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Charitable Contributions Under the Revenue Act of 1964

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COMMENTS

CHARITABLE CONTRIBUTIONS UNDER THE REVENUE ACT OF 1964

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I. INTRODUCTION

Our federal tax system encourages charitable contributions. This policy of favoritism is based upon the premise that gifts to charity in turn enrich the public in general. Indeed, Congress has long encouraged donations to qualified charitable organizations, by making gifts deductible for tax purposes.[1] By permitting these deductions, the federal tax laws are, in effect, openly subsidizing qualified charities. Thus, the charitable donation emerges as a hybrid in our tax network: it is an otherwise non-deductible "personal expense," yet deductible in ever-increasing amounts and to a correspondingly increasing class of organizations.[2]

1. See note 14 *infra.*

2. Charitable contributions may serve not only to decrease the tax dollar owed by the taxpayer, but in some cases may even increase his net income remaining after taxes. See, *e.g.*, Koch, *The Treasury's Bargain Counter*: *Contributions*, 33 TAXES 249 (1955); Lowndes, *Tax Aspects of Charitable Gifts*, 46 VA. L. REV. 394 (1960); Palmer, *Tax Saving Through Charitable Giving*, 36 TAXES 40 (1958); Penick, *Tax Economics of Charitable Giving*, 38 TAXES 111 (1960); Rogers, *Gifts to Charity Can Increase Income Even in the Lowest Brackets: How it works*, 9 J. TAXATION 230 (1958); Wallace, *How to Save Money by Giving it Away*, 47 MARQ. L. REV. 1 (1963); Wormser, *Gifts to Charity Can Actually Put Money In Your Pocket, if You're Rich Enough*, 4 J. TAXATION 211 (1956).

But for a discussion which favors charitable deductions only to the extent that the donor does not save more on taxes than the value which accrues to the charitable organization, see Rudick & Gray, *Bounty Twice Blessed: Tax Consequences of Gifts of*

The charitable contribution deduction was conceived in public policy, a fact which was best exemplified by one writer's paraphrase of the immortal words of the Bard, "The quality of the charity is not strained. It is twice blessed. It blesses him that gives and him that takes."[3] In other words, the charitable donee benefits from the gift made by the philanthropic donor, while the donor derives personal satisfaction from making a generous contribution; he receives a second stimulant in the form of a tax deduction. At the same time, the government, as an ever-present third party, adds its approval to the transaction.[4]

The theory of encouraging gifts to eleemosynary organizations, however, is not viewed *in vacuo*. A much broader view is needed: the public policy aspect of charitable giving is only realistic when coupled with certain restrictions imposed upon the donor, the gift, and the charitable recipient. The purpose of this paper is to deal with the limitations expressly and impliedly imposed upon the donor, with a particular emphasis on the changes effected by the Revenue Act of 1964.

II. PERCENTAGE LIMITATIONS

A. *"To Give or Not to Give": A Tax Concept Matures*

Deductible charitable contributions may be made by individuals, partners, corporations, trusts and estates.[5] Congress first gave its legislative blessing to charitable donations in 1917, when it permitted to the individual an income tax deduction for charitable contributions up to a maximum of 15 per cent of his taxable income.[6] Congress found it nec-

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Property to or in Trust for Charity, 16 TAX L. REV. 273 (1961). See also Silverstone, *Charitable Giving: The Need for a Logically Closed System*, 42 TAXES 429 (1964) (a master's thesis which simultaneously raises loopholes in charitable giving and condemns acquiescence by the Internal Revenue Service, contending for a more uniform system).

3. Yohlin, *Tax Blessings of Charitable Giving*, 10 PRAC. LAW. 43 (1964).

4. The Supreme Court has expressed a liberal policy in the interpretation of statutes levying taxes. The policy is that statutes are not to extend beyond their provisions by implication, beyond the clear import of the language used, nor to enlarge operations to include matters not specifically embraced. As stated in Gould v. Gould, 245 U.S. 151, 153 (1917), "In case of doubt, they are construed most strongly against the Government and in favor of the citizen." Furthermore, statutory provisions allowing contributions are not to be narrowly construed, for to do so would defeat the very purpose of such contribution. See Hight v. United States, 256 F.2d 795 (2d Cir. 1958); Estate of Whitehead, 3 T.C. 40 (1944).

As to what constitutes a "gift" under our federal tax system, a dichotomy often exists between the federal gift and income tax laws. See, *e.g.*, Klein, *An Enigma In the Federal Income Tax: The Meaning of the Word "Gift"*, 48 MINN. L. REV. 215 (1963).

5. See note 14 *infra* and accompanying text.

6. War Revenue Act of 1917, ch. 63, § 1201, 40 Stat. 330. Prior to this act, certain charitable organizations were tax-exempt, but contributions by individuals to these organizations were not deductible. See generally Revenue Act of 1905, ch. 6, § 28 (38), 36 Stat. 91 (1909), Revenue Act of 1913, ch. 16, § II(G), 38 Stat. 172.

In regard to the Revenue Act of 1917, Senator Hollis stated on September 7, 1917:

> Usually people contribute to charities and educational objects out of their surplus. After they have done everything else they want to do, after they have educated their children and traveled and spent their money on everything they

essary to raise this ceiling to 20 per cent of the donor's taxable income in 1952, a year which found charities fighting for survival within their limited income from endowment programs.[7] In 1954, the maximum allowable deduction was increased to 30 per cent;[8] but the additional 10 per cent deduction was limited to gifts made to churches, their conventions or associations,[9] hospitals or medical education organizations,[10] and any educational organization with a regular faculty, curriculum and enrolled student body in attendance at the site of the educational activities.[11]

In 1956, donors who contributed to medical research organizations engaged directly in the continuous active conduct of medical research in

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> really want, then, if they have something left over, they will contribute it to a college or to the Red Cross or for some scientific purpose. Now, when war comes we impose those heavy taxes on incomes that will be the first place where the wealthy men will be tempted to economize namely, in donations to charity. 55 CONG. REC. 6728 (1917).

7. The reason for the change in 1952, as given by the Senate Finance Committee was:

> Your committee is of the opinion that by increasing the 15% limit to 20%, much-needed relief will be given to colleges, hospitals, and other organizations who are becoming more and more dependent upon private contributors to enable them to balance their budgets and carry on their programs. The plight in which many of our educational institutions find themselves at the present time is due to the fact that their endowment income is inadequate to meet rising costs. It is only through supplemental gifts by the alumni or other persons interested in the cause of education that they are able to support their programs. Many of the smaller colleges whose alumni have not sufficient means to make contributions are able to continue their existence only through gifts or contributions received by one or two prominent families in their community. Your committee believes that it is to the best interest of the community to encourage private contributions to these institutions and it is believed that this amendment will provide some assistance in this respect. S. REP. No. 1584, 82d Cong., 2d Sess. (1952).

8. INT. REV. CODE OF 1954, § 170(b)(1)(A). All further reference to "section(s)" will be to the Internal Revenue Code of 1954 unless otherwise indicated.

9. Section 170(b)(1)(A)(i). The authority for deductions to a "religious order" was deleted in 1954, probably to avoid any inconsistency with the treatment of churches, associations and conventions under section 511, which imposes a tax on the unrelated business income of charitable organizations. Section 511(a)(2). See also Treas. Reg. § 1.170-2(b)(2) (1956).

