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Edward N. Polisher

Peter M. Winkelman

GIFTS TO MINORS — THEIR FEDERAL TAX IMPLICATIONS

By

EDWARD N. POLISHER*

AND

PETER M. WINKELMAN**

I GENERAL

Estate planning, unlike the majority of problems which arise in business planning, is concerned primarily with the family unit.

One of the more effective methods employed to accomplish the objective is the gift.[1]

Often gifts to minor children are used to effectuate the purpose. In most instances, the donor will not make an outright gift of the property to the minor because persons of tender years are incapable of managing property. Moreover, the ownership of most types of property by minors creates legal obstacles to their transfer. Hence, donors will utilize trusts set up by them for the benefit of the minor, with the trustee authorized or directed to use or to accumulate the income during minority and to distribute the accumulated income and corpus at or after the beneficiary attains the age of majority. It is this method of making gifts in trust which caused confused tax implications under prior law.

The 1939 *Code*, like the 1954 *Code*, provided for a lifetime exclusion from gift tax in the sum of $30,000.[2] In addition, the donor is allowed an annual exclusion of $3,000 per donee, except where the gift is of a future interest.[3] Under prior law, virtually all gifts in trust to a minor were held to be gifts of future interests. Before discussing the pertinent provisions enacted by the 1954 *Code*, it is necessary to examine factual situations which caused tax uncertainty under the prior law.

Definition of "Future Interest"

The term "future interest" is defined in Regulations 108, Section 86.11, implementing the 1939 *Code*, as follows:

*Edward N. Polisher—LL.B. Dickinson Law School; member of the Philadelphia Bar; Chairman of the Committee on Taxation, Philadelphia Bar Association; Author of "Estate Planning and Estate Tax Saving"; Lecturer on taxation, Dickinson School of Law.

**Peter M. Winkelman—LL.B. University of Southern California, 1953; LL.M. University of Southern California, 1954; Member of the law firm of Kaufman and Leland, Los Angeles, California; Member of ABA, Section of Taxation, National Resources Committee; Instructor of law, School of Engineering, University of Southern California.

1 See Polisher, Estate Planning and Estate Tax Saving, p. 407 et seq.
2 1939 I.R.C. § 1004(a)(1); 1954 I.R.C. § 2521.
3 1939 I.R.C. § 1003(b)(3); 1954 I.R.C. § 2503(b).

" 'Future interest' is a legal term, and includes reversions, remainders, and other interests or estates, whether vested or contingent, and whether or not supported by a particular interest or estate, which are limited to commence in use, possession or enjoyment at some future date or time."

The term is not to be used in the same sense as in the law of conveyancing. One court stated it as follows:

". . . future estates, as the term is used in the statute, are not to be understood as interests, similarly designated in the law of conveyancing. They are, rather, interests in land or other things, in which the privilege of possession or of enjoyment is future and not present; and the one essential is the possibility of future enjoyment."[4]

The term was further defined in *Fondren v. Commissioner.*[5]

". . . It is not enough to bring the exclusion into force that the donee has vested rights. In addition, he must have the right presently to use, possess or enjoy the property. These terms are not words of art, like 'fee' in the law of seizin . . . but connote the right to substantial present economic benefit. The question is of time, not when title vests, but when enjoyment begins. Whatever puts the barrier of a substantial period between the will of the beneficiary or donee now to enjoy what has been given him and that enjoyment makes the gift one of a future interest within the meaning of the regulation."

The reason for denying the exclusion for gifts of future interests is stated in House Committee Report No. 708, 72d Congress, 1st Sess., p. 29; Senate Committee Report No. 665, 72d Congress, 1st Sess., p. 41 (1932):

"The exemption being available only insofar as the donees are ascertainable, the denial of the exemption in the case of future interests is dictated by the apprehended difficulty, in many instances, of determining the number of eventual donees and the values of their respective gifts."

II GIFTS IN TRUST FOR MINORS — PRIOR TO 1954 CODE

Where the gift to the minor is made through an inter vivos trust, the income and corpus may be distributable to the minor, or for his benefit, or withheld from him, under various conditions, or on the happening of stipulated contingencies. Each situation has its own gift tax implication.

