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# Obtaining the Maximum Benefit for the Charity and the Estate in Making Charitable Gifts

Edward N. Polisher

# OBTAINING THE MAXIMUM BENEFIT FOR THE CHARITY AND THE ESTATE IN MAKING CHARITABLE GIFTS

by

Edward N. Polisher*

## I. INTRODUCTION

### (a) *Favorable Treatment of Charitable Gifts*

Under the complex Federal revenue laws in force today, the problem of an individual who desires to make a gift to charity is not a simple one, if he wishes to avail himself of the maximum tax advantages possible. Questions as to the type of property to be given, the form of the gift, the nature of the interest to be given, etc., are all vital. These deserve careful consideration from the donor if the charity is to receive the greatest benefit from the gift, and, at the same time, the personal objectives of the donor are to be attained.

The law generally favors charitable organizations. Further, the Federal revenue laws, in both language and construction, operate to advance charitable purposes. In *Helvering v. Bliss,* 293 U.S. 144 (1934), the Supreme Court stated that the liberal treatment accorded gifts to charity was intended to encourage the making of such gifts, within the limitations set by law. The practical consequence of this encouragement is that the Federal government is in fact subsidizing the organizations which receive such gifts. For it is clear that many of the contributions might never be made, or at least would not be in the amounts given, were it not for the provisions of the Internal Revenue Code granting income, estate and gift tax deductions for such contributions. In essence, the government yields up tax revenues on amounts given to charity.

### (b) *Definitions of Charitable Organizations*

The term "charity" has many definitions, depending upon its use in a specific instance and upon the one employing the term. In tax usage there is little confusion, since the Code in several places defines such organizations. Section 23 (o) (2) of the Code defines charitable organizations, contributions to which entitle the taxpayer to a deduction from income taxes. Generally such bodies are organizations "operated exclusively for religious, charitable, scientific, literary or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation."

*Member of the Philadelphia Bar, author of "Estate Planning and Estate Tax Saving", new 1948 edition, and lecturer on Taxation at Dickinson Law School.

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A similar definition is found in Section 812 (d) of the Code relating to deductions from the gross estate of a decedent for amounts bequeathed to charitable organizations. The definition of organizations to which resident-taxpayers may make contributions and be entitled to a deduction for gift tax purposes is found in Code Section 1004 (a) (2) (B). Section 1004 (b) (2) and (3) of the Code defines such organizations so far as non-resident taxpayers are concerned. The descriptions are substantially identical with the others cited above. It should be noted, however, that the Revenue Revision Act of 1948, H.R. 6712, passed by the House of Representatives but which was not acted upon by the Senate prior to adjournment in the summer of this year, proposed minor changes in the definitions so as to make all of the above definitions of charitable organizations identical.

Although not specifically related to the question of deduction from income, estate or gift taxes, the definition of exempt charitable organizations found in Section 101 of the Code should be of interest to those who contemplate a "controlled" charitable organization such as a family foundation. Almost identical language is employed in this section also.

Normally the problem of the status of the organization is not a concern of the donor, but he should be aware of the limitations of the gifts. For example, a taxpayer who makes a sizeable contribution to a political party might find, to his later dismay, that such recipient does not qualify as a charitable organization and, consequently, the deduction will be denied. It is, therefore, important that where there is any doubt whatsoever, the taxpayer reassure himself of the nature of the donee organization so that he may know whether contributions to it will receive favored tax treatment.

## *II. GENERAL IMPLICATIONS*

### (*a*) *Lifetime Transfers*

For income tax purposes, contributions to a qualifying charitable organization are deductible in full in the taxable year when paid, to an amount not in excess of 15 per centum of the taxpayer's adjusted gross income. I.R.C. Section 23 (o). It should be borne in mind that even though a taxpayer may be on an accrual basis, the deduction is allowed only for amounts actually paid within the year, and not for amounts pledged in one year and paid in a subsequent period. Treasury Regulations 111 Sec. 29.23 (o)-1.

