Estate Tac -- Deductions -- Life Beneficiary with Power to Invade Corpus of Charitable Remainder

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tial damages limits the compensatory function of a defamation action since direct proof of specific injury caused by defamation is often difficult if not impossible.\textsuperscript{35}

By the very nature of the harm resulting from defamatory publications, it is frequently not susceptible of objective proof. Libel and slander work their evil in ways that are invidious and subtle. The door of opportunity may be closed to the victim without his knowledge, his business or professional career limited by the operation of forces which he cannot identify but which, nonetheless, were set in motion by the defamatory statements.\textsuperscript{36}

In light of these considerations—an uncertain and perhaps unnecessary method of regulating jury determinations, the questionable vindicatory value of a judicial verdict without damages, and the inherent difficulty of the proof required—it seems more desirable to permit the award of substantial compensation for defamatory harm based on a presumption of damages. Maintenance of the full scope of this presumption, coupled with more thorough instructions to juries and a greater readiness to review their damages awards, is a preferable alternative to the requirement of direct proof of damage to qualify for substantial award—which seems to be the most probable effect of \textit{Bouligny}. This alternative permits compensation for unprovable but present harm, and also offers greater protection from unreasonable damages awards.

Finally, it must be admitted that it remains basically unclear exactly what the \textit{Bouligny} dictum intends to require of a plaintiff seeking compensation for damages resulting from actionable per se defamation. This added uncertainty as to what he must do to gain substantial compensation for defamatory harm should be clarified at the court's earliest opportunity.

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\textbf{Estate Tax—Deductions—Life Beneficiary with Power to Invade Corpus of Charitable Remainder}

The Internal Revenue code of 1954 provides that in the determination of the taxable estate the value of all transfers, bequest, legacies, or devises of property to certain public, charitable, or

\textsuperscript{35} Afro-American Publishing Co. v. Jaffe, 366 F.2d 649, 660 (D.C. Cir. 1966); \textit{Restatement of Torts} § 621, comment a (1938).

\textsuperscript{36} I F. Harper & F. James, \textit{The Law of Torts} 468 (1956).
religious organizations is to be deducted from the value of the gross estate.\footnote{1} By allowing the deduction congress hoped to shift to the private sector charitable expenditures it would probably otherwise have to assume. The theory seems to be that the private sector can maintain the charitable programs more economically, efficiently, and with less political interference than either federal or state government. Realizing the possibilities created for obtaining funds, the charitable organizations have undertaken extensive campaigns for contributions; and the response has been good since there are tax advantages in charitable giving for both the wealthy and those with more moderate means.\footnote{2}

A frequently used method of giving entails the establishment of a trust directing the trustee to pay the income to a private lifetime beneficiary with the remainder over to charity. The trustee is also given the power to invade the corpus of the trust in favor of the lifetime beneficiary. By using this method the testator hopes to insure the comfort and happiness of the private beneficiary and at the same time obtain a charitable deduction. In the absence of a power to invade, the amount of the deduction can be easily determined.\footnote{3} But where such a power exists a considerable amount of controversy has developed over what circumstances should exist before a deduction is allowed. The source of this controversy is the uncertainty as to the value of the interest charity will ultimately receive. The Treasury Department has taken the position that a deduction is allowable; but, to insure that charity will take an amount commensurate to the deduction allowed, the Treasury requires that the value of the remainder interest be “presently ascertainable and, hence severable from the private interest”\footnote{4} and that the possibility of an invasion be “so remote as to be negligible.”\footnote{5} These requirements may seem to present few complexities

\footnote{1 INT. REV. CODE of 1954, § 2055.}
\footnote{2 See generally, Lowndes, Tax Advantages of Charitable Giving, 46 VA. L. REV. 394 (1960); Merritt, Tax Incentives for Charitable Giving, 36 TAXES 646 (1958); Yohlin, Tax Blessings of Charitable Giving, 10 PRAC. LAW 43 (May 1964); Young, Tax Effects of Gifts to Charity, 41 TAXES 351 (1963).}
\footnote{3 Treas. Reg. § 20.2055-2(A) (1958). This section allows a deduction for the present value of the remainder interest created when property is placed in a trust to pay the income to a private lifetime beneficiary and then to pay the principal to charity. The remainder interest is valued according to the rules stated in § 20.2032-7.}
\footnote{4 Treas. Reg. § 20.2055-2(A) (1958).}
\footnote{5 Treas. Reg. § 20.2055-2(B) (1958).}
but in their application the courts have been faced with three major questions: In what order should the tests be applied? What does "presently ascertainable" mean? And what is "so remote as to be negligible?"

