

CHARITABLE REMAINDER TRUSTS UNDER THE TAX REFORM ACT OF 1969

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I. INTRODUCTION

Prior to the enactment of the Tax Reform Act of 1969,¹ the complex rules for determining the amount of a charitable deduction in the case of gifts of remainder interests in trust often operated inequitably with the result that the deductible amount did not necessarily reflect the value of the benefit which the charity ultimately received.

The primary problem—proper valuation of the charitable interest—was complicated by the very nature of the trust instrument itself in that the interests of the income beneficiary and remainderman of a trust often compete with one another, creating a conflict of interest. The income beneficiaries generally desire that the trustee pursue an investment policy which maximizes income, notwithstanding the fact that such a policy may require the trustee to sacrifice growth or even the security of the corpus. The remainderman's concern, on the other hand, lies with the protection of the corpus.

This conflict was compounded by the fact that prior to the Act the trustee was allowed considerable discretion in the administration of the trust so that he could manipulate the trust to benefit one of the interested parties more than the other. The conflict of interests and the manipulation possibilities posed extremely difficult problems with regard to the valuation of the charitable remainder. For example, prior to the Act a donor could contribute property to a trust providing that the income be paid to private persons for a period of years with the remainder going to charity. A charitable deduction generally was available for the charitable remainder interest. Under prior law, however, the amount of the allowable deduction would be determined on the basis of the unrealistic assumption that the trust earned 3½ percent a year; the present value of the periodic income payments was determined by discounting the anticipated payments at 3½ percent. In fact, the trust assets could be invested in certain property, such as high-income, high-risk assets, so as to maximize the non-charitable income interest, with the result that there was little relationship between the interest assumptions used in calculating present values and the amount

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¹ P.L. 91-172, 91st Cong., 1st Sess. (1969).

actually received by the charity.² The trustee often regarded the non-charitable interest as the prime object of the donor's bounty, charting an investment policy which favored the non-charitable party to the possible detriment of the charity.

In addition to the nature of the trustee's investment policy, a substantial number of administrative problems existed, including allocation of receipts and expenditures between income and principal, which presented unjustified opportunities for insuring that the amount actually received by the charity would be less than the amount assumed in calculating the donor's deductions.

Another aspect of the valuation problem under prior law was exhibited in cases where charitable contribution deductions were allowed for gifts of charitable remainder interests in trust even though it was unlikely that the gift would ultimately be received by the charity.³ For example, there were situations where the charity's only interest was a contingent remainder interest (i.e., a \$5,000 annuity to *A* for life, remainder to his children or to a charity if *A* had no children);⁴ or there might be a vested remainder to charity, but the trust permitted invasion of the charitable share for the benefit of the non-charitable intervening interest to an extent which was incapable of reasonably certain actuarial valuation (i.e., a \$5,000 annuity to *A* for life, remainder to a charity, but the trust provided that the trustee could pay *A* amounts in excess of \$5,000 in order to maintain his standard of living).⁵ If the gift to charity was subject to a contingency, the regulations in existence prior to the Act provided that no deduction was allowable unless the possibility that the charity would not take was so remote as to be negligible.⁶ If the gift to charity was subject to a power of invasion in favor of a non-charitable beneficiary, the existing regulations⁷ and cases⁸ allowed the deduction where the power

² H.R. Rep. No. 91-413, 91st Cong., 1st Sess. 58 (1969); S. Rep. No. 91-552, 91st Cong., 1st Sess. 87 (1969).

³ H.R. Rep. No. 91-413, 91st Cong., 1st Sess. 58 (1969).

⁴ *United States v. Provident Trust Co.*, 271 U.S. 272 (1934); See also *Allen v. First Nat'l Bank of Atlanta*, 169 F.2d 221 (5th Cir. 1948); Rev. Rul. 59-143, 1959-1 Cum. Bull. 247; *Commissioner v. Sternberger's Estate*, 348 U.S. 187 (1955), reversing 207 F.2d 600 (2d Cir. 1953); *United States v. Dean*, 224 F.2d 26 (1st Cir. 1955).

⁵ *Estate of Mary Cotton Wood*, 39 T.C. 919 (1963); *Estate of Oliver Lee*, 28 T.C. 1259 (1957), where the deduction was allowed notwithstanding the trustee's power to invade in case of "emergency"; *Mercantile-Safe Deposit & Trust Co. v. United States*, 252 F. Supp. 191 (D. Md. 1966).

⁶ Treas. Reg. §§ 1.170-1(e), 20.2055-2(b), 25.2522(a)-2(g) (1958). [All citations to sections in this article are to sections of the Internal Revenue Code of 1954, as amended to date of publication, unless otherwise indicated.] See generally Lowndes, *Tax Advantages of Charitable Gifts*, 46 Va. L. Rev. 394, 416 (1960). But cf. § 170(a)(3), which in certain cases postpones the deductions of a remainder interest in tangible personal property.

⁷ Treas. Reg. §§ 20.2055-2(b), 25.2522(a)-(b) (1958).