In explaining its rationale for striking this provision, the Senate gives this report:

> Your committee has amended subdivision (i) by striking the words 'or a religious order.' Your committee understands that church to some denominations includes religious orders as well as other organizations which, as integral parts of the church, are engaged in carrying out the functions of the church whether as civil law corporations or otherwise. It is believed that the term 'church' should be all inclusive. To retain the phrase 'or a religious order' in this section . . . will tend to limit the term and may lead to confusion in the interpretation of other provisions of the bill relating to a church, a convention, or association of churches. S. REP. No. 1622, 83d Cong., 2d Sess. 207 (1954).

10. Sections 170(b)(1)(A)(iii), and 503(b)(5).

11. Sections 170(b)(1)(A)(ii), and 503(b)(2). See also Treas. Reg. § 1.170-2(b)(3) (1956). According to the Senate Finance Committee, this increase in allowable contributions was "designed to aid [those] institutions in obtaining the additional funds they need, in view of their rising costs and the relatively low rate of return they are receiving on endowment funds." S. REP. No. 1622, 83d Cong., 2d Sess. 29 (1954).

For an expanded discussion of the background and changes affected by the Internal Revenue Code of 1954, see Rea, *Changes in Internal Revenue Code of 1954 Affecting Charitable Organizations*, 27 ROCKY MT. L. REV. 270 (1955); Sugarman, *Charitable Giving Development in Tax Planning*, 39 TAXES 1027 (1961).

conjunction with a hospital were entitled to deduct this amount within the additional 10 per cent contribution limitation.[12] By 1962, Congress found it necessary to liberalize further the additional 10 percent category to include organizations or foundations operated exclusively for the purpose of receiving, investing and administering property, and making expenditures to and for the benefit of certain state-controlled universities.[13]

B. *More Get More in '64*

1. INDIVIDUALS

The 1954 Code as amended now permits an individual donor to deduct a maximum of 30 per cent of his adjusted gross income[14] for contributions made to virtually all types of qualified charitable donees. The newest class of donees qualifying for the 30 per cent deduction consists of charitable and cultural organizations which normally receive a substantial portion of their support from a governmental body (federal, state or local), from the general public, or from both.[15] Contributions made to such governmental bodies are deductible to the extent of 30 per cent if made exclusively for public purposes.[16] A donor may make "deductible contributions" to any or all of the enumerated "public charities until the aggregate of his contributions equals 10 per cent of his adjusted gross income; thereafter, contributions which do not exceed 20 per cent of his adjusted gross income are deductible whether made to public or private charities. In short, an individual donor is now allowed a 30 per cent deduction for substantially all gifts made to "public" charities, including governmental units and charities receiving substantial support from either the government or the general public.[17] Examples of the recent expanded objects of "public" charities include the American

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12. Sections 170(b)(1)(A)(iii), and 503 (b) (5) (subject to certain limitations).

13. Sections 170(b)(1)(A)(iv), and 503(b)(3). To qualify as a beneficiary under this provision an organization must be a college or university which is the instrumentality of, or is owned and operated by, a state or political subdivision thereof. For further development from 1961 to 1962, see Webster, *Current Developments in Federal Income Taxation*, 29 TENN. L. REV. 419 (1962).

14. Adjusted gross income in this respect is computed without regard to any net operating loss carryback otherwise available under § 172. Section 170(b)(1)(A). However, capital gains are included in adjusted gross income to the extent that they are reflected in the computation of income. Helvering v. Bliss, 293 U.S. 144 (1934).

If a husband and wife combine their income by use of the joint return, their contributions may be aggregated and the total measured against the adjusted gross income. Treas. Reg. 1.170-2(a)(1) (1956). See also Taft v. Helvering, 311 U.S. 195 (1940).

15. Section 170(b) as amended, Revenue Act of 1964, § 209(a). For further articles concerning the Revenue Act of 1964, see Calechman, *How to Make Lifetime Charitable Contributions At the Lowest After Tax Cost*, 20 J. TAXATION 364 (1964); Glander, *Tax Saving Through Gifts to Education*, 25 OHIO ST. L.J. 222 (1964).

16. Section 170(b) as amended, Revenue Act of 1964, § 209(2).

17. Any charitable contribution which exceeds the maximum deduction ceiling because of the percentage or time limitations cannot be deducted as a business expense. Section 162(b).

Red Cross, the United Fund, publicly or governmentally supported museums, libraries and art institutions, to name but a few.[18]

2. PARTNERS

Partnership deduction laws remain unchanged. A partnership as such is not entitled to any charitable contribution deduction, but the individual partners may treat their proportionate shares of any partnership contribution as their individual contributions.[19]

3. CORPORATIONS

Charitable contributions made by corporate donors are still limited to five per cent of the taxable income of the corporation, computed without regard to certain credits and deductions.[20]

4. ESTATES AND TRUSTS

In the case of contributions by estates and trusts, the entire amount donated to charity may be deducted, without limitation from either the gross estate[21] or, in the case of a trust, from the gross gift.[22] Charitable contributions made by common trust funds, however, are not deductible.[23]

5. THE 1964 ACT: HOW FAR THESE LINES?

The Revenue Act of 1964 in no way effects the percentage limitations for charitable deductions made by corporations, partnerships,

18. This amendment was applied to gifts made to "public" charities, and takes effect on contributions made in taxable years beginning after 1963. See 3 RIA FED. TAX COORDINATOR ¶ K-3007 (1964). It is important to note that the tax-exempt status of any charitable organization may be withdrawn at any time by the Internal Revenue Service. For a recent article discussing the withdrawal of the tax-exempt status of a pacifist organization, see *The Revenue Code and a Charity's Politics*, 73 YALE L.J. 661 (1964). Rev. Proc. 62-30, 1962-2 CUM. BULL. 512, defines the procedures under which an organization must comply in order to obtain tax exemption. A list of all qualified charitable organizations may be found in CUMULATIVE LIST, U.S. TREASURY DEPARTMENT, ORGANIZATIONS DESCRIBED IN SECTION 170(c) OF THE INTERNAL REVENUE CODE OF 1954 (1962).

19. Sections 702(a)(4), and 703(a)(2)(D).

20. The following special deductions are excluded in determining the taxable income of a corporation for purposes of charitable contribution deductions:
(1) any charitable contribution deduction;
(2) any deduction for partially tax-exempt interest;
(3) any net operating loss carryback to the taxable year, and
(4) the special deduction permitted for Western Hemisphere trade corporations. Section 170(b)(2)(D).

The corporation deduction provision was enacted under the Revenue Act of 1936, and though the 5% ceiling has remained unchanged, other benefits, such as the carryover provision, have inured to their benefit. See note 55 *infra*.

21. For estate tax purposes, the extent to which a charitable deduction can be taken is without limitation, so long as the transfer does not exceed the value of the transferred property required to be included in the gross estate. Section 2055(d).

22. Section 642(c). The amount donated by trusts must either be paid, permanently set aside, or used by the tax-exempt charity. Treas. Reg. 1.642(c)(2) (1956). See also Cohen, *Means and Methods of Making Charitable Contributions Under the Internal Revenue Code of 1954*, 3 ST. LOUIS U.L.J. 117 (1954).

23. Section 584(d)(3). See also Treas. Reg. 1.170-1(f)(3) (1956).

trusts or estates. It speaks solely to the individual donor. Its effect is to strip the 20 per cent bracket, which was formerly the catch-all section, of practically all charitable donees. Whereas in 1954 all charitable deductions were limited generally to 20 per cent unless otherwise excepted, as of 1964 all deductions are allowed to the extent of 30 per cent, subject to certain exceptions.