Property or cash must actually be transferred or paid over to the charity. In a recent ruling of the Bureau of Internal Revenue, it was held that granting a charity the rent-free use of property was not a "payment" of a contribution so as to support a deduction for the rental value as a charitable contribution. I. T. 3918, I.R.B. 1948-17-12903. In line with this thought, it may be of interest to note a recent decision which holds that permitting a charitable organization to use property rent-free does not convert the use of the property to a business purpose. *Emmet*, 11 T.C., No. 13 (1948).

Estates and trusts are permitted a deduction without limitation as to amount, for any part of the gross income which, pursuant to the terms of a will or deed of trust, is, during the taxable year, paid to or permanently set aside for purposes specified in Section 23 (o). See I.R.C. Section 162 (a). This unlimited deduction feature is one that offers planners opportunities to employ trusts to obtain a greater benefit for charities without any additional burden upon the taxpayers. For a full discussion of charitable trusts, see Kennedy, *Federal Income Taxation of Trusts and Estates* (1948), Chapter 3.

One such plan is the use of a "short-term" trust in which property is transferred to a trustee to be held for a relatively short term, during which time the entire net income is paid over to charity, and at the expiration of the term, the corpus reverts to the grantor. This device is especially helpful to a taxpayer who is currently contributing more than 15 per cent of his income to charity and who finds that because of the organizations' great needs, he cannot reduce his gifts in the near future. By transferring income-producing property to such a trust he assures the use of the income to the charity. At the same time he has reduced his income and his contributions so that he no longer exceeds the allowable 15 per cent. The donor is not entitled to a deduction from income tax for the amount transferred to the trust since that will ultimately revert to him. However, since he gives the maximum permitted to be deducted, this is an immaterial factor. An example will illustrate the tax advantages:

> Assume X, a single man with no dependents, has income before deduction of charitable gifts of $100,000 and that he annually gives to charity the sum of $25,000. He creates a short-term charitable trust and transfers to the trustee property producing an annual income of $12,000.
> *Before creating the trust*:

| | | |
|---|---|---|
| Income | $100,000 | |
| Gifts (15% limit) | 15,000 | |
| Subject to tax | | $ 85,000 |
| Taxes on $85,000 | 47,870 | |
| Gifts not deductible | 10,000 | 57,870 |
| Remaining after gifts and taxes | | $ 27,130 |

*After creating the trust*:

| | | |
|---|---|---|
| Income | $ 88,000 | |
| Gifts ($25,000 less trust income of $12,000) | 13,000 | |
| Subject to tax | | $ 75,000 |
| Taxes on $75,000 | | 40,610 |
| Remaining after gifts and taxes | | $ 34,390 |

In addition to the financial advantage demonstrated above, there may be other features of the short-term trust that make it attractive to a donor. Should the donor desire to make a sizeable lump sum gift, he will probably find that such a gift would greatly exceed his allowable deduction for any one year. However, the trust is not required to pay over the income annually so long as such income is permanently set aside for the prescribed purposes. It may, therefore accumulate the income of several periods in order to make the large single contribution.

Still another feature is the fact that a trust need not make its contributions to organizations, but can aid individuals if the purpose is consistent with those described in Section 23 (0) of the Code. If a donor is desirous of supporting an individual's scientific research he would not be permitted a deduction for a contribution thereto unless he worked through the medium of an organization qualifying under Section 23 (o). If, however, a trust were to offer the financial assistance, the trust would be permitted a deduction for such gifts since Section 162 (a) of the Code permits deduction if income "is to be used exclusively for religious, charitable, scientific . . . purposes". *J. B. Whitehead Estate,* 3 T.C. 40 (1944), aff'd 147 F. (2d) 977 (CAA-5, 1945). Further, a fiduciary, under the above quoted portion of Section 162 (a), may deduct gross income which is to be used exclusively for religious, charitable, etc. purposes, even though payment is made to institutions outside of the United States and therefore would not be deductible by individuals under Section 23 (o). *Estate of Emily St. A. Tait,* 11 T.C. No. 89 (1948).

In creating a short-term trust the Treasury's requirements with respect to the *Clifford* rule must be kept in mind. See *Helvering v. Clifford,* 309 U.S. 331 (1940). If the period is less than ten years, the income will be taxable to the grantor even though the income is in fact paid over to charities. Treasury Regulations 111, Sec. 29.22 (a)-21 (c).