⁸ *Henslee v. Union Planters Nat'l Bank & Trust Co.*, 335 U.S. 595 (1949); *Mer-*

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to invade was limited by an ascertainable standard, which under the circumstances of the particular case made it virtually certain that the charity would take an ascertainable amount of the property. The deduction was allowed to the extent of the ascertainable amount of the property. While the courts have tended to find an ascertainable standard if the trustee's power to invade the principal is limited to amounts necessary to support the life tenant at his accustomed standard of living, a contrary result has been reached if the trustee is authorized to invade the principal for the desires, as distinguished from the needs, of the life tenant.⁹ Thus, the deduction has been disallowed because the trustee was empowered to invade the principal to provide for the life tenant's "happiness"¹⁰ or "pleasure."¹¹ These types of charitable gifts have spawned much litigation over the years with the results dependent upon the facts and circumstances of each case.¹²

It was the potential for manipulation to the detriment of the charitable remainderman, along with the uncertainty in valuation, that led Congress to introduce new rules¹³ in the Tax Reform Act of 1969, providing that a deduction for income, gift or estate tax purposes will not be allowed¹⁴ for a charitable remainder interest, unless the trust

chants Nat'l Bank v. Commissioner, 320 U.S. 256 (1943); Ithaca Trust Co. v. United States, 279 U.S. 151 (1929). See generally C. Lowndes & R. Kramer, *Federal Estate and Gift Taxes* 363-65 (1962).

⁹ Union Trust Co. v. Tomlinson, 355 F.2d 40 (5th Cir. 1966); Kline v. United States, 202 F. Supp. 849 (N.D.W. Va. 1962), *aff'd per curiam*, 313 F.2d 633 (4th Cir. 1963).

¹⁰ McGraw v. United States, 229 F. Supp. 118 (W.D. Va. 1964); Estate of Harriet M. Harris, 23 T.C.M. 635 (1964).

¹¹ Henslee v. Union Planters Nat'l Bank & Trust Co., 335 U.S. 595 (1949).

¹² See also Estate of Schildkraut v. Commissioner, 363 F.2d 40 (2d Cir. 1966), *cert. denied*, 386 U.S. 959 (1957); Estate of Choffin v. United States, 222 F. Supp. 34 (S.D. Fla. 1963); Florida Nat'l Bank v. United States, 62-2 U.S.T.C. ¶ 12,052 (S.D. Fla. 1962); Estate of Jean S. Alexander, 25 T.C. 600 (1955); Estate of Helen Stow Duker, 18 T.C. 887 (1952).

¹³ The new unitrust and annuity rules apply for income and gift tax purposes to transfers in trust and contributions made after July 31, 1969, and for estate tax purposes generally in the case of decedents dying after December 31, 1969. Subject to the exceptions provided in the Act in § 201(g)(4)(B), (g)(4)(C). However, the proposed regulations under new Int. Rev. Code of 1954, § 664, which were published in the Federal Register, August 5, 1970, provide a transitional rule which allows trusts created after July 31, 1969, and prior to January 1, 1971, to amend retroactively their governing instruments to fit within the definition of either a charitable remainder annuity trust or a charitable remainder unitrust. The only pre-amendment requirement is that an irrevocable remainder interest be left to charity. Proposed Treas. Reg. § 1.664-1(f), 35 Fed. Reg. 12469 (1970).

¹⁴ Another provision in the Act, § 201(f)(3), denies a deduction for an outright gift of a remainder trust to a charity except to the extent a deduction would have been allowed if the gift had been in trust. This has the effect of denying a charitable contribution deduction in the case of a non-trust gift of a remainder interest to charity. S. Rep. No. 91-552, 91st Cong., 1st Sess. 87 (1969). Exceptions to the general rule are provided, however, for gifts of an undivided portion of the taxpayer's entire interest in

is either in a specifically defined "annuity" or "unitrust" form.¹⁵ The purpose of the new rules is to provide a closer correlation between the charitable contributions deduction and the benefit ultimately received by the charity.¹⁶

Congress believed that the troublesome factor which created these problems—the conflict of interest between the remainderman and the income beneficiary—would be removed if the interests of the beneficiaries were not in the competing funds of principal and income, but were, rather, in exactly the same fund. Under the unitrust and annuity concept all income received is combined with the principal in a single fund, and, for purposes of determining the payment to the holder of the non-charitable "income" interest, there is no distinction between income and principal. The non-charitable beneficiary is to receive payments each year equal to a stated dollar amount or a specified percentage of the market value of the trust property. All incentive for the trustee to invest the property for the benefit of the income beneficiary is removed.¹⁷ Such a unitrust or annuity trust makes it possible for the trustee to pursue either a growth-oriented or income-oriented investment policy (or a combination thereof) with the assurance that neither investment policy could benefit one party to the detriment of the other. An examination of the provisions of the 1969 Act relating to charitable remainder trusts will show how Congress hoped to alleviate the problems that existed under prior law.

II. THE NEW RULES UNDER THE ACT

A. *Definitions and Payout Requirements*

1. *Charitable Remainder Annuity Trust*

A charitable remainder annuity trust is a trust from which a sum certain (which is not less than 5 percent of the *initial* net fair market value of all property placed in trust) is to be paid, not less often than annually, to one or more persons, at least one of which is not an organization described in section 170(c). Following the termination of the

property and remainder interest in a personal residence or farm. Int. Rev. Code of 1954, § 170(f)(3)(B).

¹⁵ The charitable deduction is also available for contributions to "pooled income arrangements," which have become an established form of charitable giving, and which are especially popular with colleges and universities. See Int. Rev. Code of 1954, §§ 170(f)(2)(A), 642(c)(5), 2055(e)(2)(A), 2522(c)(2)(A).

¹⁶ H.R. Rep. No. 91-413, 91st Cong., 1st Sess. 59 (1969); S. Rep. No. 91-552, 91st Cong., 1st Sess. 87 (1969).

