



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeals of)
JOHN J. ELMORE, ET AL., TRUSTEES)
OF HETTY J. ELMORE TRUSTS)

For Appellants: R. C. Edwards,
Certified Public Accountant

For Respondent: Buri D. Lack, Chief Counsel;
A. Ben Jacobson, Associate
Tax Counsel

O P I N I O N

These appeals are made pursuant to section 18594 of the Revenue and Taxation Code from the action of the Franchise Tax Board on protests to proposed assessments of additional personal income tax as follows:

<u>Trust</u>	<u>Trustees</u>	<u>Taxable Year Ended</u>	<u>Amount</u>
I	John J. Elmore	3-31-57	\$ 1,265.47
	Ann Kelly Elmore	3-31-58	348.24
II	R. E. Jordan	3-31-57	27.61
	Hetty J. Jordan	3-31-58	22.95
III	Stephen H. Elmore	3-31-58	21.95
	Janet B. Elmore		

Appellants herein are the above named trustees of three separate trusts, designated I, II and III. The facts and issues are identical for each assessment, and though this opinion is framed as if it were a consideration only of Trust I,

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the **decision is** determinative of the questions **raised in connection** with Trusts II and III as **well**. 'The problem **involved** in each case is **whether** a trust **declaration** created a single trust with several beneficiaries, or separate trusts for each named beneficiary.

On August 16, 1955, John J. Elmore and Ann Kelly Elmore (trustees of Trust I, and hereafter referred to as "appellants") executed a declaration of trust in which they were designated as trustees and their four minor children were named as beneficiaries. The trust instrument was approved by the settlor, Hetty J. Elmore, who was the paternal grandmother of the beneficiaries. The **trust res** consisted of cash and bonds **totalling** \$16,000. On November 8, 1955, the **settlor died**.

The trust instrument provided that **all income from** the trust estate was either to be paid to or **accumulated for** the beneficiaries, one-fourth **each, until**

... each Beneficiary shall reach the **age** of twenty-one (21) years, When each **named** Beneficiary reaches the age of twenty-one (21) years, **the Trustees shall distribute** the trust estate to the **Beneficiaries** together with the undistributed **accumulations** thereon, the Trustees reciting that at the time of the creation of the trust each of the Beneficiaries owned an undivided one-fourth'. [sic] (1/4) interest therein. Should any prior distribution be made to or for **the** benefit of any Beneficiary, such **distribu-**
tion shall be deducted from any accumulated income of such Beneficiary.

In the event of the death of 'any beneficiary, without **issue, before distribution of his interest, the trust instrument** further provided:

... the remainder of said Beneficiary's interest in this trust shall remain in trust until the last surviving Beneficiary named herein has reached the age of **twenty-one (21) years, at which time the interest.**

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of the deceased beneficiary shall be distributed to the issue of said **Beneficiary**, if living, in equal shares if more than **one**, should there be no issue of such deceased Beneficiary living when **distribution** is to be made, then the share which would otherwise be distributed to such deceased Beneficiary if living, shall be added to the corpus of the trust **estate** and be distributed in equal shares to the surviving Beneficiaries.

The trust was to terminate in all events upon the death of the last **survivor** of a group of named persons, such group **consisting of** the appellant trustees and the beneficiaries.

The first tax returns **were** filed for the fiscal year ended March **31**, 1957. For that period appellants filed four separate returns, treating the declaration of trust as having created a separate trust for each beneficiary. **Each return** showed an identical amount **of income and tax**,

In March 1958, an action for declaratory relief **was** brought in the Superior Court of Imperial County on behalf of **the** minor beneficiaries and against the trustees and unborn issue of the minor beneficiaries, The primary relief: asked **for** was a declaration that the trust **instrument** executed on **August 16**, 1955, created four separate **and equal trusts**. On **May 14**, 1958, the court issued a decree to that effect.

Separate returns were similarly filed by appellants for the fiscal year ended March **31**, 1958. **Respondent determined** that the trust instrument had created a single trust **with four** beneficiaries, and that all income for each taxable year should have been reported as income of one trust. **Accordingly, additional** taxes were assessed for the **fiscal years ended March 31**, 1957, and March 31, 1958, It is from those **proposed additional** assessments that these appeals are taken.

Appellants argue that the decree of the superior court to the effect that four separate trusts were created constituted a reformation of the trust instrument which **should be given effect as of** the date the **instrument was initially**

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executed. The **decree**, however, does not in any way purport to reform or revise the language of the document involved, but only to interpret it. The question remains whether the **interpretation** is binding upon respondent under principles of **res judicata** or otherwise.