The deduction permitted the trust is for amounts of "gross income" paid over for the charitable purposes. This has been interpreted to mean statutory gross income. Thus, where the trust had large long-term capital gains, only 50 per cent of which were included in gross income, and the trustee sought to deduct 45 per cent of the total income, as being set aside for charity pursuant to the trust agreement, the court limited the deduction to 45 per cent of the gross income as determined for tax purposes. *Commissioner v. Central Hanover Bank and Trust Co.,* 163 F. (2d) 208 (CAA-2, 1947), cert. den. 332 U.S. 830 (1947).

The Internal Revenue Code specifically permits the deduction of charitable gifts from the total gifts made during a taxable year in order to determine the "net gifts" subject to gift tax. I.R.C. Section 1004 (a) (2).

*(b) Testamentary Transfers*

The Internal Revenue Code provides that bequests in a will to a qualifying charity will be deductible from the gross estate of a decedent in determining the value of the net estate subject to tax. I.R.C. Section 812 (d). There is also a provision authorizing deduction from the gross estate of all amounts paid to such charity after the death of a testator, if such payments were on account of pledges made by the decedent during his lifetime and remained unpaid at the time of his death. It is interesting that this provision is not found in the section permitting deduction of charitable bequests, but rather in the section authorizing deduction from the gross estate of debts of the decedent. I.R.C., Section 812 (b). In both the estate and gift tax provisions of the Code, there is no limitation upon the amount that may be deducted for charitable bequests or gifts. Mention should also be made of the tax concept added by the Revenue Act of 1948, the "adjusted gross estate". See I.R.C. Section 812 (e) (2) (A). In computing the adjusted gross estate, there is to be subtracted from the gross estate certain expenses and debts of the estate allowed by Section 812 (b). Payments of pledges to charity made by the decedent during his lifetime are thus deductible in arriving at the adjusted gross estate, though charitable bequests in the will would not be.

(*c*) *Foundations and Controlled Charities*

A discussion of the general points to be kept in mind in considering charitable gifts would be incomplete without reference to foundations and controlled charities. These are generally organized by one or more individuals for purposes set forth in Section 101 (6) of the Code. The organizations are exempt from income tax and contributions to them are deductible by the donors. Usually, the organizers, their nominees or representatives, control the organization on all matters, including the investment and distribution of funds. It is of interest to note that the Bureau of Internal Revenue will not rule on the question of any organization's exempt status until there has been one year's operations to be examined. It is possible to obtain a preliminary ruling that if the organization adheres to the limitations of the creating instrument, it will be exempt when results of the operations are considered.

Much has already been written on these types of organizations and repetition would serve no useful purpose. The outstanding characteristic that must be kept in mind is the capacity of the donor who creates such an organization to continue to direct the investment and also the spending of the funds. Thus, though ownership of the property given to it may pass from the donor, control continues. As a rule, the control provision is a perpetuating one, so that upon a donor's death or retirement, the individuals succeeding to the control are the nominees of the original donor. The desirability of control without ownership is attested to by an examination of the wills of Henry Ford and Edsel Ford. The bulk of their estates consisted of stock in the Ford Motor Company and most of the shares owned by them were bequeathed to the Ford Foundation, a charitable organization. Surviving members of the family control the Foundation, and consequently, none of the shares passed beyond family domination.

In the case of large closely held business interests, the use of a controlled charity may permit retention of family control upon death of a major stockholder.

For example: In the Ford estates, bequest of the entire estates to private individuals would have resulted in estate taxes aggregating millions of dollars. Such taxes could perhaps only have been paid out of the proceeds of the sale of some of the shares of Ford Motor Company stock. The control of the enterprise might have been jeopardized. However, by leaving the bulk of the estate to an exempt organization, the value of such bequest was deducted from the gross estate in arriving at the net estate subject to taxation. Accordingly, a much lower tax was due, and there were, apparently, assets other than the stock of the Ford Motor Company available to pay such smaller amount of taxes. Thus, a judicious use of the controlled charity will permit continued control and will eliminate the necessity of liquidation of all or a portion of the business interests. For a more complete discussion of this subject see Polisher, *Estate Planning and Estate Tax Saving* (1948), Chapter XXIV.

