



BEFORE THE STATE BOARD OF EQUALIZATION  
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of  
EVERETT S. SHIPP

Appearances:

For Appellant: Mr. J. Edward Haley, Attorney at Law

For Respondent: Mr. Burl D. Lack, Chief Counsel

O P I N I O N

This appeal is made pursuant to Section 18593 of the Revenue and Taxation Code from the action of the Franchise Tax Commissioner (now succeeded by the Franchise Tax Board) on protests of Everett S. Shipp to proposed assessments of additional personal income tax in the amounts of \$42.00 and \$122.88 for the years 1943 and 1944, respectively.

On August 2, 1932, Appellant and Edna H. Shipp were husband and wife. On that date, while living apart, they executed a "Community Property and Support Agreement" declaring their intention to adjust and determine their mutual rights with respect to their community property and the Appellant's obligation for the support of the wife and their two minor children. On September 15, 1932, Edna H. Shipp obtained an interlocutory decree of divorce. The court in its decree approved "the property settlement entered into between the parties" and ordered it filed. This decree became final on September 21, 1933, and both parties have subsequently remarried.

The agreement purported to list all the community property owned by Appellant and his wife, consisting of miscellaneous property and shares of stock in three corporations controlled and managed by Appellant (hereinafter designated as corporations A; B and C). Community property omitted by reason of mistake, inadvertence or concealment was by virtue of the agreement vested equally in the parties as tenants in common. Under the terms of the agreement Appellant's wife received a 1928 automobile, her

personal effects and the household furnishings. Appellant received the family home, three insurance policies on his life in the aggregate principal sum of \$9,000, a 1931 automobile, an airplane, the sum of \$41,600 due from corporation C and a contingent claim for a refund from that corporation in an unspecified amount, it having been stipulated that not less than \$31,600 of the money due from corporation C should be applied in discharge of Appellant's indebtedness to corporation A in the amount of \$42,500. It was further agreed that Appellant should pay to Edna H. Shipp the sum of \$350 per month "for and during her natural life" and \$100 per month for the support and maintenance of each of their two minor children during the period of their minority. As security for his undertaking to pay "to the party of the, first part, during her natural life time, the sums hereinbefore provided to be so paid and as security for the payment of the sums hereinbefore provided for the support and maintenance of the children of the parties hereto" Appellant and his wife agreed to assign their respective interests in the listed shares of stock to a trustee.

The securities transferred to the trustee were to remain in Appellant's name and, for so long as he was not in default, he was to receive the dividends and income therefrom. He retained all the incidents of ownership, including the right to vote the stock and within specified limits, to substitute other securities. All of the shares of stock were expressly made available to him for the purpose of maintaining his control and management of the several corporations. At the death of the wife all the trust property remaining in the hands of the trustee was to be returned to and be the property of the Appellant.

The sole issue in this appeal is whether the aggregate amount of the \$350 payments made by Appellant to his former wife during the years 1943 and 1944 was deductible from his income under the provisions of Section 8(o) of the Personal Income Tax Act (now Section 17317.5 of the Revenue and Taxation Code), This section allowed a deduction for any amount paid by Appellant to his former wife which was required to be included in her gross income under Section 7(k) of that Act (now Sections 17104 to 17107 of the Code). Sections 7(k) and 8(o) were similar in all respects to Sections .22(k) and 23(u), respectively of the Internal Revenue Code, The first sentence of Section 7(k) read as follows:

"In the case of a wife who is divorced or legally separated from her husband under a decree of divorce or of separate maintenance, periodic payments (whether or not made at regular intervals) received subsequent to such decree in discharge of, or attributable to property transferred (in

trust or otherwise) in discharge of a legal obligation which,, because of the marital or family relationship, is imposed upon or incurred by such husband under such decree or under a written instrument incident to such divorce or separation shall be includible in the gross income of such wife, and such amounts received as are attributable to property so transferred shall not be includible in the gross income of such husband."

The Commissioner contended that the payments were not deductible by Appellant as they were not made in discharge of an obligation imposed or incurred by reason of the family or marital relationship, but rather were payments for the assignment of the wife's interest in community assets. As support for his position he relied on Frank J. DuBane, 10 T.C. 992; C. C. Rouse, 6 T.C. 908; and Johnson v. United States, 135 F. 2d 125.