First of all, "private" charitable donees do not qualify for the 10 per cent increase in limitation afforded by the 1964 Act;[24] only "public" charities are so blessed. In this regard, a "private" charity may be defined as the antithesis of a "public" charity: it is any charitable organization which does not receive a substantial portion of its support from a governmental unit, or from indirect contributions from a representative number of persons within the community.[25] Donations made to such charities will continue to be treated as before, *i.e.*, deductible to the extent of 20 per cent of the donor's adjusted gross income.[26]

By its intentional exclusion of the private charity as a favored donee, Congress has manifested a general intent to police donations made to this class of donee, and more specifically, to curb current abuses that exist in private foundations.[27] According to Treasury Secretary Dillon, it has become a prevalent practice in private foundations for the controlling parties to withhold distribution of funds to charities for extended periods of time,[28] while at the same time the funds invested by the foundation have been used to benefit the principal contributors, in the form of loans, working capital or investment capital. Such practices currently are under surveillance and tighter restrictions on these charitable foundations and their trustees can be expected in the future.[29]

Secondly, the additional 10 per cent deduction allowance is available

24. This fact may be deduced from the intentional omission of the "private" charity by definition, from amended section 170(b).

25. *Ibid.*

26. Section 170(b)(1)(B).

27. See note 28 *infra.*

28. Dillon, *Retreats on Tax Reforms*, N.Y. Times, Oct. 17, 1963, p. 11, col. 8. For further information on this crackdown, see Peril, *Tax-Exempt Targets: The Patman Report and Private Charitable Foundations*, 42 TAXES 69 (1964).

Not all is gloom, however, for the private charitable foundation. Of some consolation is the fact that the Treasury will now rule on the tax exempt nature of the foundation much more quickly than before. Originally, a foundation was required to operate for one full year prior to a Treasury ruling on its exemption, as evidence of its *modus operandi.* As of 1963, this delay was eliminated—a determination letter or ruling will now be issued upon application if the organization can describe its *proposed* operation in sufficient detail to enable the Treasury to decide whether the exemption qualifies. It will not suffice, however, simply to restate the purposes of the organization, or to state that the proposed activities will be in furtherance of such purposes. Rev. Proc. 63-30, 1963-2 CUM. BULL. 769.

29. For a critical analysis of the private foundation under the 1964 Act, see Karst, *The Tax Exemption of Donor-Controlled Foundations*, 25 OHIO ST. L.J. 183 (1964); Peril, *Tax-Exempt Targets: The Patman Report and Private Charitable Foundations*, 42 TAXES 69 (1964).

to the taxpayer only when his gift is paid *directly to* a designated qualified charity.[30] This includes gifts made to publicly- and governmentally-supported organizations, as well as the charities formerly comprising the 30 per cent bracket. Thus, if a contribution is made "for the use of" the charitable organization rather than "directly to" the donee, the 30 per cent deduction will be denied. For example, a contribution to a public charity such as the United Fund generally will be deemed to have been made "for the use of" rather than "directly to" the charity. Of course, this treatment limits the charitable deduction with respect to gifts made to this type of charity to 20 per cent of the donor's adjusted gross income.

However, a donor desiring to make a contribution amounting to 30 per cent of his adjusted gross income to a public charity such as the United Fund, still may be entitled to a deduction to the extent of the full amount of the gift. To accomplish this within the bounds of the "directly to" restriction, the donor would be required to deliver two checks to the United Fund, one drawn in favor of the Fund in an amount equal to 20 per cent of his adjusted gross income, and a second check for the additional 10 per cent drawn to the order of a specific organization of a class designated in the 30 per cent category. When this procedure is followed, the Treasury permits the foundation to act as a conduit in delivering the check to the specific charitable organization.[31]

III. Unlimited Deductions

A. *The "8 of 10 Year" Provision*

The unlimited deduction provision creates a statutory exception to the percentage limitation otherwise imposed upon the donor.[32] On the authority of the 1954 Code, an individual taxpayer is allowed, at his own election,[33] an unlimited charitable contribution deduction if in the current tax year and in eight of the ten preceding years,[34] the taxpayer's

30. Treas. Reg. § 1.170-1(c)(2)(iv) (1962).

31. Rev. Rul. 55-1, 1955-1 Cum. Bull. 26. The second check drawn to the order of the specific organization must be delivered to the order of the specific organization, "directly and unconditionally" to the foundation. However, this device is only available where the fund-raising foundation provides for satisfaction of pledges and transfers in this manner.

32. See note 15 *supra* and accompanying text.

33. Section 170(b)(1)(C). To determine the effect of election on income taxes paid in prior years, as well as refunds and credits received, see discussion in 3 RIA Fed. Tax Coordinator ¶ K-3014 (1964).

34. The forerunner of this "8-of-10 year" provision was the Revenue Act of 1924, ch. 234, § 214(a)(10), 43 Stat. 271, which permitted a taxpayer an unlimited deduction if in the taxable year and in each of the ten preceding years, the total of the taxpayer's income taxes and charitable contributions exceeded 90% of his income before deduction.

The present unlimited deduction provision was introduced by Senator Couzens of Michigan, allegedly for the benefit of an order of nuns who had vowed to contribute all their income to the church. See Rudick & Gray, *Bounty Twice Blessed: Tax Consequences of Gifts of Property to or in Trust for Charity*, 16 Tax L. Rev. 273 (1961).

gifts to charity and his federal income taxes paid are in excess of 90 per cent of his taxable income.[35]

B. *"Private" Crackdown*

As a general rule under the Revenue Act of 1964, all gifts made to public charitable organizations are entitled to qualify for the unlimited deduction provision,[36] but contributions to private foundations qualify only in certain instances. In short, no longer are gifts to private charities "automatically" included in satisfying the 90 per cent test. Contributions made to private charities, which are not supported by governmental bodies or the general public, do not qualify for the unlimited deduction provision unless either of the following rigid requirements are met:[37]

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35. Section 170(b)(1)(C). Taxable income in this regard is computed without regard to deductions for charitable contributions, personal exemptions, and net operating loss *carrybacks* for each of those years. Thus, the 90% test must be met independently each year and a shortage in one year cannot be covered by an excess in later years. See generally Geller, *When and How to Take Full Advantage of the Net Operating Loss Carry-Over*, N.Y.U. 8TH TAX INST. ON FED. TAX 547 (1950). But Rev. Rul. 64-172, 1964 INT. REV. BULL. No. 23, at 11, provides that in determining taxable income for the year for purposes of unlimited deduction, a net operating loss deduction for a taxable year attributable to net operating loss *carryovers* is taken into account. Thus, taxable income is reduced by such carryovers.

To illustrate: assume taxpayer A's net operating figures are as follows:

1961 — $ 50,000 Net Operating Gain
1962 — (100,000) Net Operating Loss
1963 — 125,000 Net Operating Gain

In determining A's taxable income from 1961 to 1963 for purposes of the unlimited deduction provision, taxable income is computed without regard to net operating loss carrybacks. So in 1961, A would not be entitled to carryback $50,000 of net operating loss suffered in 1962 to offset the net operating gain recognized in 1961, for unlimited deduction purposes, even though $50,000 worth of net operating loss in 1962 could be carried back to 1961 for income tax purposes. Thus, A's taxable income in 1961 for this purpose, assuming no other income, would be $50,000, and in 1962, $100,000 loss.

