

Appeal of William J. and Elizabeth G. Cusack

The issue presented in this appeal is whether capital gains realized by a trust are taxable to the appellants under the grantor trust provisions of section **17781** et seq. of the Revenue and Taxation Code.

In 1974 appellants created the Cusack Family Trust. The appellants were grantors and lifetime beneficiaries, The trustees were appellants' two **sons-in-law** and one of appellants' daughters.

Article 3 of the trust provides for quarterly income distributions to appellants, principal distribution upon the written instruction of the grantors, and discretionary principal distribution by the trustees as they deem **necessary** for the grantor's reasonable comfort, support or maintenance. Article 6 states:

During the lifetime of both Trustors either of them may revoke the trust as to the revoking party's community one-half of the trust assets, The power of revocation shall be exercised by written notice delivered to the other **Trustor** and the Trustees.

This trust may be amended during the lifetime of both Trustors by the joint written consent of both Trustors.

Upon the death of either **Trustor**, this trust shall become irrevocable and not subject to amendment or modification in any manner whatsoever.

On January 15, 1977, appellants executed the following supplement to the Trust:

The Trustors declare that it is now and **since the** inception of this Trust has been their intention that all capital gains realized in said Trust shall remain in the Trust and not be considered as income distributable to Trustors **or** subject to withdrawal by Trustors or either of them.

During 1977 and 1978 the trust received income from dividends, interest, and capital gains. The capital gains were reported as fiduciary income on the trust's tax returns, while the remainder of the trust income was reported on appellants' joint personal income tax returns.

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In the course of examining the fiduciary returns of the trust, respondent determined that the entire trust was a grantor **trust**, and the capital gains should have been included in **appellants'** returns. Proposed assessments were issued, appellants protested, and respondent affirmed the assessments. This **timely** appeal followed.

When a grantor is treated as the owner of any portion of a trust, as specified in chapter 9, article 5, of the **Personal Income Tax Law**, the income, deductions, and credits attributable to that portion of the trust are included in computing the taxable income and credits of the grantor to the extent that such items would be applicable to an individual. (**Rev. & Tax. Code, § 17781.**) One of the situations in which a grantor is treated as the owner of a trust is that in which the grantor has the power to revoke.

The grantor shall be treated as the owner of any portion of a **trust**, whether or not he is treated as such owner under any other provision of this article, where at any time the power to revest in the grantor title to such portion is exercisable by the grantor or a nonadverse party, or both. (**Rev. & Tax. Cod?, § 17789, subd. (a).**)

Appellants argue that their 1977 amendment of the trust precluded them from regaining title to any capital gains, making that portion of the trust irrevocable **and**, therefore, not subject to the grantor trust provisions. Respondent argues that the amendment merely modified article 3 regarding distribution of income and principal during the grantors' lifetimes, **but** did not affect the ability of appellants to revoke the trust and revest all the trust assets, including capital gains, in themselves.

The power of revocation in article 6 is, on its face, applicable to all the trust assets. In addition, the law of California favors the revocability of trusts, providing that a voluntary trust is revocable unless expressly made irrevocable by the instrument creating the trust. (**Civ. Code, § 2280.**) Given these factors, we believe that a clear statement of irrevocability is required to exclude any particular assets from the power of revocation which appellants **have** retained over this trust. We cannot conclude that the ambiguous language of the 1977 amendment so restricts appellants' power to revoke.

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We find that appellants had the power to revoke the trust in its entirety. Since, upon revocation, the trustee must transfer his title in the entire trust estate to the grantors (Civ. Code, § 2280), the grantors had the power to re-vest in themselves title to the capital gains. The entire **trust**, including the capital gains, is a grantor **trust**, with all items of trust income taxable to appellants. The action of the Franchise Tax Board is, therefore, sustained.

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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 the protest of William J. and Elizabeth G. Cusack against proposed assessments of additional personal income tax in the amounts of \$1,143.23 and \$295.30 for the years 1977 and 1978, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 5th day of January, 1982, by the State Board of Equalization, with Board Members Mr. Reilly, Mr. Dronenburg, and Mr. Nevins present.

_____	, Chairman
George R. Reilly	, Member
Ernest J. Dronenburg, Jr.	, Member
Richard Nevins	, Member
_____	, Member