Accumulation of Income and Distribution of Income and Corpus at a Later Date

1. The leading Supreme Court case involving the accumulation of income, with distribution of accumulated income and corpus at a future date, is *United States v. Pelzer.*[6] There, the donor created a trust for the benefit of his grandchildren, eight of whom were then living and named as beneficiaries. The income was to be accumulated for ten years, at the termination of which time living grandchildren,

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4 Comm. v. Wells, 132 F.2d 405 (6th Cir. 1942); see Polisher, op. cit., p. 443 et seq.

5 324 U.S. 18, 20, 65 Sup. Ct. 499, 89 L.Ed. 668 (1954).

6 312 U.S. 399, 61 Sup. Ct. 659, 85 L.Ed. 913 (1941).

including grandchildren both after the creation of the trust, were to begin receiving income from the trust. The gifts were held to be future interests because the beneficiaries had to survive the ten year period in order to receive the benefits under the trust intrument. "The 'use, possession or enjoyment' of each donee is thus postponed to the happening of a future uncertain event."

2. *Accumulation of Income and Distribution of Accumulated Income and Corpus at a Later Date — Trustee Has Power to Invade for Benefit of Minor*

(a.) Trustee's power discretionary. A second situation involving gifts to minors is in those cases where distribution was to be deferred until the minor attained a specified age but where the trustee had the discretion to distribute the income or invade the corpus to provide for the support, maintenance and education of the minor beneficiary. There are two Supreme Court decisions on this point.[7]

In *Fondren v. Commissioner,*[8] gifts were made to seven irrevocable trusts for the benefit of the donor's minor grandchildren. The income was to be accumulated, and the corpus and accumulated income were to be distributed to the beneficiaries at specified dates in the future. The final distribution of corpus and accomulated income was to be made when the beneficiaries reached the age of thirty-five. The instrument further provided that the trustee was to have the discretion to invade the corpus to provide for the maintenance, education and support of the beneficiaries whenever the trustee considered such action to be necessary. The taxpayer asserted that he should be allowed the annual exclusion, that the gift was not of a future interest since the trustee's power to invade corpus gave the beneficiary the present right of enjoyment of the trust property. The court rejected this contention, holding that, although the trustee had the power to distribute corpus to the beneficiaries if the need arose, the gift was of a future interest because distribution was contingent upon the need arising. Since this was an event which was not certain to occur, the interest was future. The court also stated:

> "It does not follow, as petitioners say, that if the exemption does not apply in this case it can apply in no other made for a minor's benefit. Whenever provision is made for immediate application of the fund for such a purpose, whether of income or of corpus, the exemption applies."

In *Commissioner v. Disston,*[9] the income was to be accumulated for each minor until he reached the age of twenty-one; thereafter the income was to be paid to each beneficiary until he attained the age of forty-five, at which time he received his share of the principal. The trustees had the discretion to apply trust income to the support of the minors and also to invade corpus, if necessary. It was held that the gifts were of future interests. The taxpayer argued that the provisions

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7 For a more comprehensive discussion of this situation, see Polisher, "Recent Developments in Federal Gift Tax", 50 Dick. L. Rev. 49 (1946).

8 324 U.S. 18, 65 Sup. Ct. 499, 89 L.Ed. 668 (1945). See also, Rassas v. Comm. 196 F.2d 611 (7th Cir. 1952).

9 325 U.S. 442, 65 Sup. Ct. 1328, 89 L.Ed. 1720 (1945).

authorizing the trustee to apply the income to the support of the minors and to invade corpus, distinguished this from the *Fondren* case. Commenting upon this contention, the Court stated:

> "But, even though the trustees were under a duty to apply the income for support, irrespective of outside sources of revenue, there is always the question how much, if any, of the income can actually be applied for the permitted purposes. The existence of a duty so to apply the income gives no clue to the amount that will be needed for that purpose, or the requirements for maintenance, education and support that were foreseeable at the time the gifts were made. In the absence of some indication from the face of the trust or surrounding circumstances that a steady flow of some ascertainable portion of income to the minor would be required, there is no basis for a conclusion that there is a gift of anything other than for the future."

(b.) Trustee required to invade corpus. A variation of the above situation arises where the trusteee is *required* by the trust instrument to invade corpus for the benefit of the minor beneficiary.