In determining A's taxable income in 1963, however, the net operating loss may be carried forward to offset any gains in subsequent years. A would then be entitled to carry forward his loss in 1962 to offset gains realized in 1963. *Query:* since income tax consideration under section 172 requires that net operating loss carrybacks be carried back three years, prior to carrying forward offsetting income in five successive years, will the commissioner allow the full extent of the $100,000 loss in 1962 to be carried forward to offset $100,000 of gain in 1963; or inasmuch as only $50,000 would otherwise be available for carryforward, would the carryover be limited to this amount? It is submitted that the latter method would be the most consistent with the net operating loss provision of the Code; otherwise, the keeping of two separate schedules of net operating loss would be required.

36. The objects and requisites of the charitable corporations, trust, community chest, fund or foundation, must be of the type specified in § 170(c)(2):

(1) it must have been created or organized in or under the Law of the United States, any state, the District of Columbia, or any possession of the United States; §§ 170(c)(2)(A), 7701(a)(9).
(2) it must have been organized and operated exclusively for religious, scientific, charitable, literary, or educational purposes or for prevention of cruelty to children or animals;
(3) no part of the net earnings of such organization inures to the benefit of any private individual or shareholder; and
(4) no substantial part of the activities of the organization is carrying on propaganda, or otherwise attempting, to influence legislation.

37. Section 170(g), as amended, Revenue Act of 1964, § 209(g)(3). But any donor who has met the 90% test in any given year cannot now be disqualified as a result of a retroactive change in the law, enacted in a subsequent year, which tends to increase the taxable

(1) The private charitable organization must devote "substantially more than half" of its *assets* directly for the active conduct of its charitable activities. Moreover, "substantially all" of the *income* received must be expended directly for the active conduct of such activities;[38] or

(2) The private charitable organization must spend an amount equal to at least half of the donor's contribution in a particular manner.[39]

Even though a charitable organization may qualify for the unlimited deduction under one of the two methods just mentioned, the deduction still may be denied if the organization engages in certain "disqualifying transactions."[40] The commissioner has, in effect, approved the organization, subject to its continued good conduct; the good conduct is considered ended when it engages in "disqualifying transactions." These prohibited disqualifying acts occur when an organization engages in any one of the following transactions with the donor or his "tax family."[41]

(1) Lends any part of its income or corpus;
(2) Pays unreasonable compensation;
(3) Makes any of its services available on a preferential basis; or
(4) Purchases or sells more than a minimal amount of securities or other property.[42]

For this purpose, any of the above transactions made during the taxable year in which the contribution is received, the three preceding

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income in the prior year so that contributions amount to less than 90%. Kress v. United States, 159 F. Supp. 338 (Ct. Cl. 1958).

38. Section 170(b)(2)(B).

39. Section 170(g)(3). Within three years after the contribution has been received, or within a longer time as the Treasury may allow, upon good cause being shown by the organization, at least 50% of the donor's contribution must be expended for one or more of the following: "(1) The active conduct of the activities for which purpose the organization was formed, or (2) Assets which are directly devoted to such active conduct," or (3) Contributions to organizations which are described in section 170(b)(1)(A), as qualifying for the additional 10% deduction, or to organizations devoting more than half of their assets to charity.

For the period beginning with the taxable year in which such contributions are received and ending with the taxable year in which the above tests regarding the contributions are satisfied, the organization must spend *all* of its net income (determined without regard to capital gains and losses) for the purposes described in (1) through (3) above.

The donor, however, may elect to have the amounts an organization spends after the close of any of its taxable years and on or before the 15th day of the third month following the close of that year treated as expended during the taxable year. Section 170(g)(3).

40. Sections 503(c), and 681(b)(2).

41. Section 170(g)(4). Those members of the donors's "tax family" include:
(1) any member of his family [including only his brothers and sisters (whole blood and half blood), spouse, ancestors, and lineal descendents, § 276(c)(4)];
(2) any employee of the donor;
(3) any officer or employee of a corporation in which he owns (directly or indirectly) at least half of the value of the outstanding stock; or
(4) any partner or employee of a partnership in which he owns (directly or indirectly) at least half of the capital or profits interest.

42. *Ibid.*

taxable years, or the three following taxable years, will disqualify the charity.[43] However, the 1964 disqualification takes effect only with respect to contributions actually paid in 1964, and later years.[44] Thus, contributions made to all otherwise qualified private charities during 1963 and earlier years may be included in computing the eight-of-ten year provision.

An unlimited charitable contribution deduction taken by a taxpayer in a high income bracket or by one who makes excessive contributions is, in effect, a 90 per cent government-subsidized gift. It may even result in an increased after-tax income to the donor, because the unlimited deduction served to place him in a lower tax bracket.[45] The benefit from electing to use the unlimited deduction is not immediate, of course, but can be realized only in the tenth year. In other words, during those first eight years when the taxpayer is qualifying he is not allowed the benefit of the unlimited deduction privilege, either as a present deduction, or as a retroactive deduction upon qualifying.

IV. CARRYOVER PROVISION

The 1964 amended Code affords tax relief to the over-generous taxpayer whose contributions in any one year exceed the 30 per cent deduction allowance, and which otherwise would be forever barred as a deduction. The relief granted enables an individual who makes an annual contribution exceeding his 30 per cent ceiling to carry forward and deduct the excess during the next five years.[46]

A. *"Piecemeal" Confusion*

Prior to the Revenue Act of 1964, only corporations contributing more than the annual maximum ceiling were allowed any type of carryover for the excess—and this was limited to the two immediately succeeding years.[47] However, an individual who made a large gift in one year would forever forfeit the right to claim the excess as a tax deduction. This position with respect to individuals had a two-fold effect on large contributions made by them—either the donor was completely discouraged from making the gift, or he was encourgaed to give by the "piecemeal" or by some similarly motivated method. But even "piecemeal" giving was not without complexity and inconvenience, especially when the donor desired to give property in which he owned an undivided interest.

43. Those "disqualifying transactions" occurring prior to February 26, 1964 are excluded. Section 170(g)(4).

44. Section 170(g)(4).

45. Before deciding against electing to use the unlimited deduction provision, a "borderline" taxpayer should be advised of five hypothetical instances where the election is most advantageous. See Wellen, *The Unlimited Deduction for Charitable Contributions*, 7 Sw. L.J. 38 (1953).

46. Section 170(b)(5).

47. Section 170(b)(2).

Assume, for example, that taxpayer *A*'s maximum deduction of 30 per cent was equal to 25,000 dollars per year, and that he wished to give property worth 150,000 dollars to charity. To obtain the full tax benefit, *A* would have to make a gift of an undivided one-sixth (25,000/150,000) interest in the property each year. In addition, he would be required to surrender possession of the property to the charity for a period of time each year corresponding to the interest which the charity held in the property with the donor as tenant-in-common. Cumbersome as it has been, the validity of this form of transfer has been recognized by the Treasury when applied to real property,[48] patents,[49] standing timber,[50] and certain art objects.[51] It should be noted that the Treasury requires that the charity actually receive a vested interest in the property,[52] and a mere promise by the donor to do so in the future is insufficient.[53]

B. *The Five Year "Spread" Formation*

As of 1964, an individual taxpayer can effectively "spread" his large contribution over five taxable years without much of the former inconvenience.[54] A corporation can also carry over its excess contributions for five years instead of two, subject to the same restrictions placed on carryovers by the individual.[55]

It is now possible for the individual taxpayer to contribute the entire amount of the property worth 150,000 dollars in the first year, and to take his allowable deduction of 25,000 dollars in the year of contribution, as well as future deductions of 25,000 dollars in each of five succeeding years.[56] Thus, an individual can give property in a lump sum without forfeiting the charitable deduction for the excess. In addition, the donor no longer need postpone making his contributions until

48. Rev. Rul. 58-261, 1958-1 CUM. BULL. 143; Rev. Rul. 57-511, 1957-2 CUM. BULL. 158. For an analysis of possible gift tax ramifications of gift-sale transfers, see Williamson, *How to Use Gifts in Estate Planning*, 2 TAX COUNSELOR'S Q. 53 (1958).