Another advantage of a controlled charity should be mentioned here since it relates to the subsequent discussion. A donor may, if he wishes, make maximum contributions every year and so obtain a maximum deduction on his income tax returns. However, it is not obligatory upon the foundation to make annual contributions. Therefore, over a period of years, the gifts may be accumulated in order that one lump sum may be given in one subsequent year. Thus, a donor might obtain the greatest possible income tax benefit from his contributions, yet can retain control, through the foundation or other type of organization, so that gifts to specific charities may be made in such time and in such amounts as will result in the greatest possible benefits to such charities. Without an intervening controlled charity, contributions must go to the active charity and accumulation is impossible, if maximum contributions are made annually.

In recent years exempt organizations have, to an increasingly greater extent, entered into competitive business activities. To date there have been no legislative or judicial changes in the rule that permits continued exemption from taxation of its income so long as the organization's funds have been used for the prescribed purposes, regardless of the sources of such funds. *Trinidad v. Sagrada Orden de Predicadores,* 263 U.S. 578 (1924). However, recent legislative rumblings have been heard on this subject, and although no action has as yet been taken, consideration should be given to possible restrictions upon this tax-free conduct of competitive business activities by charitable organizations.

## *III. Form of Gift or Bequest*

### (*a*) *Outright Gift*

A traditional pedagogical approach to property law likens title to a bundle of sticks. Applying that rationale to the present discussion, the question that must be considered is, "How many sticks should be given to the charity?" It frequently occurs that the best interests of the donor and the charity can be served by giving less than a complete title.

If an outright gift of the entire property is made, the full value of the property is deductible for income, estate or gift tax purposes. I.R.C. Section 23 (o), 812 (d) and 1004 (a) (2). When such a contribution is made, the complete title passes at the time of the gift and the charitable organization immediately gets the benefit of the property transferred.

(*b*) *Charitable Remainder after Interest for Life to an Individual*

There may be situations, however, in which personal desires of the donor argue against an outright gift of the property to the charity. If the donor desires the property to provide an income for individuals for a stated period or for their lives, yet wishes the charity to ultimately receive the property, he must consider other types of disposition. A simple solution to this problem would be the transfer of the property giving a life estate or an estate for years to the named individuals, and upon the termination of such prior estate, a remainder interest to the charity. This may be done through the use of a trust or by a direct conveyance, the mechanics of the transfer being relatively unimportant.

If this suggestion were adopted, the charity, though receiving nothing immediately, knows that ultimately it will own the property, and therefore may plan accordingly. At the same time, the individual beneficiaries, though they do not receive the property in such manner that they could consume it, are, nevertheless, assured of the income from the property for the stipulated period.

In such case, the donor is entitled to a deduction for income, estate or gift tax purposes for the value of the remainder interest that was given to charity. *Ithaca Trust Company v. U.S.*, 279 U.S. 151 (1929). *See also* Treasury Regulations 105, Sec. 81.44. The value of such interest is computed by reference to tables set forth in Treasury Regulations applicable to gift and estate taxes. *See* Treasury Regulations 105, Sec. 81.10 (i). The tables are based upon assumed interest rates and life expectancies and the valuations determined by using the tables will not be disturbed even though the life tenant survives the date of creation of the trust by only a short period. *Bankers Trust Company v. Higgins*, 158 F. (2d) 957 (CAA-2, 1947).

This basic plan may be subject to a number of variations, and the possibilities of adapting it to a particular circumstance should never be overlooked. For example: A donor may wish to give the entire title to property to charity, subject, however, to an annuity charge thereon in favor of a named individual. If this is done, the value of the property, less the estimated value of the annuity charge (determined by reference to standard assumptions as to interest rates and life expectancy) will be deductible, since the deduction is for the value of the interest given to charity. This method may be employed where the donor wishes to assure an adequate income to the individual annuitant, but, at the same time, desires that the charity have the immediate full use of the property.