In *Smith v. Commissioner,*[10] the taxpayer created two trusts for her grandchildren, ages sixteen and nineteen respectively. The trustees were empowered and directed, in their sole discretion, to use the principal and income for the education and preparation of the beneficiaries to attain and occupy a desirable position in life and to pay each beneficiary his share of the corpus at the age of twenty-four. The Court held that the gifts were of present interests because it was apparent that the trustee was compelled to invade corpus in order to carry out the instructions of the donor. The Court distinguished the *Pelzer* case on the ground that there the trustee could not distribute corpus for a period of ten years. The Court also distinguished *Commissioner v. Gardner,*[11] in which it was held that the gifts were of future interests. In the latter, stated the court, the trustees could only distribute such part of the corpus as they deemed necessary for the support, maintenance and education of the beneficiaries, after consultation with the minor beneficiaries. The power of the trustee might or might not be exercised.

There is some question as to whether or not the *Smith* case remained good law after the *Fondren* and *Disston* decisions. In both cases the trustee had the discretion to invade corpus, whereas the basis for the *Smith* decisions was that the trustee was compelled to invade corpus in order to carry out the terms of the instrument. According to the cases which followed the *Fondren* decision, the *Smith* case apparently continued to be good law.

For example, in *Willis D. Wood,*[12] the taxpayer made a gift of property in trust for a minor, the income to be accumulated and distributed with the corpus when the minor attained the age of twenty-one. The trustee was required to make distributions of income and corpus to the minor only upon the request of the donor.

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10 131 F.2d 254 (8th Cir. 1942).
11 127 F.2d 929 (7th Cir. 1942).
12 16 TC 962 (1951).

It was held that the gift of income was the gift of a future interest because it was contingent upon the taxpayer making a request for distribution. The *Smith* case was distinguished on this basis.

The *Smith* case was also differentiated in *Katherine Schuhmacher*,[13] on the ground that the minors did not have the right to the present enjoyment of the property.

3. *Accumulation of Income and Distribution of Income and Corpus at a Later Date — Minor, Through Guardian Has Right to Terminate Trust at Any Time*

A recent innovation has occurred where the income was to be accmulated and distributed with corpus at a later date.[14] The minor or the minor through his guardian had the right to terminate the trust and demand the corpus at any time. The courts were split in their interpretation of this provision.

In *Kieckhefer v. Commissioner*,[15] the taxpayer made a gift in trust to his grandson and the trustee was directed to pay to the beneficiary such income from the trust as may be necessary for his education, comfort and support and to accumulate the balance until the grandson reached twenty-one. The trustee was directed to pay over the entire corpus to the grandson, whenever the grandson or his legally appointed guardian made a demand in writing for the corpus. Under applicable state law, the minor could not make such a demand without the appointment of a guardian. The court held that the gift was of a present interest, since the grandson had the right to the corpus at any time. The court added that since it was state law, rather than the donor, which imposed restrictions on the beneficiary's right to demand the corpus, the transfer was of a present interest.

A different result was reached in *Stifel v. Commissioner*,[16] where the taxpayer created three irrevocable trusts for his minor children, aged eleven, seven and four respectively. The trustee was directed to apply the income from the trust and so much of the principal as, in his discretion, was necessary for the support, etc. of the children during their lifetime and upon their death to pay the income to their executors. The power was given to the children or their guardians, during their minority, to terminate the trust by demanding payment of the corpus and accumulated income. The court stated that if the beneficiaries had been adults, their interests would have been present, but here the following differentiating factors were present: (1) None of the children could himself have made such a demand; he could only do so through a guardian; (2) the donor did not wish to have a guardian appointed because he wanted the children to learn how to handle money themselves; (3) no guardian was appointed. On these facts it was held that the interests created were future. The *Kieckhefer* case was distinguished on the ground that there a guardian had been appointed. The court stated that if

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13 8 TC 543 (1947).
14 See Polisher, op. cit., Supplement, p. 155.
15 189 F.2d 118 (7th Cir. 1951). See also Strekalovsky v. Delaney, 78 F. Supp. 556 (D.C. Mass. 1948); Gilmore v. Comm., 213 F.2d 520 (6th Cir. 1954).
16 197 F.2d 107 (2d Cir. 1952).

there had been a guardian who could have demanded the corpus at any time, the result might have been different.