49. Rev. Rul. 58-260, 1958-1 CUM. BULL. 126.

50. Stuart A. Rogers, 38 T.C. 785 (1962).

51. Rev. Rul. 57-293, 1957-2 CUM. BULL. 153. The deduction was permitted to the extent that a 25% interest in title was transferred to a museum by deed, and the museum had the right to possession for three months in the year. A similar gift made by deed, however, subject to the provision that the donor retain possession "until such time as he shall have transferred the entire interest in the object to the museum," was disallowed.

52. Rev. Rul. 57-511, 1957-2 CUM. BULL. 158.

53. Rev. Rul. 58-455, 1958-2 CUM. BULL. 100.

54. See note 46 *supra*. The carryover provision takes effect on contributions made after July 1, 1964.

55. Section 170(b)(2)(D). If the corporation is on the accrual basis the deduction will be permitted in the taxable year, if the board of directors authorizes payment, and payment is made within two and one-half months following the close of the taxable year. Section 170(a)(2). *Compare* Faucette Co., 17 T.C. 187 (1951), *with* Treas. Reg. 1.170-3(b) (1956) *and* Rev. Rul. 57-228, 1957-1 CUM. BULL. 506.

56. This, of course, assumes that the donor's maximum allowance remained constant and no other contributions were made during those years.

the end of the taxable year to avail himself of the maximum deduction. A year-end computation of adjusted gross income will, of course, be necessary, but its purpose will not be to determine how much shall be given at that time, but rather how much of the contribution *already made* may be deducted in the current year, and to set up a schedule for the unused carryover. For the generous donor who finds it necessary or expedient to make a large donation in any one taxable year, spreading the gift over five additional years may well result in the greatest incidence of tax savings in the highest tax bracket.

1. SOME RESTRICTIONS

In viewing the carryover provisions of the 1964 Revenue Act, it is essential to examine their built-in restrictions. Of prime importance is the fact that the five-year carryover provision applies only to excess charitable contributions made to donees in the 30 per cent "public" charity category; it is not applicable to any excess of donations made to the 20 per cent category of "private" donees.[57] Thus, an individual donor cannot circumvent the annual 20 per cent restriction on certain gifts merely by deducting the excess over the next five years. In other words, if the private donee contributions are not used in the year of contribution the excess is forever lost as a deduction. The donor is always entitled to the customary 20 per cent deduction for private donee contributions made each year, but in no case is the donor entitled to a yearly deduction in excess of 20 per cent for private charities.

To illustrate, assume that an individual taxpaper desired to give property worth 100,000 dollars to his private charitable foundation. If his adjusted gross income were 100,000 dollars, his allowable ceiling for deductions in 1964 would be 20,000 dollars. This hypothetical taxpayer would be faced with the dilemma which all donors faced prior to 1964. He could either: (1) contribute to a public charity of the 30 per cent type which qualifies for the five-year carryover; (2) give to the private charity "piecemeal" fashion; or (3) give the lump sum to charity and forfeit the excess 80,000 dollar donation as a deduction. In short, a donor who contributes by means of his private charitable foundation would not be benefited by the carryover provisions of the 1964 Act.

In addition, the carryover provision does not increase in any way the amount which may be deducted in any subsequent year. The carryover, therefore, is only available to the extent that no other contributions are made in five successive years following the year of contribution. Consequently, a lump sum donation of property actually given in one year may effectively limit the donor's desire to make any further donations for five years, since he will be reaping the tax benefits of his contribution for the succeeding five years after the taxable year of that

57. Section 170(b)(5)(A).

donation. But this concept of "relation-back" giving may be of little significance to the charities which solicit additional gifts in the ensuing years. Charitable organizations in fact often earmark anticipated gifts and actually incur expenses to that extent in advance of the time of actual receipt of the gift.

Quite properly, the carryover provisions do allow for the alleviation of charitable pressures on the donor during these five future "locked-in" tax years.[58] They permit the donor to make new gifts in each successive year, and to receive a future tax benefit in an amount up to his maximum allowance for such year. Although the tax benefit from the new gift necessarily would be postponed,—for as long as five years—the fact remains that a tax benefit would exist. Subsequent annual gifts would be treated in the same manner.

Moreover, a favorable tax result may ensue from this new carryover provision, in that such "postponed beneficial" giving may more effectively afford the taxpayer the opportunity to take advantage of the maximum annual allowable deduction. This is so because he is is no longer required to predict accurately his yearly adjusted gross income,[59] assuming that his income in future years will remain as projected, and assuming that the donor survives his future "deductible" years.

2. SOME PITFALLS

If the donor under-estimates his future income or certain financial windfalls occur within the next five years, the donor may reap a tax benefit with respect to his previous charitable contributions. The increased income will allow additional charitable deductions for contributions made in such subsequent years, to the extent that the increased income results in an increased adjusted gross income and thereby increases the maximum charitable deduction permitted. Another possible benefit is that the additional income may permit the donor to "write-off" at a faster rate more of the lump sum contribution made during an earlier year.

However, if the donor's income decreases substantially within five years after the initial contribution, the converse may be true. For example, assume that a taxpayer contributed property worth 120,000 dollars to a public charity in 1964. His deductible allowance of 20,000 dollars (30 per cent of his adjusted gross income in 1964) would be utilized in 1964—the year of contribution, and the excess $100,000 carried forward for successive years until 1969. If the taxpayer suffers financial reverses in 1965, a reduction in his deductible ceiling in 1965

58. No restriction is mentioned in the Revenue Act of 1964 which would prevent a donor from deducting all succeeding annual gifts five years later.

59. With the carryover provision, yearly estimating errors by the donor may be corrected in the long run over a period of five years.

would reduce his projected ceiling accordingly. Indeed, even if the donor's income returned to the projected norm during the years from 1966 to 1969 to permit the annual deduction, the 10,000 dollars which could not be deducted in 1965 would be forever wasted, unless income increases in subsequent years served to increase his maximum deduction to that extent.

If the donor dies prior to receiving his full charitable deduction, the expected tax benefits of the non-deducted portion are lost.[60] Thus, returning to the previous illustration, if the donor should die before the anticipated years of deduction, *i.e.*, some time prior to 1969, no income tax deduction could be taken for that portion of the 100,000 dollars which remained unused. Moreover, the excess cannot be deducted as a contribution on the decedent donor's estate tax return, because he has made a completed inter vivos transfer of the property, rather than a testamentary transfer.[61] Consequently, the effect of his death is in a tax "penalty" to the extent of the unused carryover.

It is submitted that such tax consequences are inconsistent with the legislative policy of encouraging charitable contributions. To ease this burden, the Congress could provide that any charitable carryover unconsumed at the donor's death may be deducted from the donor's estate for estate tax purposes. It is true that even while the donor is alive, the right to carryover the excess is but an inchoate right: it is merely a right of the donor to deduct a certain amount in future years *conditioned* upon the donor's income attaining the necessary levels during those future years. Thus, it may be argued that since it is impossible to predetermine the amount of the carryover deduction in successive years while the donor is alive, how would it be possible to value the carryover deduction for estate tax purposes? However, the right to extraordinary tax relief at the death of the donor is not without precedent. In the area of testamentary gifts to individuals, for example, section 1014(a) of the Internal Revenue Code of 1954 permits the beneficiaries to take the property with a "stepped-up" basis, *i.e.*, at the fair market value at the death of the decedent, rather than at decedent's own basis.[62] If such legislative grace is granted with respect to dispositions to private individuals, should not a comparable measure likewise be accorded to charitable dispositions?