¹⁷ The unitrust concept was presented as a solution to the problems created by conflicting interests in the same fund by Robert M. Lovell. See Lovell, *The Unitrust*, 105 *Trusts & Estates* 215 (1966). See also Del Cotto & Joyce, *Taxation of the Trust Annuity; the Unitrust Under the Constitution and Internal Revenue Code*, 23 *Tax L. Rev.* 257 (1968).

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above-stated payment (which is the only amount that may be paid to a non-charitable party),¹⁸ the remainder interest of the trust is to be transferred to, or for the use of, an organization described in section 170(c), or is to be retained by the trust for such a use.¹⁹

Example: A places securities valued at \$100,000 in trust, his son to receive \$6,000 annually for life, remainder to A's church.

The proposed regulations define a "sum certain" as a stated dollar amount that is the same as to each recipient or as to the total amount payable over the permissible period.²⁰ The requirement that the amount of the annuity be the same each year prevents the annuity from being determined by reference to a price index or from changing specified amounts at specified times; but it does permit a joint and survivor annuity.²¹ Moreover, for the entire period the total of the annual amounts payable to the income interests shall not be less than 5 percent of the initial net fair market value of the property placed in trust.²²

2. Charitable Remainder Unitrust

A charitable remainder unitrust is a trust from which a fixed percentage (which is not less than 5 percent) of the net fair market value of its assets, *valued annually*, is to be paid, not less often than annually, to one or more persons, at least one of which is not an organization described in section 170(c). Following the termination of the above-stated payment (which is the only amount which may be paid to a non-charitable party), the remainder interest of the trust is to be transferred to, or for the use of, an organization described in section 170(c), or is to be retained by the trust for such a use.²³

Example: A places securities in trust specifying that his son is to receive annual payments equal to 6 percent of the net fair market value of the trust determined annually for life, remainder to his church.

¹⁸ Thus, no deduction will be allowed for any form of contingent remainder interest to charity. A similar rule restricts the formation of a charitable remainder unitrust. See Int. Rev. Code of 1954, § 664(d)(2)(B). The purpose of these provisions is to eliminate the uncertainty in valuation caused by contingent-type charitable gifts under prior law.

¹⁹ Int. Rev. Code of 1954, § 664(d)(1).

²⁰ Proposed Treas. Reg. § 1.664-2(a)(1), 35 Fed. Reg. 12469 (1970).

²¹ Id. § 1.664-3(a)(5), 35 Fed. Reg. 12471 (1970).

²² Id. § 1.664-2(a)(2), 35 Fed. Reg. 12469 (1970). Also relief is provided in the case where a grantor, including a testator, of a trust underestimates in good faith the initial fair market value of the property irrevocably placed in the annuity trust, provided that the grantor, or executor, consents to accept such estimated value for purposes of determining the appropriate charitable contributions deduction.

²³ Int. Rev. Code of 1954, § 664(d)(2).

The proposed regulations define the net fair market value of the trust assets to include all accrued assets and accrued liabilities. A percentage is "fixed" if the percentage is the same as to each recipient, or as to the total percentage payable during the payout period.²⁴ The fixed percentage with respect to all beneficiaries taken together may not be less than 5 percent for the entire period.²⁵

The minimum 5 percent payout requirement applicable to both the unitrust and annuity trust was added by Congress to prevent the use of the charitable remainder trust to circumvent the current income distribution requirement imposed on private foundations.²⁶ In the absence of these rules, it would be possible to establish a charitable remainder trust providing for a minimal payout to the non-charitable income beneficiary (substantially less than the amount of trust income), which would allow it to accumulate trust income in excess of the payout requirement of the unitrust and annuity trust without tax for the future benefit of charity.²⁷

3. *Exception to Strict Unitrust Payout Rule*

A qualified charitable remainder unitrust can provide for the distribution each year of either the 5 percent of the net fair market value of its assets (valued annually), or the amount of the trust income (as defined under section 643(b)), whichever is lower.²⁸ *No comparable rules are provided for annuity trusts.*²⁹ This payment requirement may not be discretionary with the trustee. In addition, deficiencies in income, that is, where the trust income was less than the stated amount payable to the income beneficiary, could be made up in later years when the trust income exceeds the amount otherwise payable to the income beneficiary for that year.³⁰ The Treasury has construed the second part of the exception to the regular unitrust payout format as optional; consequently the proposed regulation provides that the trust can distribute under the first part of the exception alone or under both parts.³¹ Allowing a charitable remainder unitrust to distribute to the income beneficiary the lesser of the trust income or the stated payout

²⁴ Proposed Treas. Reg. § 1.664-3(a)(1)(ii), 35 Fed. Reg. 12470 (1970).

²⁵ Id. § 1.664-3(a)(2), 35 Fed. Reg. 12471 (1970).

²⁶ Int. Rev. Code of 1954, § 4942(e).

²⁷ S. Rep. No. 91-552, 91st Cong., 1st Sess. 90 (1969).

²⁸ Int. Rev. Code of 1954, § 664(d)(3)(A).

²⁹ In the Senate version of what became Int. Rev. Code, § 664, the alternative payout rule extended to the annuity trust as well as the unitrust. See S. Rep. No. 91-552, 91st Cong., 1st Sess. 89 (1969). The Conference Committee limited the application of the rule to the unitrust. See H.R. Rep. No. 91-782, 91st Cong., 1st Sess. (1969).

³⁰ Int. Rev. Code of 1954, § 664(d)(3)(B); Proposed Treas. Reg. § 1.664-3(a)(1)(ii), 35 Fed. Reg. 12470 (1970).