A recent revenue ruling[17] dealth with the situation where gifts were made in trust, the terms of which provided that the trustee, in his uncontrolled discretion, was to use the net income and principal for the support, education or benefit of the donor's minor children, in such amounts and at such times as shall be in accordance with the needs of the beneficiaries, as though he were holding the property as guardian of the beneficiaries. There was no legal guardian appointed. It held that since no guardian was ever appointed to demand immediate distribution, the gift was of a future interest.

Another ruling,[18] however, held that where stock is issued in the name of a minor and the gift is unqualified and unrestricted, there is a gift of a present interest, even though a legal guardian is not appointed. ". . . disabilities placed upon minors by state statutes should not be considered decisive in determining whether such donees have the immediate enjoyment of the property or the income therefrom within the purport of the federal gift tax law."

4. *Corpus a Gift of a Future Interest; Income a Gift of a Present Interest*

(a.) No power to invade corpus. Although the gift of corpus might be a future interest, if the income were presently distributable, the income could qualify as a present interest.[19]

(b.) Trustee has power to invade corpus. Where the income was payable annually to the beneficiary, with the corpus to be distributed at a later date, and the trustee had the power to invade corpus for the benefit of the beneficiary, the gift of corpus was a future interest, and the gift of annual income was also held to be a future interest. The taxpayer contended that the annual exclusion should be available because each beneficiary's present right to income from the corpus could not be diminished by the child's future receipt of the principal itself. Any distribution of principal would merely have the economic effect of adding beneficial incidents of ownership to those which the child already possessed.

The Commissioner on the other hand asserted that, since the right to income was subject to termination at any time by transfer to the beneficiary of the entire principal, it was impossible to assign any value as a gift in present enjoyment to the right to receive the income. The Commissioner prevailed in *Evans v. Commissioner.*[20] There the taxpayer set up a trust for her six children. The trustee was directed to pay the net income to the children for life and was further directed to expend such sums from corpus for the education, comfort and support of each child as he, in his uncontrolled discretion, shall deem necessary. The instrument provided for gifts over upon the death of each child. The court held that the gift

17 Revenue Ruling 54-91, I.R.B. 1954-10, p. 14.
18 Revenue Ruling 54-400, I.R.B. 38, p. 13.
19 Sensenbrenner v. Comm., 134 F.2d 883 (7th Cir. 1943); Jesse S. Phillips, 12 TC 216 (1949); Fisher v. Comm., 132 F.2d 383 (9th Cir. 1942); Edward J. Kelly, 19 TC 27 (1952).
20 198 F.2d 435 (3rd Cir. 1952).

of principal was a future interest, whereas the gift of income was a present interest. But the annual exclusion on account of the gift of income was not allowed because it could not be valued. That is, since the corpus which produced the income could be destroyed, or reduced at a later time, the amount, and thus the present income interest, was incapable of valuation at the time the gift was made.[21]

In *Kniep v. Commissioner*,[22] the taxpayer prevailed. Trusts were created in which the income was payable to the beneficiaries each year, until the beneficiaries attained the age of sixty, at which time they were to receive their proportionate share of corpus. The trustees had the discretionary power to invade corpus for the maintenance of the beneficiaries or in case of an emergency. But this power was limited to the amount of $1,000 a year. Payments thus made were not to affect the beneficiary's share of income but were to be deducted from the share of the corpus otherwise payable to that beneficiary. It was held that for purposes of determining the annual exclusion, the present rights to income were valued by deducting from corpus each year the maximum amounts which the trustees could invade for that year.