To obtain a deduction the burden is on the taxpayer to show that the necessary requirements have been met. First, he must prove that the power of invasion is limited by a "presently ascertainable" standard. Without such a standard no deduction is allowed. If such a standard is found, he must then prove that the possibility of an invasion is negligible; but where no standard exists the courts refuse to consider this problem. In those cases where there is a standard but the possibility of invasion is more than remote the courts must decide what amount of the claimed deduction is to be denied.

In Moffet v. Commissioner the Fourth Circuit denied the entire deduction when it found that the possibility of invasion was not "so remote as to be negligible." In that case the testator established a million and a half dollar trust from which yearly payments were to be made to his widow for life. Charity was to receive the remainder. In denying the deduction the court was unimpressed by the taxpayer's argument that a deduction should be allowed for the present value of the charitable remainder computed after subtracting from the original trust corpus an amount determined by the multiplication of the expected annual invasion by the widow's life expectancy. This decision was clearly repudiated by the Second Circuit in Schildkraut v. Commissioner. There, on substantially the same facts, a partial deduction was allowed. The court held that the requirement that the possibility of invasion be negligible did not apply in this context. It felt that the proper test was whether there is an interest that is "presently ascertainable" and "assurance" that charity will ultimately receive it. In short, the court took the position of the Treasury Department in Revenue

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7 Ithaca Trust Co. v. United States, 279 U.S. 151 (1929).
9 269 F.2d 738 (4th Cir. 1959).
10 368 F.2d 40 (2d Cir. 1967).
Ruling 54-285\textsuperscript{11} that "if the facts indicate the probability of an invasion to a limited extent which is calculable in accordance with an ascertainable standard, the deduction should be denied only to such extent." From these two cases it is clear that there is a serious dispute as to whether a negligible possibility of invasion is a prerequisite for any deduction. In the light of this dispute it would be advisable for the testator to utilize some other tax saving method where it appears that even a limited invasion is probable. The simplest solution would be an outright devise by the testator, after consultation with an attorney, to the widow and charity of interests approximately equal in value to those they would have taken under the trust.

There has been some criticism of the requirement that a "presently ascertainable" standard must exist within the will before a deduction is allowed. Those who criticize are in effect rejecting the "two-step" analysis. In a dissent in \textit{Merchants National Bank v. Commissioner}\textsuperscript{12} Mr. Justice Douglas, with whom Mr. Justice Jackson concurred, argued that in determining whether the standard was ascertainable the court should consider such outside factors as the frugality and conservatism of the trustee, the habits of the beneficiary, and the nature of the investments. These factors might make certain what on the face of the will appears uncertain; thus, the likelihood of invasion should be the determining factor. By using this test it is felt that the congressional policy of favoring charity would be better served. In support of this argument cases can be cited where the charitable deduction was denied even though the facts showed that, as a matter of common experience, the charitable beneficiary was as assured of receiving the corpus intact as in other cases where an ascertainable standard was found and a deduction allowed.\textsuperscript{13} This inconsistency seems to be the basis for most objections to the present "two-step" test.

In answer to these criticisms the Court has said that "[w]hat common experience may regard as remote in the generality of cases

\textsuperscript{11} 1954-2 \textsc{cum. bull.} 302.
\textsuperscript{12} 320 U.S. 256 (1943).
may nonetheless be beyond the realm of precise prediction in the single instance." In sum, the Court was pointing to the additional uncertainty created by the absence of a "presently ascertainable" standard. Whether or not a standard exists would in itself be an important factor in determining the likelihood of an invasion. Without a limiting standard the courts can only speculate as to the needs or desires of the lifetime beneficiary. Of course the courts can look to the beneficiary's past station in life and draw some conclusions as to his frugality but in light of the general uncertainty surrounding human affairs no adequate projection can be made. In fact, without first establishing a standard it is difficult to see how the likelihood of an invasion can be determined. Furthermore it must be remembered that the tax is imposed on the transfer of property or the act of the testator and that when he creates a trust giving charity a vested interest subject to divestment for the benefit of the private beneficiary he is only secondarily concerned with the charitable beneficiary. When this intent is considered in conjunction with the broad power of invasion given the trustee it does not seem unfair to deny the deduction.