³¹ Proposed Treas. Reg. § 1.664-3(a)(1)(ii), 35 Fed. Reg. 12470 (1970).

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will prevent a trust from having to invade its corpus when the income for a year is below that originally contemplated.

B. Taxation of the Charitable Remainder Trust

The charitable remainder trust is exempt from income taxes for each year in which it has no unrelated business taxable income.⁸² The exemption is to be determined on a year-by-year basis, and includes all taxes imposed by subtitle A of the Code. Loss of the exemption caused by having unrelated business taxable income subjects all of the trust income to taxation, not just the unrelated business taxable income.⁸³

The taxes imposed upon a non-exempt trust are computed under the rules prescribed by subchapter J of the Code for a complex trust, except that the taxation of distributions to recipients is to be determined under the characterization rules of Section 665(b) of the Code. The proposed regulation takes a penalty approach by providing no credit to the recipient for taxes paid by the trust. It also provides that subpart E of subchapter J does not apply to a non-exempt trust.⁸⁴

In order for a charitable remainder trust to maintain a tax-exempt status it must be either an annuity trust in every respect, or a unitrust in every respect, but not a combination of the two.⁸⁵ This rule reflects the Treasury's policy decision that a grantor should not be allowed to reserve an interest of the greater (or lesser) of a sum certain or a fixed percentage of the trust assets because of the actuarial difficulty in measuring the remainder interest.⁸⁶ The trust must also meet the definition of, and function exclusively as, a charitable remainder trust from its creation.⁸⁷ This rule is designed to prevent the creation of a trust which technically meets the definition of a charitable remainder trust, from acting as a vehicle for other purposes, and deducting expenses relating to such other purposes from income (i.e., a pour-over trust which is used as a vehicle to administer an

⁸² Int. Rev. Code of 1954, § 664(c).

⁸³ Proposed Treas. Reg. § 1.664-1(c), 35 Fed. Reg. 12468 (1970).

⁸⁴ Id. § 1.664-1(c), 35 Fed. Reg. 12468 (1970).

⁸⁵ Id. § 1.664-1(a)(2), 35 Fed. Reg. 12467-2468 (1970).

⁸⁶ Id.

For example, a trust which provides for the payment each year to a noncharitable beneficiary of the greater of the sum certain or a fixed percentage of the value of the trust assets is not exempt inasmuch as the trust is neither a charitable remainder annuity trust (for the reason that the payment for the year may be a fixed percentage of the value of the trust assets which is not a "sum certain") nor a charitable remainder unitrust (for the reason that the payment for the year may be a sum certain which is not a "fixed percentage" of the trust assets).

⁸⁷ Proposed Treas. Reg. § 1.664-1(a)(3), 35 Fed. Reg. 12468 (1970).

estate).³⁸ Also, for this purpose, a charitable remainder trust will be deemed to be created at the earliest time that the grantor or any other person is not treated as the owner of such trust, or any portion thereof, under the "grantor-trust" rules of subpart E (part 1 of subchapter J).³⁹

Example: In 1971, *H* creates a revocable trust which is to pay *W* 5 percent of the value of the trust assets, valued annually, for her life, remainder to charity. The trust is not a charitable remainder trust since it is revocable. In 1975, *H* predeceases *W* at which time the trust becomes irrevocable. At *H*'s death, the trust becomes a charitable remainder trust, if all of the other requirements of a charitable remainder trust are met.⁴⁰

It is important to note that certain of the new private foundation rules are applicable to charitable remainder trusts.⁴¹

C. Common Features of the Annuity Trust and Unitrust

1. Permissible Recipients

With regard to both the annuity trust and the unitrust, the statute requires an annual payment to one or more persons, at least one of which is not an organization described in section 170(c).⁴² The proposed regulations require that the person or persons be named, but may include members of a named class.⁴³ If the non-charitable recipient is an individual or individuals, all such individuals must be living at the time of the creation of the trust to prevent excessive delay before the charity will receive the corpus.⁴⁴

2. "Grantor-Trust" Limitation

The regulations specifically provide that no person may have the power to alter the amount to be paid to any named person if such power would cause the trust to be a subpart E trust.⁴⁵ This provision

³⁸ Id. § 1.664-1(a)(3), Example (2), 35 Fed. Reg. 12468 (1970).

³⁹ See note 45 infra.

⁴⁰ Proposed Treas. Reg. § 1.664-1(a)(3), Example (1), 35 Fed. Reg. 12468 (1970).

⁴¹ Int. Rev. Code of 1954, § 4947(a)(2); Proposed Treas. Reg. § 1.664-1(b), 35 Fed. Reg. 12468 (1970).

⁴² Int. Rev. Code of 1954, § 664(d)(1)(A), (d)(2)(A).

⁴³ Proposed Treas. Reg. §§ 1.664-2(a)(3), 1.664-3(a)(3), 35 Fed. Reg. 12470 (1970).

⁴⁴ Int. Rev. Code of 1954, § 664(d)(1)(A), (d)(2)(A); Proposed Treas. Reg. §§ 1.664-2(a)(3), 1.664-3(a)(3), 35 Fed. Reg. 12471 (1970).