In determining the validity of a plea of **res judicata**, it is necessary to establish that the party against whom the **pleas** asserted was a party or in privity with a party to the **prior** adjudication, (Bernhard v. Bank of America, 19 Cal. 2d 807 [122 P.2d 892].) Clearly neither the respondent nor the State of California in any other, capacity was represented in the earlier declaratory action in the superior court; therefore respondent is not directly bound under principles of **res judicata** (In re L. A. County Pioneer Society, 40 Cal. 2d 52 [257 P.2d 1].)

A further argument, that the judgment **is** in rem and **conclusive** against the whole world, is not borne out by the language of the decree, which merely states that "**this judgment** shall be and is binding upon all the persons appearing in this **matter.**" Even a judgment in rem, moreover, does not **bind** the state where **it** has not been brought into the proceedings by appropriate pleadings and service of process, unless **the intent to bind it is** actually expressed in the statute providing for the proceeding or should fairly be inferred, (Berton v. All Persons, 176 Cal, 610 [170 P. 151]; Newcomb v. City of Newport Beach, 7 Cal, 2d 393 [60 P.2d 825].) **Section 1060 of the Code of Civil Procedure**, which provides for declaratory **relief actions**, does not expressly purport to bind the state and **no** compelling reason appears why the state **should be bound, in absentia**, by a proceeding such as that before us.

In determining **federal** income **tax** liability the federal courts have held that a focal adjudication **of property** rights **will** be given conclusive effect if it was decided on the merits in an adversary proceeding before a state court of **competent** jurisdiction, and if **no fraud** or collusion--is shown to have existed, (Freuler v. Helvering, 291 U.S. 35 [78 L. Ed. 634]; Eisenmenger v. Commissioner, 145 F.2d 103; Estate of Ostella Carruth, 28 T.C. 871,) The legal basis **for giving** effect **to such** a judgment is not that the United States is **bound** under principles **of res judicata**, **but is rather that** the state court has made a **conclusive** determination **of the property rights which are being taxed by the federal government.**

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When the courts speak of the vitiating effect of "collusion" they do not mean to imply fraudulent or improper conduct, but simply that all interested parties agreed to the order and that it was apparently to their advantage from a tax standpoint to do so. (Saulsbury v. United States, 199 F.2d 578.) The proceeding which resulted in the declaratory judgment involved here seems clearly to have been initiated for tax reasons. Though the complaint alleged the existence of a controversy, there appears to have been no real conflict of interest between the parties. The declaration obtained was economically advantageous to all of them from a tax standpoint, and no other real motive for litigation is evident. Following the precedent set by the federal courts, we must conclude that the judgment is not binding for tax purposes because "collusion" in this very loose sense was present. (See Estate of Arthur Sweet, 24 T.C. 488, aff'd, 234 F.2d 401, cert. denied, 352 U.S. 1878 [1 L. Ed, 2d 79].) We will thus proceed to consider the terms of the trust instrument itself,

It is well settled that it is the intent of the trustdr which controls in the interpretation of any trust instrument. The question of whether the trustor has created one trust or more than one trust depends primarily on the expressions of his intention in the trust instrument itself. (Wells Fargo Bank, etc., Co. v. Superior Court, 32 Cal, 2d 1 [193 P.2d 721]; Huntington National Bank v. Commissioner, 90 F.2d 876.)

The relevant provisions of the instrument here under discussion are essentially the same as those found in Appeal of Citizens National Trust and Savings Bank of Los Angeles, Trustee, Cal. St. Bd. of Equal., Dec. 16, 1959, Appeal of Samuel, Greenberg, Trustee, Cal. St. Bd. of Equal., Aug. 7, 1963, and Appeal of Title Insurance and Trust Co., Trustee, Cal. St. Bd. of Equal., Oct. 21, 1963. In each of those cases we held that but *one* trust was created. The factors which lead us to reach the same conclusion here are that the instrument is consistently framed in terms of a single trust with several beneficiaries (Hale v. Dominion National Bank, 186 F.2d 374, cert. denied, 342 U.S. 821 [96 L. Ed, 621]), and each of the beneficiaries had a contingent right to receive, in trust, the shares of the others, (McHarg v. Fitzpatrick, 210 F.2d 792; Fort Worth National Bank v. United States, 137 F. Supp. 71.) We conclude that respondent properly combined the reported income and treated it as the income from a single trust,

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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 Board on protests to proposed assessments of additional personal income tax as follows:

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III	Stephen H. Elmore Janet B. Elmore	3-31-58	21.95

be and the same is hereby sustained,

Done at Sacramento, California, this 27th day of October, 1964, by the State Board of Equalization.

Paul R. Leake, Chairman
Lobby W. Lynch, Member
Richard Stein, Member
_____, Member
_____, Member

ATTEST: W. Freeman, Secretary