, the Code accords individuals and corporations who make outright gifts to charity only limited deductions for income tax purposes.[75] Decisions like that of the Tax Court in *Clark* permit the settlor of a temporary trust to escape that restriction. Should Congress desire to exempt taxpayers to the full extent of their charitable donations, it could allow an unlimited income tax deduction.[76] Absent such legislative action, courts should not fabricate an exemption benefiting only those wealthy enough to fund short-term trusts.

75. Individuals may deduct charitable contributions up to 20% of adjusted gross income, INT. REV. CODE § 23(o); corporations, up to 5% of net income, INT. REV. CODE § 23(q).

But the Code treats differently situations where charity alone, and not the donor as well, benefits. Thus genuine charitable trusts and foundations are tax exempt. INT. REV. CODE § 101. And the gift tax does not apply to charitable donations. INT. REV. CODE § 1004(a)(2).

See, generally, Clark, *How To Get the Most Out of the Deduction for Charitable Contributions by Individuals and Business*, PROCEEDINGS OF N.Y.U. 6TH ANN. INSTITUTE ON FEDERAL TAXATION 1015 (1948); Lynch, *The 'Charities' Provisions of the Internal Reveneue Code*, 10 FORD. L. REV. 234 (1941); Note, 34 VA. L. REV. 182 (1948).

76. See Abbell, *Human Nature, Charitable Contributions and Uncle Sam*, 28 TAXES 243 (1950).