Still another advantage lies in the limitation of payments to the individual annuitant. Thus, by providing for the annuity, the donor has freed any of the property's excess income from any claims of the annuitant and such excess income may be used by the charity. Conversely, he has guaranteed a regular income to the annuitant payable by the charity even though the property may not earn the amount of the annuity.

The transfer of property to charity, subject to an annuity in favor of a named individual, will not adversely affect the charity's right to exemption under Section 101 (6) of the Code. Recently the Tax Court held this to be the rule even though the charitable organization was created by the instrument which also provided for the annuity. The basic inquiry in this matter appears to be whether the organization is, in fact, operated for the prescribed charitable purposes, or whether it is merely a subterfuge for private benefit. If the latter, exemption will be denied, as will the deduction for contributions thereto; but if the annuity is not provided as a cloak for perverting the prescribed charitable purpose, no untoward tax consequences will develop merely from the provision for the annuity. *Edward Orton, Jr. Ceramic Foundation,* 9 T.C. 533 (1947), appeal to CCA 6th pending.

(*c*) *Invasion of Corpus for Life Tenant's Benefit*

In providing for a charitable remainder in property the donor may be confronted with the question, "What if the income is inadequate for the life tenant?" There is, of course, a method of meeting this problem. It is by authorizing the invasion of the corpus of the trust, or consumption of the principal, if the circumstances require it. However, there are tax consequences which flow from such a provision.

As a general rule, if, in the light of all circumstances, the likelihood of invasion is slight, and in all probability the corpus will pass intact to the charity-remainderman, the deduction for the full amount of the corpus will be allowed. *Ithaca Trust Company* v. *U. S.,* 279 U. S. 151 (1929). The Treasury's official position on this situation is that the amount which will ultimately pass to charity must be clearly ascertainable at the time of the transfer, and the possibility of diversion from the charity must be "so remote as to be negligible". Treasury Regulations 105, Sec. 81.46. If, for example, corpus may be invaded at the discretion of the life tenant, no deduction will be allowed for a charitable gift or bequest, since the life tenant may consume the principal without restraint. On the other hand, if there is set forth a well-defined standard for the consumption of principal, and if consideration of all circumstances lead to the conclusion that it is probable that the entire remainder will pass to charity, the deduction will be granted. Each case must be separately considered and determined since factors such as the age, health, living habits, personal wealth and other income of the life beneficiary are vital in reaching a conclusion on the likelihood of invasion of the corpus. See Polisher, *Estate Planning and Estate Tax Saving,* (1948), pages 277-279.

(*d*) *Remainder to Individual after Charitable Interest for Stated Term*

If a donor's concern is for the income of an individual after the passage of a stated period of time or after his death or the death of another individual, he may find it possible to benefit a charity and still make provision for the beneficiary. This can be accomplished by transferring property to charity for a term of years or for the life of a named person and providing for a remainder over to an individual beneficiary.

If this procedure is adopted, the value of the charitable interest, computed by reference to tables set forth in the Gift and Estate Tax Regulations, will be deductible for income, gift, or estate tax purposes. *M. M. Jackson, Executor* (Estate *of M. V. Eagan*), 18 B.T.A. 875 (1930) (Acq. IX-2 C.B. 30). *See* Regulations 105, Sec. 81.10 (i) for valuation method.

By employing this device, the donor has assured the charity the use or benefit of the property for the stated period. Thus the charity may plan to use the property during such period and will receive benefits accordingly. On the other hand, the individual beneficiary who will ultimately receive the property knows that upon the occurrence of a particular event—lapse of the stated period of time or death of a designated individual—he will then receive the property, even though he presently enjoys nothing from the transfer.

This plan is most appropriate for a donor who feels that so long as he lives the beneficiary will never want, but wishes to provide for him in the event of his death. At the same time, he desires to make a present gift to a charitable organization in which he is interested. He can serve both ends, and if the property transferred is income-producing, he shall have also reduced his taxable income by having made the transfer.

## IV. CHOICE OF PROPERTY

An important consideration of a taxpayer contemplating charitable gifts or bequests is "What property should be given to charity?" If a donor owns but one type of property there is no problem. But normally he will own several different kinds of property and, tax-wise, the choice of what is given is a material question.