Assuming that an estate tax deduction were permitted, the final issue would then concern the method of measuring the amount of deduction available to the decedent's estate. On its face the fairest method would seem to be one which would respect the donor's intent regarding

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60. The carryover provision is basically an income tax deduction, not an estate tax deduction. See generally § 170(g).

61. Section 2055(a).

62. For an article discussing the present legislative intent on this question, see Heckerling, *The Death of the "Stepped-Up" Basis at Death*, 37 SO. CAL. L. REV. 247 (1964).

his determination of his future income and deductions, had he lived. So if a decedent donor projected that he could deduct 20,000 dollars for each of five successive years, at his death, under this method a conclusive presumption should arise that his future income would have permitted a charitable deduction in the amount of his unused carryover. Legislative amendment to that effect would encourage gifts of substantial amounts to charity by elderly donors who would then be assured that their estates would not "suffer" because of their lifetime generosity. It is no defense to say that elderly donors might misuse this privilege by over-estimating their projected income in hopes that their estate would benefit by their rapid expiration, since persons die for reasons other than to effect a tax saving. Furthermore, the decedent could achieve the same tax result merely by making a testamentary disposition of the property in question.

3. SOME ALTERNATIVES

a. "Heir-Conditioned" Giving

Absent an amendment to the 1964 Revenue Act as proposed above, it would be most advisable for elderly donees to continue to make large donations of property "piecemeal," and avoid the use of the carryover. For example, if a donor made an inter vivos gift of a one-fifth undivided interest in real property, at his death the interest transferred would not be subject to estate tax, and only the value of the retained four-fifths interest which the donor held would be includible in his gross estate. If the donor made provisions for a testamentary disposition of the remainder of his property including the retained four-fifths interest, this would result in the greatest estate tax benefit, in as much as a testamentary contribution may be made without limitation.[63] Thus, the elderly donor can be assured that the full extent of his gift will be deductible—either from income as fractional interests transferred through inter vivos gifts or from the gross estate as a charitable testamentary contribution to charity. Furthermore, as an incidental benefit of giving the remainder as a testamentary contribution, the decedent-donor's *gross* estate is increased by the amount of the property interest retained at death, thereby increasing the maximum marital deduction. The potential increase in the *taxable* estate, however, is offset by a corresponding charitable contribution deduction to the estate, permitting a boost in the marital deduction through already "tax-free" property.[64]

The "piecemeal" method of giving to achieve advantageous tax benefits may also be preferred over the carryover method when the donor desires to give large gifts over a period of *more* than five years. To illustrate, assume that *A* owns Blackacre worth 200,000 dollars which he wishes to contribute to a public charity, *X*. *A's* adjusted gross income

63. See note 21 *supra*.
64. Section 2056(a).

in 1964 is 60,000 dollars, which would permit a maximum charitable deduction of 18,000 dollars (60,000 $\times$ 30 per cent public charity limitation) during 1964. *A* is 45 years of age, with an annual salary of 10,000 dollars and income of 50,000 dollars from property other than Blackacre. It is evident at the outset that in view of *A's* fixed income, his maximum charitable contribution deduction will not vary substantially from 18,000 dollars per year. At this rate, if *A* were to donate Blackacre to charity in a lump sum in 1964, a deduction of 18,000 dollars in 1964, and in each of the succeeding 5 years, would only total 108,000 dollars. In 1970, no further carryover would be permitted and the remaining 92,000 dollars would be lost. However, if the piece-meal method were used, *A* still could deduct 18,000 dollars in 1964 and a similar amount in each of the five successive years, as in the former method, but the greatest tax benefits would occur in subsequent years beyond the five year period—the contributions in subsequent years need not be successive, nor equivalent, for in years of economic reverses smaller fractional gifts may be made without jeopardizing the donor's deduction, the donor is not compelled to take the full deduction within five years after contribution, and completion of the gift may be delayed until the donor's death.[65]

Of course, the piecemeal method may not be as beneficial to the charity as when the donor gives the lump sum and carries over the excess, because when an undivided interest is given each year, the donor as co-tenant, has the right to the use of the property to the extent of his common ownership therein. However, by merely refraining from exercising these rights, a "willing" donor could allow the charity full control.[66] Or in the alternative, the donor could lease his undivided interest in the property to the charity pending its later contribution by the donor. The fact that in the original year of contribution the donor intended ultimately to donate the entire asset will not cause the entire gift to be attributed to the taxpayer in the initial taxable year.[67]

b. Promissory Notes: "Piecemeal" Family Member

The taxpayer may utilize promissory notes as an additional method of spreading out a gift of property. Under this method of making donations

65. For other advantages of piecemeal giving to charity, see Quiggle, *Tax Advantages Spur Charitable Gifts of Unusual Properties*, 13 J. TAXATION 96 (1960); *Piecemeal Gifts of Large Asset Can Cut Gift Tax*, 21 J. TAXATION 293 (1964).

66. No deduction is allowed, of course, for this retained right which is voluntarily surrendered for the charitable organization to use, provided the donor has utilized his maximum charitable contribution deduction by giving the other undivided interest in the property to the organization.

67. Boman v. Commissioner, 240 F.2d 767 (8th Cir. 1957); Albert T. Felix, 21 T.C. 794 (1954). *Contra*, Rev. Rul. 54-9, 1954-1 CUM. BULL. 20.

In determining what type of property to donate to charity, see Bixler, *To Give Is to Hold*, 100 TRUSTS & ESTATES 1102 (1961) (includes charts on the computation of maximum deductions available for each type of property, written by a certified public accountant); Stewart, *Gifts of Real and Personal Property Are Charitable Contributions*, 23 ALA. LAW. 173 (1962).

the taxpayer transfers property to charity in return for promissory notes given on the property so transferred. As each note matures, the taxpayer cancels the indebtedness, taking a corresponding contribution deduction for that amount. In this manner the taxpayer can spread out his gift of property for a period of time beyond the 1964 carryover period of five years. Inherent in this form of giving is the concept of contributing fractional interests each year, though the exact form may vary slightly in each case.

For example, in *Andrus v. Burnet*,[68] eight relatives wished to establish a memorial for their deceased mother. Their contribution was accomplished by conveying real property to a charitable organization, which in exchange gave notes to each of the grantors. Upon the cancellation of each of the notes, the donors took that amount as a charitable deduction. The court reversed the commissioner's findings and held that the gift was not completed at the time of the transfer of the property, and thus each cancellation of indebtedness to the charity created a deduction.[69] The court was impressed with the bilateral nature of the transaction, with land passing from one party and notes from the other. Though the notes were not secured by a mortgage, they were given by a solvent maker and the holders could have negotiated them, given them away or presented them for payment at maturity, as their desires or subsequent necessities required.