⁴⁵ Proposed Treas. Reg. §§ 1.664-2(a)(3), 1.664-3(a)(3), 35 Fed. Reg. 12470-12471 (1970). Subpart E (§ 671 and following), part 1, subchapter J, chapter 1 of the 1954 Code codifies, with modifications, the Regulations under the 1939 Code which were based on the Supreme Court decision, *Helvering v. Clifford*, 309 U.S. 331 (1940). Subpart E contains provisions taxing income of a trust to the grantor or another person

appears unnecessary since the proposed regulations already provided that a charitable remainder trust will not be deemed created until such time that subpart E does not apply.⁴⁶

It is important to note that traditionally, trusts have been created for the life of the husband, with the wife being designated as a survivor beneficiary; the husband, however, retains the right to revoke his wife's right to receive life income by delivering to the trustee an instrument stating that the income payments are to cease on his death (and not the death of the survivor), and that the principal is to be delivered to the charity on the husband's death. Even though the husband reserves the right to accelerate the charitable remainder, the charitable deduction is based upon the assumption that the husband will not revoke his wife's right to receive income payments if she survives. Under the proposed regulations,⁴⁷ however, the husband would be prohibited in the above case from retaining a right to revoke the survivor's interest during his lifetime even though it would result in the charitable remainderman receiving its interest earlier in many cases.

3. *Payment Period*

The payment period shall be either the life or lives of a named individual or individuals, or for a term of years not to exceed 20 years.⁴⁸ Only an individual or a charitable organization may receive an amount for the life of an individual. If an individual receives an amount for life it must be for only *his* life. The length of the term of years is required to be ascertainable with certainty at the time of the creation of the trust, except that the term may be terminated by the death of the recipient. This latter rule is necessary for accurate actuarial computation. The persons can receive their interests concurrently or successively. As previously stated, the proposed regulations require that the

under certain circumstances where such party retains control over the trust's corpus or income. These circumstances are in general as follows:

1. If the grantor has retained a reversionary interest in the trust, within specified time limits (Int. Rev. Code of 1954, § 673);
2. If the grantor or a non-adverse party has certain powers over the beneficial interests under the trust (Int. Rev. Code of 1954, § 674);
3. If certain administrative powers over the trust exist under which the grantor can or does benefit (Int. Rev. Code of 1954, § 675);
4. If the grantor or a non-adverse party has a power to revoke the trust or return the corpus to the grantor (Int. Rev. Code of 1954, § 676); or
5. If the grantor or a non-adverse party has the power to distribute income to or for the benefit of the grantor (Int. Rev. Code of 1954, § 677).

Under Int. Rev. Code of 1954, § 678, income of a trust is taxed to a person other than the grantor to the extent that he has the sole power to vest corpus or income in himself.

⁴⁶ Proposed Treas. Reg. § 1.664-1(a)(3), 35 Fed. Reg. 12468 (1970).

⁴⁷ Id. § 1.664-2(a)(3), 35 Fed. Reg. 12470 (1970) for the annuity trust; Proposed Treas. Reg. 1.664-3(a)(3), 35 Fed. Reg. 12471 (1970) for the unitrust.

⁴⁸ Int. Rev. Code of 1954, § 664(d)(1)(A), (d)(2)(A).

5 percent requirement must be met until the termination of all of the annual payments. For example, the following provisions would satisfy the above rules:

- (1) an amount to *A* and *B* for their joint lives and then to the survivor;
- (2) an amount to *A* for life or for a term of years, whichever is longer (or shorter), if the length of the term of years is not longer than 20 years;
- (3) an amount to *A* for a term of years not longer than 20 years and then to *B* for life;
- (4) an amount to *A* for his life and an amount to *B* for his life if the amount given to each individual is not less than 5 percent of the initial net fair market value in the case of an annuity trust (or if the percentage given to each individual in a unitrust, is not less than 5 percent).⁴⁹

It is important to note that the proposed regulations would deny a charitable deduction in the case where joint parties, such as husband and wife, provide for the survivor to receive only one-half of the income, with the remaining half of the trust corpus to be paid outright to the charity on the death of the first to die.⁵⁰ The deduction would also be denied where a parent creates a charitable trust for two or more children, providing that on a child's death, the charity would receive a portion of the corpus which generated income for that child, instead of increasing the income of the surviving child or children. The practitioner can achieve the desired result by severing the property at the outset and creating two one-life trusts. However, it is often difficult and expensive to sever the property, and it is almost always more expensive to administer two trusts rather than one.

It would appear reasonable for the Treasury to allow the governing instrument to provide that a designated percentage of the trust corpus be delivered to the charitable remainderman on the death of the first beneficiary. This would benefit charitable organizations who

⁴⁹ Proposed Treas. Reg. §§ 1.664-2(a)(5), 1.664-3(a)(5), 35 Fed. Reg. 12470-2471 (1970).

⁵⁰ Proposed Treas. Reg., § 1.664-2(a)(2), 35 Fed. Reg. 12469 (1970) provides: Except as provided in paragraph (e) of § 1.664-1 (relating to short taxable years), for the entire period described in paragraph (5) of this paragraph, the total amounts payable under subparagraph (1) of this paragraph shall not be less than 5 percent of the initial net fair market value of the property placed irrevocably in trust as finally determined for federal tax purposes. (Emphasis added.)

Proposed Treas. Reg. § 1.664-3(a)(2), 35 Fed. Reg. 12471 (1970) provides: "The fixed percentage described as subparagraphs (1)(i) of this paragraph with respect to all beneficiaries taken together shall be not less than 5 percent for the entire period specified in paragraph (5) of this paragraph." (Emphasis added.)

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would receive their remainder interest earlier in many cases. The 5 percent test for the unitrust would be met if the payments to the survivor are determined by multiplying the stated percentage (set when the trust is initially created) by the net fair market value of the unitrust assets, determined annually, after deducting the designated percentage of the trust assets which were delivered to the charity on the death of the first to die. The 5 percent test for the annuity trust would be met where the stated dollar amount is reduced by the same percentage as the percentage of the corpus paid to the charity on the death of the first to die.