### (a) *Property which has Enhanced in Value*

It is generally advantageous to give property that has enhanced in value and whose current fair market value exceeds the taxpayer's basis for the property. In making a gift of such property, the taxpayer will be entitled to a deduction for the value of the property at the time of the gift. Regulations 111, Sec. 29.23 (o)-1. However, the donor need not report any gain as being realized on the transfer since the property was not sold or exchanged and thus no income was realized within the meaning of the Code. The tax benefits flowing from a gift of such property are demonstrated by the following illustrations:

Assume a donor is making a charitable gift of $5,000.00 He owns stocks which cost him $1,000.00, but which are worth $5,000.00:

1. If the stocks are sold and then a gift of $5,000.00 in cash is made, the taxpayer will have realized a gain in the amount of $4,000.00. In or-

der to make the gift he must pay out of his other funds, the tax upon the gain realized.

2. If the stocks were given directly to charity, no additional funds would be required. There would be no gain realized under the Code and therefore no tax to be paid.

Thus, in both cases the donor has parted with the property and has become entitled to a deduction for a charitable contribution of $5,000.00. However, in the former instance, his failure to give the securities in kind will have cost him the tax upon the enhancement in value.

It follows that by giving property that has increased in value over the donor's tax basis, the taxpayer is in essence making a tax-free disposition of the property at a gain.

Strange as it may appear, the Code does operate to permit this "tax-free" sale at a gain, in the circumstances outlined above. In 1938 there was a legislative proposal to limit the deduction to the basis of the property contributed. This bill passed the House but not the Senate. So ended the only legislative attempt to change the situation. However, it must be borne in mind that the 1938 proposal was only concerned with the amount of deduction that was permitted, and not with the determination of income. In a recent ruling of the Income Tax division of the Bureau of Internal Revenue, it was held that a farmer must include in his gross income the fair market value of crops donated to charity and for which he claimed a deduction as a charitable contribution under Section 23 (o) of the Code. I.T. 3910, I.R.B. 1948-13-12826. The implications of this ruling may be far reaching and, though it is too early to determine how far it may be extended, it should be kept in mind when gifts of property that have enhanced in value are contemplated.

A further word of caution should be mentioned in connection with this suggestion. If a taxpayer has made a pledge to a charity for a stated amount, a transfer of property which has enhanced in value in satisfaction of the pledge, will result in taxable gain for the excess of the pledge over the basis of the property. *Estate of John T. Harrington,* 2 T.C.M. 540 (1943).

*(b) Property Which has Declined in Value*

Just as it is generally to the advantage of the taxpayer to give property which has increased in value, so is it to his disadvantage to give to charity property which has declined in value below his basis. Since the deduction is for the fair market value of the gift, a donation of such property would result in a deduction only for the value thereof. On the other hand, if the property were sold, and then the proceeds of the sale were given to the charity, the taxpayer would then have (1) a deduction for the loss on the sale of the property, and (2) a deduction for the amount contributed to the charity. For example:

Assume a donor wishes to make a charitable contribution of $500.00. He owns stock which cost him $1,000.00, but which is worth only $500.00:

1. He transfers the stock to the charity, and is entitled to a deduction under Section 23 (o) of the Code, of $500.00.

2. He sells the stock and then contributes the proceeds of sale to the charity. He is entitled to a deduction of $500 under Section 23 (e), limited by the capital loss provisions of Section 117. In addition, he is entitled to a deduction of $500.00 under Section 23 (o) for a charitable contribution.

In both transactions, the donor has only parted with the shares of stock, but in the latter he has become entitled to an additional deduction for the loss on the sale of the securities.

(*c*) *Valuation of Property*

It frequently happens that a taxpayer will, in planning his estate, realize that certain of his assets are more readily valued than others. If he is considering charitable transfers, either lifetime or testamentary, it should be pointed out that normally he will make the over-all plan more simple if he gives to charity property that is difficult to value. Certain types of property, such as patents, trade-marks, business interests that are closely held, and good will may present valuation problems for an executor to deal with. However, if such properties are disposed of to charity many vexing problems are by-passed. In such case, the valuation would become immaterial because the figure at which the property was included in the gross estate would be the same amount for which a deduction would be allowed for charitable bequests. By eliminating from the net taxable estate items difficult to value, the taxpayer is in a better position to estimate the estate taxes. Accordingly, a more accurate lifetime plan may be made for the estate distribution.