In *Nelson Story*,[70] the donors conveyed property to a charity for the erection of a memorial chapel for their son, who was killed in World War II. The notes received by the donors were secured by a mortgage. The court held that since the donors wished to supervise the construction of the chapel, the retention of the mortgage showed a general intent not to make a present conveyance of the entire property. The test used by the court was not whether the donors intended at the inception to collect the debt as it matured, but whether they intended to make a present total transfer, as against creating a future obligation, which from time to time could be forgiven.[71]

The one cautionary note directed to this form of contribution was illustrated in *Minnie E. Deal*.[72] In that case the taxpayer transferred land into a trust, naming her daughters trustees. They were given the discretion to pay her the income for life to meet her reasonable needs; at her death the remainder was to go to her daughters. On the same day that the trust was executed, the daughters gave notes to their mother. These notes were later cancelled and the amount taken as a gift tax ex-

68. 50 F.2d 332 (D.C. Cir. 1931).
69. *Id.* at 333.
70. 38 T.C. 936 (1962).
71. *Id.* at 942.
72. 29 T.C. 730 (1958).

clusion. The court, looking to the substance of the transaction to determine whether a bona fide debt was created, found that the overall intent was to make a present gift rather than a sale, and taxed the present transfer under the gift tax provisions.[73]

Though the *Deal* case dealt with a gift made to a private individual as opposed to a charity, the case indicates that the commissioner will, in either case, treat the gift as consummated in the year of transfer, unless the original transaction created a bona fide indebtedness. This fact was re-emphasized in the recent case of *Selsor R. Haygood*,[74] wherein a mother deeded real property to her sons subject to a vendor's lien. The lien bore no interest and the notes were payable in annual installments of 3,000 dollars. No payments were ever made by the sons, who were in fact financially unable to meet the payments. Instead, each year the mother cancelled the notes taking that amount as a gift to the sons. The court held that due to the enforceable nature of the notes, the entire value of the transaction was not a gift when the lien was created.[75]

Thus, if promissory notes are to be used in making charitable contributions, to be certain of deductions in future years, the notes should be secured by the property transferred to the charity. The mere donative intent of the transferor may not in every case prevent the commissioner from treating the entire transaction as a gift *ab initio*, and thus defeating the use of any carryover.[76]

C. *Check List: Use of Carryover vs. "Piecemeal" Giving*

In summary, the new carryover provision should not be permitted to create the false impression that lump sum gifts of property should be made in every instance. Before any decision is made in this regard, the following factors should be considered as a check-list:

(1) Are the contemplated charitable donees public or private? Only public charities defined under the amended 30 per cent category qualify for the carryover; private foundations and trusts are excluded.

(2) Is the charitable intent of the donor to make a present or a

73. Int. Rev. Code of 1939, § 1000(a), 53 Stat. 144 (now INT. REV. CODE OF 1954, § 2501(a)).

74. 42 T.C. No. 71 (Aug. 24, 1964).

75. *Ibid.*

76. See note 72 *supra* and accompanying text. It should be noted at this point that making charitable contributions by the use of fractional interests given either outright each year or through the cancellation of indebtedness, are not the only alternatives to the use of the carryover provision. A further suggestion, for example, is the use of a charitable trust. For a general discussion on the trust and other alternative modes of charitable giving, see, *e.g.*, Fraser, *Charitable Giving as an Element in Planning Lifetime and Testamentary Giving*, N.Y.U. 19TH INST. ON FED. TAX 751 (1961); Trautman, *Taxation of Gifts in Trust to Charities Reserving a Life Income Interest*, 14 VAND. L. REV. 597 (1961); Vestal, *Critical Evaluation of the Charitable Trust as a Giving Device*, WASH. U.L.Q. 195 (1957).

testamentary gift? Often a donor's intent is predicated upon the needs of a specific charity. If a testamentary disposition is contemplated, the estate tax provisions permit a charitable deduction without limitation. Only if the donor wishes to make an inter vivos gift does the carryover provision apply.

(3) What type of property will be given? Property subject to division may be given more easily in separate transfers than a lump sum of property in which the donor has an undivided interest.

(4) Is the property to be given tangible personal property? A gift of a future interest in this type of property is not deductible.[77]

(5) What is the value of the property to be given? As a general rule, the carryover provision may not be effectively used unless the value of the property contributed is susceptible of being deducted within five years following the year of contribution. In other words, if the total of the donor's projected charitable deductions for five years after the year of contribution is less than the amount of the contribution, the donor will waste a portion of the tax benefits of the gift, even though utilizing the carryover to the fullest. It would thus be advisable to give the property piecemeal.

(6) What are the foreseeable future needs of the donor, his family and his business? Is he in a financial position which enables him to give the entire property, or would a retained partial interest be preferred? Does the donor have other sufficient property to meet future emergencies?

(7) What is the age and physical condition of the donor? If his life expectancy or health is such that death may be imminent, charitable giving should be fractional each year, rather than in a large single gift. Testamentary dispositions can, of course, convey the remainder to charity.

(8) If the donor were to give a lump sum and die shortly thereafter, would local law invalidate the gift as against certain members of the donor's family?[78]

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77. See note 85 *infra* and accompanying text.

78. *E.g.*, FLA. STAT. § 731.19 (1963), provides that both the amounts which may be contributed to charitable organizations, as well as the times at which the donations may be made are subject to control by the statute, if made within a certain period prior to the death of the donor. In short, a devise or bequest made to a charity is voidable unless executed according to the statute at least six months prior to the death of the testator, or unless the testator's next prior will, executed more than six months before his death, made a charitable bequest or devise of the same amount to the same charitable organization and for the same purpose. See generally Taylor v. Payne, 154 Fla. 359, 17 So.2d 615 (1944); Joslin, *Florida's Charitable "Mortmain" Act*, 7 MIAMI L.Q. 488 (1953). For a discussion of other than specific Florida state law, see Drye, *Testamentary Gifts of Income to Charity*, 13 TAX L. REV. 49 (1957).

(9) What is the projected income of the donor during the next five years? What are his longer range income possibilities? Can he best utilize the tax benefits by making the gift now or later?

(10) Will social pressures necessitate other gifts in subsequent years notwithstanding a former bulk gift? If the donor does contemplate making large gifts in successive years, and is already in a high income tax bracket, he should consider using the unlimited deduction provision.[79]

(11) What is the fiscal condition of the general economy? In periods of rising inflation, a one-shot gift the first year will be worth less per dollar deduction taken in later years. The lump sum gift is only a hedge in times of depression.

(12) Is the taxpayer an individual or a corporation? Both corporations and individuals are now entitled to carryover certain excessive contributions for five years.[80]

(13) Are the deductions of the taxpayer large enough to warrant the filing of an itemized income tax return? An individual who elects the standard deduction is not entitled to any separate charitable contribution deduction.[81]

V. TANGIBLE PERSONAL PROPERTY

A. *To Give Is To Hold*[82]

Prior to the Revenue Act of 1964 a taxpayer who donated to charity a remainder interest in tangible personal property was entitled to deduct the value of the future interest as a charitable contribution in the year in which the donation was made.[83] The deduction was permitted even though the donor remained, for all practical purposes, the owner of the property, and continued to enjoy the use and benefits thereof for as long as he lived.