What language constitutes an "ascertainable standard?" In answer to this question the Court has said that the purposes for which the corpus may be invaded must be subject to "reliable prediction" rather than "rough guesses" or "approximation" and that there must be a standard "fixed in fact and capable of being stated in definite terms of money." The first class of standards held to be ascertainable are those where the trustee's power of invasion is limited to the amount necessary to insure that the lifetime beneficiary will continue to live according to his or her accustomed standard of living. Other language held to connote the objective station in life standard includes "support, maintenance, welfare, and comfort," "comfort and support," "comfort and welfare,"

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15 Young Mens Christian Ass'n v. Davis, 264 U.S. 47 (1924).
17 Id. at 261.
18 Ithaca Trust Co. v. United States, 279 U.S. 151, 154 (1929).
19 Ithaca Trust Co. v. United States, 279 U.S. 151 (1929); Lincoln Rochester Trust Co. v. Commissioner, 181, F.2d 424 (2d Cir. 1950); Estate of Leonard O. Carlson, 21 T.C. 291 (1953).
22 Blodget v. Delaney, 201 F.2d 589 (1st Cir. 1953).
"care and maintenance,"23 and "comfortable maintenance and support."24 The objective standard has also been implied where the invasion was limited to periods created by physical or economic emergencies.25

Where there is subjective language such as "use and benefit,"26 "comfortable support and maintenance and for any other reasonable requirements,"27 "need or desire,"28 "support, maintenance, and comfort, including luxuries,"29 and "welfare, comfort, and happiness,"30 the courts have been prone to say that the standard is unascertainable. Expansive language directing the trustee to invade the corpus for the proper maintenance and support of the beneficiary to the same generous extent that the testator, if living, could do has caused an otherwise objective standard to fail for subjectivity.31 Directions by the testator to the effect that the trustee in exercising his discretion is to favor the private beneficiary over the charity have also rendered the remainder nondeductible.32

23 Estate of Nellie H. Jennings, 10 T.C. 241 (1946).
24 Hartford-Connecticut Trust Co. v. Eaton, 36 F.2d 710 (2d Cir. 1929).
25 Payment by the trustee was to be limited to cases of need "on account of any sickness, accident, want, or other emergency," Commissioner v. Wells Fargo Bank & Union Trust Co., 145 F.2d 130 (9th Cir. 1944); "in case she should, by reason of accident, illness, or other unusual circumstances so require," Commissioner v. Bank of America Trust & Savings Ass'n, 133 F.2d 753 (9th Cir. 1943); "in case of illness or other emergency" affecting the beneficiary or his family, Union & New Haven Trust Co. v. United States, 265 F. Supp. 800 (D. Conn. 1967); and for any "emergency, illness, or necessity," Estate of Oliver Lee, 28 T.C. 1259 (1957).
26 Newton Trust Co. v. Commissioner, 160 F.2d 175 (1st Cir. 1947).
27 State Street Bank & Trust Co. v. United States, 313 F.2d 29 (1st Cir. 1963).
28 Gammons v. Hassett, 121 F.2d 229 (1st Cir. 1941), cert. denied, 314 U.S. 673 (1941).
30 United States v. Powell, 307 F.2d 821 (10th Cir. 1962).
31 Kline v. United States, 202 F. Supp. 849 (N.D. W.Va. 1962), aff'd per curiam, 313 F.2d 633 (4th Cir. 1963). Directions to the trustee to make payments "for any other purpose which my trustee shall deem expedient, necessary, or desirable for the benefit and use of my sister," Zentmayer v. Commissioner, 336 F.2d 488 (3d Cir. 1964); "for any purpose which may add to her (beneficiary's) comfort or convenience," Seubert v. Shaughnessy, 233 F.2d 134 (2d Cir. 1956); and "of such portion of the trust as my sister may in writing request with her judgement as to need being conclusive," Merrill Trust Co. v. United States, 167 F. Supp. 474 (D. Me. 1958), have rendered an otherwise objective standard subjective.
32 Typical examples are directions that the trustee's first object to be accomplished is to provide for the beneficiary in "such manner as she may desire," Henslee v. Union Planters Nat'l Bank & Trust Co., 335 U.S. 595 (1949); that in the exercise of his discretion he is to be liberal to the life time beneficiary, Merchants Nat'l Bank v. Commissioner, 320 U.S. 256
Furthermore the use of subjective or expansive language in conjunction with a limitation permitting invasion only in cases of emergency have caused the standard to be unascertainable. It seems though that in this latter situation the courts will more readily imply an objective standard.