4. *Special Exceptions*

An amount shall not be treated as paid to or for the use of any person other than an organization described in section 170(c) if the amount is transferred for full and adequate consideration, for example, trustees' fees. A trust can pay off encumbrances upon the property placed in trust.⁵¹ Such payment is not treated as payment to or for the use of a non-charitable party. The transfer to the trust of property which is subject to an encumbrance is viewed as a net gift. However, the prohibition against "self-dealing" would prohibit such transfers where the charitable trust assumes or takes subject to a mortgage which was placed on the property by the donor within the preceding ten-year period.⁵² This latter rule, which generally applies to a private foundation's activities, prohibits certain acts between the charitable organization and its donor or related parties—termed "disqualified persons"—and provides for a progressive series of sanctions against the violating parties.

For these purposes, the contribution of property by a disqualified person to the charitable entity is a prohibited sale or exchange if the charitable entity assumes a mortgage on the property, or takes subject to a mortgage placed on the property by a disqualified person within the ten-year period ending on the date of the transfer.⁵³ The trust may not be subject to a power to invade, alter, amend or revoke for the beneficial use of a person other than a charitable organization, and the governing instrument may provide that specified amounts shall be paid (or may be paid in the discretion of the trustee) to an organization described in section 170(c).⁵⁴

⁵¹ Proposed Treas. Reg. §§ 1.664-2(a)(4), 1.664-3(a)(4), 35 Fed. Reg. 12470-2471 (1970).

⁵² See Int. Rev. Code of 1954, §§ 4947(a)(2), 4941(d)(1)(A), 4941(d)(2)(A).

⁵³ Int. Rev. Code of 1954, § 4941(d)(2)(A).

⁵⁴ Proposed Treas. Reg. §§ 1.664-2(a)(4), 1.664-3(a)(4), 35 Fed. Reg. 12470-2471 (1970).

5. *Permissible Remaindermen*

The statute requires that the trust corpus "be transferred to, or for the use of, an organization described in section 170(c) or [that it] be retained by the trust for such a use."⁵⁵ The Treasury construes this rule to permit part of the corpus to be retained and part to be transferred. If the corpus is retained for a charitable use, the taxable year of the trust will end and the trust will be treated as a private foundation pursuant to section 4947(a)(1). Consequently, the trust will normally have a short taxable year as its last taxable year. The proposed regulations allow more than one charitable organization to be the remainderman, and such interests may be enjoyed either concurrently or successively.⁵⁶

It is important to note that the governing instrument must provide that if at the time any trust property is to be transferred to or for the use of a remainderman, such remainderman is not an organization described in section 170(c), the property must be transferred to or for the use of an organization or organizations which are described in section 170(c), or be retained for such use. Apparently, the charitable remainderman does not have to be named at the creation of the trust, but need only be designated by any party (including the grantor) prior to ultimate distribution of the corpus.⁵⁷ The purpose of these rules is to insure that the corpus which gave rise to the charitable deduction actually inures to the benefit of a charitable organization.

D. *Annual Unitrust Valuation Date*

A unitrust must distribute annually a "fixed percentage (which is not less than 5 percent) of the net fair market value of its assets *valued annually*" to the income beneficiary or beneficiaries. (Emphasis added.)⁵⁸ While the statute requires annual valuation it does not specify on what date the assets are to be valued. In the proposed regulations, the Treasury provides that the valuation can be made at *any* one date during the taxable year of the trust, or by taking an average of valuations made on more than one date, so long as the same valuation date or dates and method are used each year. The amount which must be paid each year shall be based upon the valuation for such year.⁵⁹ This rule prevents the trust from skipping a distribution in the first year.⁶⁰

⁵⁵ Int. Rev. Code of 1954, § 664 (d)(1)(C), (d)(2)(C).

⁵⁶ Proposed Treas. Reg. §§ 1.664-2(a)(6), 1.664-3(a)(6), 35 Fed. Reg. 12470-2471 (1970).

⁵⁷ Id.

⁵⁸ Int. Rev. Code of 1954, § 664(d)(2)(A).

⁵⁹ Proposed Treas. Reg. § 1.664-3(a)(1)(ii)(b), 35 Fed. Reg. 12470 (1970).

⁶⁰ Id.

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If the unitrust payout is valued at the beginning of the taxable year, the payout to the non-charitable income beneficiary will, in most cases, be less than if it is valued at the end of the year, leaving a greater amount of property available for the charitable remainderman. This is so because the income and appreciation will not enter the payout formula until the first day of the following year. It may also be advantageous from an administrative standpoint since the payout amount would be fixed on the first day of the taxable year (with the exception of additional transfers made during the year), thereby allowing the trust twelve months to satisfy the payout formula.