The DuBane case clearly holds that payments for the purchase of property from the wife are not deductible by the husband under Section 23(u) of the Internal Revenue Code. Johnson v. United States, supra; C. C. Rouse, supra; and Long v. Commissioner of Internal Revenue, 173 F. 2d 471, are authority for the proposition that the transfer of a wife's interest in community property for a consideration, as distinguished from an equal division thereof, constitutes a bargain and sale.

Neither the agreement nor the record herein shows the value of the listed property or the amount of income received by Appellant from the assigned shares of stock. Liquidation of the trust upon default, however, was subject to Appellant's right to substitute the sum of \$75,000 and receive back the deposited shares of stock.

Under Section 161a of the Civil Code Mrs. Shipp during the continuance of the marriage had a present, existing and equal interest in the community property. The Appellant has not called our attention to, nor has our research disclosed, any decision of the State or Federal courts holding the receipt of periodic payments in discharge of the wife's interest in such property to be within the scope of Section 7(k) of the Personal Income Tax Act or Section 22(k) of the Internal Revenue Code. As shedding light on the question, however, Article 7(k)-1(b) of the Personal Income Tax Regulations of 1943 (now Reg, 17104-17107 of Title 18 of the California Administrative Code), which was

substantially similar to Section 29,22(k)-1 of Federal Regulations 111, says, in part, that "Sec. 7(k) does not apply to that part of any periodic payment attributable to that portion of any interest in property transferred in discharge of the husband's obligation under the decree or instrument incidental thereto, which interest originally belonged to the wife."

Under the agreement before us it appears that Mrs. Shipp disposed of both her community property rights and her rights to support. Although the trust provisions of the agreement were construed in Pagel v. Shipp, 68 Cal. App. 2d 12, the court in that action did not; as Appellant contends, decide of which rights the monthly payments were in discharge, We must, accordingly, determine this question solely upon the facts in evidence,,

As shown by the agreement, Appellant and his former wife had acquired very substantial amounts of community property during the period of their marriage. Upon dissolution of the marital community Mrs. Shipp received from the community only a used automobile, the household furnishings and her personal effects. If we omit from consideration the monthly payments assumed by Appellant, there is a complete absence of consideration for this grossly unequal division of the community assets. To assume, however, that Mrs. Shipp relinquished her rights in the bulk of the community property without adequate consideration would be to ignore the realities of the situation. We must necessarily conclude, therefore, that the \$350 monthly payments constituted the consideration for the assignment by Edna H. Shipp of her rights in the shares of stock and other community property.

In Thomas E. Hogg, 13 T.C. 361, and Floyd H. Brown, 16 T.C. 623, the periodic payments in issue, as here, arose out of an agreement settling both the wife's property rights and support rights. In each case, the balancing of benefits received by the wife under the property division against those received by the husband, and other evidence, indicated the periodic payments to have been in consideration of the wife's waiver of support rights, and the court so found., Viewing the agreement before us in the light most favorable to Appellant, however, we are unable to see even a semblance of equality in the property division. Furthermore, if any part of the monthly payments was attributable to the waiver of support rights by Mrs. Shipp, rather than to the property settlement,, the Appellant has failed to present evidence upon which an allocation could be made. Upon the basis of the record before us, accordingly, we are unable to conclude that the disallowance by the Commissioner of Appellant's deductions in the aggregate amount of the monthly payments was erroneous,

O R D E R

Pursuant to the views expressed in the opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED,, ADJUDGED AND DECREED, pursuant to Section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Commissioner (now succeeded by the Franchise Tax Board) on protests of Everett S. Shipp to proposed assessments of additional personal income tax in the amounts of \$42.00 and \$12'2.88 for the years 1943 and 1944, respectively, be and the same is hereby sustained.

Done at Los Angeles, California, this 7th day of October, 1952, by the State Board of Equalization.

\_\_\_\_\_, Chairman  
Wm. G. Bonelli \_\_\_\_\_, Member  
J. H. Quinn \_\_\_\_\_, Member  
Geo. R. Reilly \_\_\_\_\_, Member  
Thomas H. Kuchel \_\_\_\_\_, Member

ATTEST: Dixwell L. Pierce, Secretary