In the construction and interpretation of a will the primary purpose of the court is to ascertain the intention of the testator. To do this the courts must necessarily interpret the will in accordance with the applicable state law since it is that law which ultimately determines the extent of the trustee's power of invasion. This dependence upon state law in determining the existence of a standard creates what at first appears to be an inconsistency between the courts' words and actions. The federal courts have consistently refused to consider outside circumstances in order to make the standard ascertainable. Yet we find that the state courts construe the language used by the testator in the light of such outside circumstances as the condition of the testator's family, how he was circumstanced, his relationship to the beneficiary, the financial condition of the beneficiary (at least where it was known to the testator), and even the motives which are reasonably supposed to influence him. Thus, in a sense, extrinsic circumstances sometimes in-

(1943); that he is to give "sympathetic consideration to any request" made by the beneficiary, Union Trust Co. v. Tomlinson, 355 F.2d 40 (5th Cir. 1966); and that his powers are to be liberally construed in favor of the private beneficiary, Industrial Trust Co. v. Commissioner, 151 F.2d 592 (1st Cir. 1945), cert. denied, 327 U.S. 788 (1946). 

38 In DeCastro v. Commissioner, 155 F.2d 254, (2d Cir. 1946), cert. denied, 329 U.S. 727 (1946), the court held that a provision allowing invasion if other income did not "amply" provide for the life beneficiary's needs rendered the remainder nondeductible. A similar result was reached in Estate of Helen H. Thompson, 27 F-H Tax Ct. Rep. & Mem. Dec. ¶ 58-100 (1958), where the trustee was directed to make payments "for the best interest of the beneficiary during illness or emergency of any kind."


38 Salisbury v. United States, 378 F.2d 700 (2d Cir. 1967).

39 Blodget v. Delany, 201 F.2d 589 (1st Cir. 1953).

37 Seubert v. Shaughnessy, 233 F.2d 134 (2d Cir. 1956). The court indicated that extrinsic facts such as the financial condition of the life beneficiary were irrelevant to the question of whether or not there was an ascertainable standard.

directly enter into the determination of an “ascertainable standard.” Despite the apparent inconsistency there is a distinction that can be drawn between these two practices. In the latter instance the courts are using the outside factors to determine the testator’s intent expressed in the language of the will. In the former if the court finds that the language is subjective it will not allow the deduction just because those same factors show that the likelihood of invasion is remote.

What is “so remote as to be negligible?” Must the taxpayer prove that it is impossible for charity not to take? This question was answered in the negative by the court in Hamilton National Bank v. United States. The court made it clear that a charitable deduction will be allowed even though some uncertainty exists. In defining “so remote as to be negligible” the court said “a negligible possibility is a possibility that would in the ordinary and reasonable affairs of men be disregarded in arriving at a present valuation of a future remainder interest in a serious business transaction, with no deduction in the value of the remainder interest being made by reason of the existence of such a possibility.” Whether such a possibility exists is a question of fact. No general rules or conclusions can be reached as each case must necessarily be decided on its own particular facts.