On the other hand, if an "end of the year" valuation date were selected, the payout would include a percentage of the income and unrealized appreciation relating to that year. A payment will be considered made on the last date of a taxable year of a trust if the payment is made within 2½ months after the close of the taxable year, or within such longer period as is shown to the satisfaction of the Commissioner or his delegate to be reasonable.⁶¹ Of course, the grantor may select any other date on which the assets of the trust could be more easily valued. For example, if an asset held by the trust was stock of a closely-held corporation, the grantor could select a valuation date which coincided with the end of the financial year of the corporation. However, any time the valuation date is subsequent to the first day of the year, income will have to be added to the asset value at the beginning of the taxable year before the fixed percentage may be applied.⁶²

E. *Future Contributions*

Future contributions may be made to a unitrust⁶³ but not to an annuity trust.⁶⁴ The apparent reason for the Treasury's disallowance of future contributions in the case of an annuity trust is its concern that such a rule might provide the donor with a means of funding an increased annuity out of prior contributions, or funding a prior "sum certain" amount with new contributions. It is suggested that the future contributions to annuity trusts should be allowed, provided that a formula clause is included in the governing instrument which requires the amount of the increase in the annuity to be the same percentage of the fair market value of the contributed property that

⁶¹ *Id.*

⁶² Proposed Treas. Reg. § 1.664-1(e)(ii), 35 Fed. Reg. 12469 (1970), requires the governing instrument to provide that in the case of a charitable remainder unitrust with a short taxable year in which no valuation date occurs before the end of the taxable year of trust, the trust assets shall be valued on the last day of the taxable year of the trust.

⁶³ *Id.* § 1.664-3(a)(1)(ii)(b), 35 Fed. Reg. 12470 (1970).

⁶⁴ *Id.* § 1.664-2(b), 35 Fed. Reg. 12470 (1970).

the amount of the original annuity bears to the fair market value of all of the trust assets at the date of the contribution (with the further proviso that such percentage under the formula must exceed 5 percent at the time of the new contribution).

In the case of additional contributions to the unitrust, the proposed regulations require that the governing instrument provide that such contributions be valued on the contribution date if there is no regular valuation after the contribution date, and that a pro-rata portion of the required payout be paid with respect to such contributions.⁶⁵

F. Calculation of a Charitable Remainder Interest

In view of new unitrust and annuity concepts, the charitable remainder interest is to be computed on the basis of the actual relative interests of the income and charitable remainder beneficiaries in the trust property. Although, under prior law, the remainder interest was computed by assuming that the income beneficiary would receive $3\frac{1}{2}$ percent each year (the $3\frac{1}{2}$ percent rate was also used to determine the present value of the charitable remainder interest), the proposed regulations prescribe new tables reflecting the use of a 6 percent discount rate and new lives⁶⁶ (separate tables for male and female annuitants) which are to be retroactively applied to July 31, 1969.⁶⁷

In the charitable remainder annuity trust case, the computation should be made by first valuing the present value of the income interest (either based upon life expectancy or term of years) using a 6 percent discount rate. (The present value of an annuity is computed under Section 20.2031-10 of the Estate Tax Regulations.) This amount (present value of the income interest) would then be subtracted from the fair market value of the property transferred to determine the value of the charitable remainder for tax deduction purposes.

In the case of the charitable remainder unitrust, basis tables are provided in the proposed regulations for the computation of the deductible interest.⁶⁸ The proposed regulations also provide that if the governing instrument does not prescribe when the distribution shall be made during the taxable year of the unitrust, the computation of present value shall be made on the assumption that the

⁶⁵ Id. § 1.664-3(b), 35 Fed. Reg. 12471 (1970).

⁶⁶ The new tables use as their basis for mortality assumptions, actuarial data supplied by the United States Life Tables: 1959-61, published by the U.S. Department of Health, Education and Welfare, Public Health Service, as compared to the old tables which were based upon information gained in the 1939-1941 census.

⁶⁷ Proposed Treas. Reg. §§ 1.664-2(c), 31 Fed. Reg. 12470 (1970), 1.664-4(a), 35 Fed. Reg. 12471 (1970).

⁶⁸ Id. § 1.664-4(b)(5), 35 Fed. Reg. 12471 (1970).

distribution is made on the first day of the taxable year of the trust.⁶⁹ Because of the large number of possible combinations of valuation dates and payout sequences, the proposed regulations provide for the Commissioner to supply the factor upon request, if conditions permit, and the factor is not provided for in the regulations. The request must be accompanied by a full statement of the relevant information. If the Commissioner furnishes the factor, a copy of the letter supplying the factor shall be attached to the tax return. If the Commissioner does not furnish the factor, the taxpayer must furnish a factor computed in accordance with the actuarial assumptions set forth in proposed regulations, section 1.664-(a)(1), that is, a 6 percent discount factor and new mortality tables.⁷⁰ Any claim for deduction for the value of a remainder interest in a charitable remainder unitrust or annuity trust must be supported by a full statement attached to the return showing the computation of the present value of such interest.⁷¹

*G. Character of Distributions to
Non-Charitable Income Beneficiary*

Section 664(b) of the Code and proposed regulations, section 1.664-1(d)(1) specify how income is to be taxed to the beneficiary of the unitrust or annuity trust. The income retains the character it had in the trust.⁷² Each payment is treated as follows:

First, ordinary income to the extent of the trust's ordinary income for the year and any undistributed ordinary income for prior years;

Second, as short-term capital gain to the extent of the sum of the trust's net short-term capital gain for the taxable year and its undistributed net short-term capital gains for prior years (determined on a cumulative net basis);

Third, as long-term capital gain to the extent of the trust's long-term capital gain for the year and undistributed net long-term capital gains for prior years (determined on a cumulative net basis);

Fourth, as "other" (e.g., tax-exempt) income to the extent of the

⁶⁹ Id. § 1.664-4(a)(1), 35 Fed. Reg. 12471 (1970).

⁷⁰ Id. § 1.664-4(a)(3), 35 Fed. Reg. 12471 (1970).

⁷¹ Id. §§ 1.664-2(c), 1.664-4(a)(4), 35 Fed. Reg. 12470 (1970).