(*d*) *Liquidity of Property*

An estate planner knows that the assets included in the estate are of varying degrees of liquidity. Consideration, therefore, should be given to transferring to charity the less liquid assets. Since estate costs of administration and death taxes are payable in cash, provision must be made to pay such costs. If assets that are not readily convertible into cash are the only ones available to the executor, the disposition upon such assets to raise cash may present difficulties. If the need for cash is pressing, it is possible that the sale will be "forced", and that only a fraction of their true value will be realized. On the other hand, if such less-liquid assets constitute the charitable bequests and only property readily convertible into cash is turned over to the executor, the problem of financing the payment of death charges, estate administration costs and taxes is a less burdensome one. Included in the category of less-liquid assets are works of art, business interests and real estate, and generally, minority interests in close corporations.

(*e*) *Coordination with Over-All Plan*

The determination of what property shall be bequeathed to charity is not one that can be made in a vacuum. The answer to the question can only be arrived at after a detailed study and consideration of the over-all estate plan. If there are any "controlled" charities involved, the plan should take that into account. In this connection, bear in mind that if there is no existing foundation or controlled charity, the will may establish such an organization. Reference has already been made in this article to foundations, and its repetition here would serve no useful purpose. However, the ramifications of such organizations in relationship to any particular estate plan should be exhaustively considered.

It may well be that a more complete realization of a taxpayer's desires can be effected by the use of property other than the type which he presently owns. In such a case the taxpayer, either during his lifetime may change the type of property which he owns, or he may direct that after his death his executor shall make such change. If, for example, a closely-held business interest constitutes the principal asset of the taxpayer, he may wish, preliminary to making a charitable bequest, to assure that the control of the business will always remain with his family. It may require that an unincorporated business be changed to a corporation in order for his desires to be carried out. His wishes can be fulfilled through the creation of two types of stock and the bequest to charity of only the non-voting shares. This is essentially what was done in the wills of Henry Ford and Edsel Ford, where the major portions of their estates, consisting of non-voting stock in the business interests, were bequeathed to the Ford Foundation, an exempt charitable organization.

Should the primary desire of the testator be to assure an income to the charity, it might be more in accord with his wishes to cause a cumulative preferred stock or an interest bearing obligation to be created and to bequeath such preferred stock or obligation to the charitable organization. In such a way the charity will be assured of an income, regardless of the dividend policy that may be pursued by the future directors of the corporation.

It hardly need be mentioned that any proposed changes in the capital structure of a corporation should be entered into only after a full consideration of all their income tax implications so that no untoward tax consequences will result from the consummation of such plans.

### (f) *Life Insurance*

A final word with respect to the type of property that may be given or bequeathed should be expressed concerning the use of life insurance policies or proceeds thereof. If, during the lifetime of a taxpayer, an insurance contract is irrevocably transferred as a gift to a charity, the donor will be entitled to a deduction for his contribution in the amount of the replacement value of the contract. *Guggenheim v. Rasquin,* 312 U.S. 254 (1941). Signal premiums or paid-up contracts are valued at a replacement figure, but many other types of contracts cannot be replaced. However, where the policy gifted is an annual premium contract, the amount of the deduction will be the sum of the interpolated terminal reserve at the date of the gift and the proportionate part of the gross premium last paid before the date of the gift which covers the period extending beyond that date. Regulations 108, Sec. 86.19 (i).

If the donor, after irrevocably transferring all his rights in the policy to a charity, pays the premiums on the policy, he will be entitled to a deduction for income tax purposes for the premiums when he pays them. O.D. 299, 1 C.B. 151.

Upon the death of the insured, the charity will receive the proceeds of the contracts. If, because of payment of premiums, the proceeds are includible in the gross estate of the insured, the estate will be entitled to a deduction for amounts paid over to charity. *McKelvy* v. *Commossioner*, 82 F. (2d) 395 (CCA-3, 1936).