The rule of the *Evans* case has been changed by Section 2503(b) of the 1954 *Code.*

III CHANGES MADE BY 1954 REVENUE CODE

1. *Present Interest Subject to Power to Diminish*

Section 2503(b) provides that where there has been a transfer to any person of a present interest in property, the possibility that such present interest may be diminished by the exercise of a power shall be disregarded in determining whether the gift of such an interest is a future interest, provided that no part of such interest will at any time pass to any other person. This provision applies to adult beneficiaries as well as minor beneficiaries. Thus, assume that under the terms of a trust, the income is payable to A for life, with the remainder payable to B upon A's death, and that the trustee has uncontrolled power to pay over the trust principal to A in whole or in part at any time. Although in such case A's present right to receive income may be terminated, no other person has the right to such income interest. Accordingly, under this section, the present right in A will not be treated as a gift of a future interest. This rule will not apply, however, if the trustee would pay over any part of the corpus during A's life to persons other than A. The crucial requirement under this section is that A's income interest cannot be affected or reduced during his lifetime. The fact that the corpus will pass to B on A's death will not prevent A's income interest from being deemed a present interest. The Cod, however, does not provide how such interest shall be valued.

21 See also Cadwell Tyler II, 12 T.C.M. 407 (1953). In Floyd H. Newmaker, 12 T.C.M. 232 (1953), the same result was reached in a gift in trust of stock in a family corporation, where there was no established dividend policy nor any assurance, because of family control, that future dividends would ever be paid.
22 172 F.2d 755 (8th Cir. 1949).

In the *Kniep case,*[23] the income interest was valued with reference to the maximum amount by which the trustee was authorized to invade corpus each year. That will not aid where the power to invade is unlimited. Perhaps where there is an unlimited discretion to invade corpus for the benefit of the minor, as was true in the *Evans* case,[24] the method of valuation may be ascertained by reference to the "charitable remainder" cases.[25] These cases are concerned with the problem of a testator leaving a life interest in property to a named benficiary in trust, the trustee to have the power to invade the corpus for the "comfort and welfare" of the life tenant and the remainder to go to a named charity. In these cases, the courts have held that where the power to invade is limited to a definite standard, the charitable remainder is capable of valution. Where the power of invasion, however, is not limited by a definite standard, the gift cannot be valued.[26] The same valuation standards used in these cases could be applied in valuing the interest of a gift to a minor.[27]

2. *Gifts to Minors*

(a.) 1954 *Code* provision. Section 2503(c) provides:

> "No part of a gift to an individual who has not attained the age of 21 years on the date of such transfer shall be considered a gift of a future interest in property for purposes of subsection (b) if the property and income therefrom:
>
> (1) may be expended by, or for the benefit of, the donee before his attaining the age of 21 years, and
>
> (2) will to the extent not so expended —
>
> (A) pass to the donee on his attaining the age of 21 years, and
> (B) in the event the donee dies before attaining the age of 21 years, be payable to the estate of the donee or as he may appoint under a general power of appointment as defined in Section 2514(c)."

The problems of interpreting the section do not appear to be unduly intricate. First, both the income and property must conform to the specified condition or no part of the gift will qualify under the section. Thus, *Sensenbrenner v. Commissioner*[28] and similar cases, which held that the gift of corpus could be a future interest,

[23] See n. 22, supra.
[24] See n. 20, supra.
[25] See Ithaca Trust Co. v. U.S., 279 U.S. 151, 49 Sup. Ct. 291, 73 L.Ed. 647 (1929); Blodget v. Delaney, 201 F.2d 589 (1st Cir. 1953); Reg. 105, § 81.44; Polisher, op. cit. 337-346.
[26] See Reg. 105, §§ 81.10(i), and 81.10(j) for valuation tables. See Polisher, op. cit. 348-349; 275-279.
[27] Merchants National Bank of Boston, Exec. v. Comm., 320 U.S. 256, 64 Sup. Ct. 108, 88 L.Ed. 35 (1943); Gammons v. Hassett, 121 F.2d 229 (1st Cir. 1941), cert. denied, 314 U.S. 673, 62 Sup. Ct. 135, 86 L.Ed. 538 (1941). But see Comm. v. Estate of L. Sternberger, 55-1 U.S.T.C. Para. 11,504 (U.S. S. Ct. 1955), where the charitable bequest was to take effect only if decedent's childless twenty-seven year old daughter died without descendants surviving her and her mother. The Tax Court and Court of Appeals had approved the estate's actuarial computations as fairly reflecting the present value of one-half of a two million dollar residue, reduced in proportion to the chance that the charity will receive it. The following actuarial tables were used: (1) Combined Experience and Mortality Table prescribed in section 81.10 of the estate tax regulations, to determine the joint life expectancy of decedent's wife and daughter. (2) Th eAmerican Remarriage Table,

while the gift of income could be a present interest, are overruled. Under the House Bill, the income was *required* to be expended for the minor's benefit, for the exclusion to be available.[29] This provision, however, was changed by the Senate so that now the exlusion will apply if the income or property *may* be expended for the minor's benefit before he attains the age of twenty-one.