What facts are to be considered? The courts have stated that only those facts existing at the testator’s death are relevant. In

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39 Where there has been a state court decision which is neither collusive nor inoperative, on the extent of the trustee’s power of invasion, it seems that the federal courts in applying the federal tax statute must make their determination in accordance with the state court ruling. Henrickson v. Baker-Boyer Nat’l Bank, 139 F.2d 877 (9th Cir. 1944). Professors Lowndes and Kramer point out that where there is no state court decision on the particular trust under consideration the federal courts generally construe and apply the state law for themselves. C. LOWNDES & R. KRAMER, FEDERAL ESTATE AND GIFT TAXES, 57 (2d ed. 1962). In construing the will the federal courts must necessarily take into account all the factors which are relevant in the particular state jurisdiction to the interpretation of a will. To do otherwise would be unrealistic as no accurate interpretation of the language used could be made. Furthermore, if the outside factors were completely ignored a tax might often be imposed on interests which by State Law were certain to go to charity.


42 Ithaca Trust Co. v. United States, 279 U.S. 151 (1929); Lincoln Rochester Trust Co. v. McGowan, 217 F.2d 287 (2d Cir. 1954).
Lincoln Rochester Trust Co. v. McGowan the court said that "actual events occurring after the testator's death may never be substituted for the estimate of probable events made as of the time of the testator's death and based upon circumstances as they existed on that date." For later events to be considered their admission must "have sufficiently high probative value in establishing or clarifying the circumstances as they existed at the time of the testator's death."

In Allen v. First National Bank property was left by the testator to his wife for life and then to the children (including those born posthumously) and descendants that survive her. In the event there were no survivors the property was to go to designated charities. In allowing a deduction the court had to decide whether or not it was proper to admit evidence of the fact that no child had been born posthumously. In admitting the evidence the court said that it was merely evidence establishing the existence of a state of facts which existed at the date of the testator's death. The evidence tended to establish that as of the date of death there would not and could not be any child born of the marriage. Later events held inadmissible included an actual invasion of the corpus after the date of death and evidence of the later death of the private beneficiary. The distinction is, as the above court pointed out, that evidence of this nature has no connection at all with the facts existing at the time of the testator's death.

The factors which seem to weigh most heavily with the courts are the life expectancy of the beneficiary, the beneficiary's past standard of living, the income of the trust, and the independent means of the beneficiary available for the payment of such expenses. In their consideration of this last factor another important question must be answered by the court: does the applicable state law require that the lifetime beneficiary substantially exhaust his own

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217 F.2d 287, 293 (2d Cir. 1954).
Id.
169 F.2d 221 (5th Cir. 1948).
Wells Fargo Bank & Union Trust Co. v. Commissioner, 145 F.2d 132 (9th Cir. 1944). The court said that it was improper to be influenced by such evidence.
Estate of Eunice M. Greene, 11 T.C. 205 (1948); Estate of John W. Holmes, 5 T.C. 1289 (1945).
private resources before an invasion can be made? In *Christy v. Commissioner* a deduction was not allowed principally because Pennsylvania had no such requirement. Had this case arisen in another jurisdiction the deduction probably would have been allowed. Some other factors considered by the courts include the beneficiary's ability to work, the probability that he will continue to work, the number of his dependants, the state of the beneficiary's health, and the character of the trustee.

In reviewing the decisions of the courts in this area it is evident that much confusion exists. But from these cases several general propositions can be deduced. First, the power of invasion should be limited to that amount necessary to maintain the beneficiary according to his prior station in life. Secondly, subjective or expansive language should not be used to limit the power of invasion as it seems to be an invitation to a law suit. Furthermore most charitable interests have been held nondeductible where this language was used. Thirdly, if tax considerations are the prime concern, a provision to the effect that the beneficiary must exhaust his assets before an invasion can be made should be included in the testator's will if the applicable state law has no such requirement. Lastly, the testator should not rely upon getting a partial deduction. If a trust has been established and it later appears that a deduction will be denied consideration should be given to disclaiming the power of invasion.

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40 8 T.C. 862 (1947).
49 Union & New Haven Trust Co. v. United States, 265 F. Supp. 800 (D. Conn. 1967). In Connecticut the invasion of the corpus is conditioned upon the exhaustion of the beneficiary's assets.
63 Int. Rev. Code of 1954, § 2055. This section provides that included in the amount deductible is the value of all the interest which passes to charity as the result of an irrevocable disclaimer. For a deduction to be taken the disclaimer must be filed in the probate court before the estate tax return is filed.