B. *No Strings Attached*

The 1964 Revenue Act provides that a donor who gives away certain property to charity while retaining an interest therein is not entitled to deduct any portion of the gift as a charitable contribution.[84] More specifically, a gift of a future interest in tangible personal property will be considered as completed for tax purposes only when all the in-

79. See note 36 *supra* and accompanying text.
80. See note 55 *supra*.
81. Section 63(b). See also Hulse, *How the Standard Deduction Affects Contributions*, 26 TAXES 784 (1948).
82. Heading taken from Bixler, *To Give Is to Hold*, 100 Trusts & Estates 1102 (1961).
83. Treas. Regs. §§ 1.170-1(d) and 1.170-2(d) (1956). The valuation of the remainder interests given to a charitable organization is determined according to the present actuarial tables appearing in the gift tax regulations. Treas. Reg. § 2512-5 (1961).
84. See note 85 *infra*.

tervening rights to the actual possession have expired, or such rights are held by persons other than the donor or his "tax family."[85]

No longer may a taxpayer take a charitable deduction for gifts of future interests such as by giving an art collection to a museum while retaining a life interest to the possession of the property. For any gift of tangible personal property made after July 1, 1964, wherein the donor retains any interest, he can only deduct the value of the gift to charity when the charity procures full control over the gift property, regardless of whether the taxpayer retains control for one year, ten years or for life.[86] Thus, if a donor makes a gift in which he reserves an interest for a specified term of years, he will be denied a present deduction, but he may deduct the fair market value of the entire property passing to the charity if he survives to the end of the period. Similarly, a retained life interest in the donor will preclude any lifetime deduction in connection with the property. In short, the commissioner will cause the donor's retained interest to effect a postponement of the deductible contribution until all his reserved rights have terminated.[87]

This provision of the 1964 Revenue Act is not without inherent exceptions:

(1) Gifts of future interests made prior to July 1, 1964, will continue to qualify for the current deduction of the present value of the remainder interest.[88] This is true even though the charity does not in fact receive the property until 1964 or later. In other words, only if a gift of this nature was made in the first half of 1964 or earlier is the donor not bound by the new act.

(2) This provision is not applicable when the retained rights in the gift of tangible personal property are held by others than the donor or his "tax family."[89] The donor, by transferring his retained beneficial interest in the gift property to a "non-tax-relative" is entitled to deduct as a charitable contribution the value of the remainder interest, as of the time the tranfer is made.[90] No charitable deduction is available, of course, for the value of the beneficial life interest transferred, if the transferee is a non-charitable entity. The gift of the remainder interest to the charity is treated as a transfer of a present interest for federal income tax purposes, notwithstanding the fact that the property may be completely depleted or depreciated at the death of the donor. Indeed, the value of a remainder interest of a non-depreciable asset such as a valuable art work, would provide the donor with the maximum deduc-

85. Section 170(f). See also S. REP. No. 805, 88th Cong., 2d Sess. 214 (1964).
86. Section 170(f).
87. H.R. REP. No. 749, 88th Cong., 2d Sess. A50 (1964).
88. Section 170(f). See also Rev. Rul. 58-455, 1958-2 CUM. BULL. 100.
89. Section 170(f).
90. Section 170(f).

tion for substantially the *entire* value at the time of transfer. Upon the gift of the present interest of the same property to a third party, not part of his "tax family," a secondary benefit would inure to the donor in the form of personal goodwill.[91]

It is conceded that the end result to the charity of receipt of such remainder interest is identical to the situation in which the taxpayer bequeaths the entire property to charity by will—since the charitable organization has no right to the use or possession of the property in either instance until the death of the donor. It is further agreed that the taxpayer could deduct the full amount of the charitable bequest as a contribution at death. But the right to accelerate the charitable deduction, and the donor's passion for recognition during his lifetime are often dominant factors responsible for the election to make gifts of future interests.

(3) Deductible gifts may still be made of future interests in real property.[92] Accessions and fixtures which are intended to be severable from the realty, however, retain their classification as tangible personal property.[93] The amount which may be deducted for a gift of such a future or remainder interest in real property is the present value of the remainder interest.[94] To determine what constitutes a "future interest," the same rules apply which govern future interests for gift tax exclusion purposes, *i.e.*, future interests are all interests which are to commence in use, possession or enjoyment at some future time, notwithstanding a contrary classification of the interest under state law.[95] This test is one of substance and not merely of form. A contribution which in form purports to be a present interest, therefore, will be deemed a future interest, if the donor presently retains the beneficial enjoyment of the property by a "loan" of the property from the charitable organization.[96]

(4) A donor is still permitted to make a deductible contribution of a future interest of intangible personal property such as stock.[97] But any dividends or other income received during the time the property is retained by the donor will be fully taxable to him.[98]

(5) A donor may make an immediate transfer to charity of a partial present interest in the property without being subjected to the

91. The primary benefit of transferring the retained rights in the property to a "non-tax-family member" lies in the fact that the transferor is entitled to the charitable contribution deduction for the remainder interest at the time the transfer is made to the non-charitable donee. The incidental benefit is purely personal satisfaction to the donor.

92. Section 170(f).

93. H.R. REP. No. 749, 88th Cong., 2d Sess. A51 (1964).

94. Treas. Regs. §§ 1.170-1(d) and 1.170-2(d) (1956).

95. Treas. Reg. 25.2503-3 (1958).

96. H.R. REP. No. 749, 88th Cong., 2d Sess. A51 (1964).

97. Section 170(f).

98. Treas. Regs. §§ 1.61-7(a) and 1.61-9(c) (1957).

rule requiring postponement of the deduction. Property which is capable of easy division is most ideally suited for this method of giving. The "piecemeal" method of giving tangible personal property, therefore, stands unchanged. A transfer *in praesenti* of a partial interest in tangible personal property is still acceptable, and it will be deductible as of the time of tranfer. A transfer of a remainder interest in tangible personal property which will vest with the charity in the future is deductible only at the time the donor relinquishes all his rights to the use and possession of the property.[99]

As a general rule, therefore, under the new postponement of deduction provision, a taxpayer will receive no greater federal tax advantage by giving a remainder interest in tangible personal property to charity than by making a testamentary contribution of the same property by will, unless the donor otherwise qualifies under one of the above-listed exceptions. In either case, at the death of the donor, the fair market value of the entire property, though includible in the decedent's gross estate, is offset by an equivalent charitable contribution deduction.

VI. CONCLUSION

Private charitable organizations, and more specifically, private foundations, have precipitated the major changes in charitable contributions under the Revenue Act of 1964. In demonstrating a general intent to restrict contributions made to private charities, Congress has manifested its apparent disapproval of sham gifts to charity, such as gifts which either are never received by a bona fide charitable organization, or are diverted en route to the charity by use of the conduit foundation, for noncharitable purposes and for indeterminate periods of time.

The private charity is excluded completely from the application of the 30 per cent ceiling and the five-year carryover provision, which are the two most significant provisions produced by the 1964 Act. Under no circumstances can gifts to private organizations qualify for these purposes. Even a qualification under the stringent standards imposed upon private charities by the new unlimited deduction provision will not permit a carryover or 30 per cent deduction.

What, then, is the future for the private charity? The Revenue Act of 1964 did not sound the death knell for either the private charity or private foundation; rather it adopted a laissez faire policy, at least for the moment. The donor-controlled foundations will continue to be treated for federal tax purposes as if the 1964 Act were never passed. The only exception to this is a "show me" attitude taken by the commissioner in the area of unlimited deductions. That is, gifts to private charitable foundations may still qualify for the "8-of-10 year" unlimited

99. See note 85 *supra*.

deduction purposes, provided the donor rebuts the presumption of sham to the satisfaction of a skeptical commissioner.[100] In short, Congress has increased the allowances of its faithful children, but the privileges of its black sheep remain unchanged.

The present status quo position of the private charitable organization is by no means a green light, for statutory regulations with respect to these organizations presently are being considered by Congress. Thus, it behooves those in donor-controlled foundations to tread softly, being especially aware of any possible "questionable" practices. Continued misuse of the private "conduit" may result in disqualification of the specific foundation, or even permanent extinction of the entire class.

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100. This presumption is rebutted only upon the private charitable organization's meeting of certain requirements, as set forth in note 37 *supra* and accompanying text.