(b.) May be expended for the benefit of the donee. If the corpus or income is not expended on behalf of the donee, the corpus must pass to the minor upon his reaching the age of twenty-one. Thus, if the income and corpus is to be retained in trust until the beneficiary reaches the age of twenty-four, the exclusion would not be available. If the trust is not to terminate until the donee attains the age of twenty-four, but under the terms of the trust the income or corpus may be expended in its entirety for the benefit of the minor before the minor attains the age of twenty-one, the gift would not qualify as the gift of a present interest.

(c.) Payable to the estate. This phrase may be illustrated by several simple examples. If the beneficiary dies before he reaches the age of twenty-one and the trust provides that the corpus must be paid to his estate, although actual payment is not made until after the decedent would have been twenty-one, the exclusion would undoubtedly be applicable.

If the trust instrument provides that, in the event the donee dies before attaining the age of twenty-one, the corpus shall pass to X, the exclusion would not be available because clearly the corpus does not pass to the estate of the minor-beneficiary.

(d.) General power of appointment. May a minor make a will? Under the law of many states, there are restrictions on the power of a minor to dispose of his property by will.[30] Hence, in drafting trust instruments, the donor should provide that if the minor dies before attaining the age of twenty-one, the property shall pass to the person or persons he shall appoint, but if he cannot validly exercise such power because of a disability imposed by state law, the property shall pass to his estate.

If the donor were given the power to designate takers in default of the exercise of the power of appointment, a serious question would arise as to whether the gift had ever been completed. Although there are no cases directly in point, it would appear that the retention of a power to change the beneficial interests

published by the Casualty Actuarial Society, to establish the probability of remarriage of the daughter. (3) To estimate the chance of a first child being born to decedant's daughter, a table prepared in accordance with accepted actuarial principles upon data derived from statistics published by the Bureau of Census. The Court denied the deduction because there was no assurance that the charity would receive anything. The case appears to cast some doubt upon the use of actuarial tables in computing charitable deductions, at least where the tables used are other than the life expectancy tables prescribed by the Commissioner.

28 See n. 19, supra.

29 H.R. 8300 § 2503(c), p. 358.

30 Atkinson, Wills, 2d Ed. 1953, p. 230. The rules in the various states are collected in Bordwell, Statute Law of Wills, 14 Iowa L. Rev. 177-179 (1929).

may be sufficient to render the gift incomplete.[31] Moreover, the gift would fail to meet the requirements of Section 2503(c) as a present interest.

(e.) Use of qualifying trust for successive gifts. Once the trust is created for the benefit of the minor, so that it qualifies as a present interest, as to which the annual exclusion would be available under the 1954 *Revenue Code,* there would be no reason, tax-wise, why the same trust may not be the recipient of additional gifts in succeeding years. Moreover, should the donor's spouse consent to the gift, the donor could double the gift-tax-free transfer to the trust for each beneficiary, up to the amount of $6,000 annually.[31a]

The problem, aside from the gift tax implications, of utilizing the trust for additional, successive gifts, would lie in the wisdom of accumulating a substantial amount of assets in the trust, which must be turned over to the beneficiary when he reaches twenty-one years of age.

(f.) Estate tax implications.

(1) To the donor of the property. If the donor parts with the complete control over the property, it will not be includible in his gross estate, for federal estate tax purposes, absent a transfer in contemplation of death. Ownership vests in the donee and he need not survive the donor in order to obtain the enjoyment and possession of the property.[32]

(2) To the minor. It seems clear that where the corpus is payable to the estate of the beneficiary, the property would be includible in the latter's gross estate. If the beneficiary were given a special power of appointment over the corpus, it would result in excluding the property from his gross estate, but this would simultaneously deny to the donor the annual gift tax exclusion with respect to the gift.

(g.) Income tax implications.

(1) Amounts paid to a beneficiary the donor is obligated to support. Under Section 2503(c) the donor may obtain the benefit of the annual gift tax exclusion, if the income or corpus *may* be distributed to the beneficiary. Under Section 677 (b), such a provision does not render the income taxable to the grantor unless it is actually paid for the support of the minor beneficiary whom the grantor is under an obligation to support.[33] If the trust instrument, however, *requires* that the income be used to support such a beneficiary, the income will also be taxable to the grantor.[34]

A power in the donor as trustee to distribute corpus will not render the trust income taxable to the donor if, (1) the power is limited by a reasonably defin-

31 See Polisher, op. cit. 431-439.
31a Helvering v. Hutchings 312 U.S. 393, 61 Sup. Ct. 653, 85 L.Ed. 909 (1941); Reg. 108, § 86.10. Each beneficiary, not the trust, is considered the donee for the purposes of the annual exclusion.
32 Regulation 105, § 81.17, examples 3 and 6.
33 Section 667(b) corresponds to Section 167(c) of the 1939 Code; see Polisher, op. cit. 379 et seq.
34 Comm. v. Schweitzer, 296 U.S. 551 (1935).

ite standard which is set forth in the trust instrument, or (2) the power is to distribute to an income beneficiary, provided that the distribution of corpus must be chargeable against the proportionate share of corpus held in trust for the payment of the income to the beneficiary as if the corpus constituted a separate trust.[35]

Under Section 678(c), a trustee, who is not the donor, may be subjected to tax on the income applied to the support of a beneficiary, where the beneficiary is one whom the trustee is obligated to support. Thus, if a grandfather established a trust for the benefit of his grandchild with the donor's son as the trustee and the trustee used the income to support his son, the son would be taxed on such income.

(2) Power to withhold income during minority. Under Section 674(b) the grantor of a trust may be given the power to withhold the distribution of the income of a trust to a beneficiary without having the income therefrom taxable to himself. In the case of all beneficiaries except minors, the income so accumulated must ultimately be payable to the beneficiaries, to the estate of the beneficiaries or to their appointees; or upon termination of the trust, to the current income beneficiaries. Under Section 674(b)(7), however, the grantor has the power to withhold the income from distribution to a beneficiary during the period of minority and add it to corpus without being taxed on the income, even though there is no provision for ultimate distribution to the beneficiary or to his estate. This section would provide income tax advantages to a grantor using short-term trusts, but note that unless the corpus and accumulated income passes to the beneficiary at the age of twenty-one, the annual gift tax exclusion will be lost.

In granting the power to the trustee to withhold income from minor beneficiaries, the donor must not act as the trustee. If he does, the trust corpus will be includible in his gross estate for federal estate tax purposes. For example, in *Lober v. United States,*[36] the decedant was the trustee of trusts for his children. He had the power to invest and reinvest the trust corpus in whatever manner he deemed to be proper. He could accumulate and reinvest the income in the same manner, but when the children attained the age of twenty-one they were to be paid the accumulated income. The principal was to be paid to each child upon attaining the age of twenty-five. The trusts were irrevocable and if any child died before reaching twenty-five, his share passed to his estate. The decedant had the power to terminate the trusts at any time and pay over the corpus to his children. On these facts it was held that the property was includible in the gross estate of the decedent.

III Conclusion

While a gift to a minor may result in tax savings, the gift might prove to be wasteful, and, therefore, should not be made, if it would result in handing over a large amount of property to the minor upon his attaining the age of twenty-one. Ordinarily, beneficiaries of such years are inexperienced in the

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[35] See 1954 I.R.C., § 674(b)(5).
[36] 346 U.S. 335 (1953).

management, conservation and disposition of substantial property values. The effect upon the beneficiaries themselves having control over important sums of money or property, upon their futures, their work attitudes and careers may be disruptive. The tax savings could easily be lost by the unwise dissipation of the funds by the erstwhile minor. Before transferring valuable assets in trust for the benefit of his children, the donor should also consider that, although his current property holdings may be sufficient to maintain his standard of living now, changes in his economic status by whatever cause could result in severe hardship. The donor's steps once taken cannot be retraced. Thus, in making a gift to a minor, the donor must take into account not only the income, estate and gift tax consequences, but he also should reflect upon the social and economic results which might flow from such a gift.