⁷² Expenses that are reasonably related to one or more classes of items or corpus shall be so allocated to the category. Indirect expenses will be allocated upon the basis of the net income for such taxable year of the various classes of items of income. All federal income taxes and all Chapter 42 taxes shall be allocated to corpus. Id. § 1.664-1(d)(2), 35 Fed. Reg. 12468 (1970). If there are two or more recipients, each will be treated as receiving his pro-rata portion of categories of income and corpus. Id. § 1.664-1(d)(3), 35 Fed. Reg. 12468 (1970).

trust's "other" income for the year, and any undistributed "other" income for prior years;

Fifth, as a tax-free distribution of principal.

A loss in one of the above categories may not be used to reduce a gain in any other category.

An example of how the income beneficiary is to treat distributions is as follows:

Year 1. After multiplying the stated percentage by the net fair market value of the unitrust, it is determined that the beneficiary is to receive \$5,000 for Year 1. During the year the trust:

Received: \$1,000 in interest (taxable)

\$1,000 in dividends;

Sold: a block of stock for \$4,000 which had a \$3,000 cost-basis (short-term);

Sold: another block of stock for \$9,000 which had a \$9,000 cost-basis (long-term);

Received: \$1,000 in interest from tax-free municipal bonds.

On the \$5,000 the beneficiary receives for the year, he is taxed as follows:

1. \$2,000 is ordinary income;
2. \$1,000 is short-term capital gain income;
3. \$1,000 is tax-free interest;
4. \$1,000 is non-taxable return of principal.

Year 2. After multiplying the stated percentage by the net fair market value of the unitrust, it is determined that the beneficiary is to receive \$6,000 for Year 2.

During the year the trust:

Received: \$7,500 in dividends;

Sold: a block of stock for \$10,000 which had a \$6,000 cost-basis (long-term);

Sold: a block of stock for \$5,000 which had an \$8,000 cost-basis (long-term).

The entire \$6,000 received by the beneficiary is taxed as ordinary income.

Year 3. After multiplying the stated percentage by the net fair market value of the unitrust, it is determined that the beneficiary is to receive \$5,500 for Year 3.

During the year the trust:

Received: \$2,000 in interest (taxable);

Received: \$1,000 in interest from tax-free municipal bonds;

Sold: a block of stock for \$5,000 which had a \$5,000 cost-basis (long-term).

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On the \$5,500 the beneficiary receives, he is taxed as follows:

1. \$3,500 is ordinary income (\$2,000 in interest received by the trust in Year 3 plus \$1,500 of dividends undistributed in Year 2);
2. \$1,000 is long-term capital gain income (undistributed in Year 2);
3. \$1,000 is tax-free interest.

H. Year of Inclusion

The recipient shall include in his gross income those amounts which are paid, credited, or required to be distributed in the taxable year or years of the trust ending within or with his taxable year.⁷³

I. Distributions in Kind

In the case of a distribution made in property other than cash, the fair market value of the property paid, credited, or required to be distributed shall be considered as an amount realized by the trust from the sale or other disposition of property. The basis of the property in the hands of the recipient is its fair market value at the time it was paid, credited, or required to be distributed.⁷⁴

Example: On January 1, 1971, X created a charitable remainder annuity trust under which X is to receive \$5,000 per year. During 1971, the trust earns \$500 of ordinary income. On December 31, 1971, the trust distributed cash of \$500 and property having a fair market value of \$4,500 and a basis of \$2,200. The trust is deemed to have realized a capital gain of \$2,300. X shall treat the distribution of \$5,000 as being ordinary income of \$500, capital gain of \$2,300 and trust corpus of \$2,200. The basis of the property is the \$4,500 in the hands of X.

J. Special Income Termination Rule

The proposed regulations specifically authorize that the governing instrument may provide that the regular periodical payment may terminate on the payment date next preceding the income beneficiary's death. This eliminates the necessity of allocating part of the last payment between the parties. The fact that the recipient does not receive such last payment shall not be taken into account for purposes of determining the present value of the remainder interest.⁷⁵

⁷³ Id. § 1.664-1(d)(4), 35 Fed. Reg. 12469 (1970). See also Int. Rev. Code of 1954, § 662(c).

⁷⁴ Proposed Treas. Reg. § 1.664-1(d)(5), 35 Fed. Reg. 12469 (1970).

⁷⁵ Id. § 1.664-1(e), 35 Fed. Reg. 12469 (1970).

K. Pooled Income Fund—Section 642(c)(5) of the Code

The new rules provide that a charitable tax deduction for income, gift, or estate tax purposes will not be allowed for a charitable remainder interest unless the trust is either in the annuity or unitrust form. However, a further exception was made for a pooled income arrangement⁷⁶ subject to appropriate limitations contained in section 642(c)(5).

A pooled income fund is very much like a charitable remainder trust with reserved income for life. The main difference is that the donor's irrevocable gift is commingled with similar contributions in a fund maintained by the organization to which the remainder interest is contributed. There is no requirement in the Code as to the number of contributors necessary to form a pooled fund. It is conceivable that two or more individuals could easily convince a local publicly supported organization to join in the formation of such a fund. The individuals would receive a charitable deduction for the gift of the irrevocable remainder interest to charity notwithstanding the fact that the instrument did not comply with the unitrust and annuity rules. It is important to note that these pool arrangements can still receive the set-aside deduction to the extent that they accumulate capital gains for charity.⁷⁷

A pooled arrangement shall not be treated as an association taxable as a corporation within the meaning of section 7701(a)(3); nor will the provisions of subpart E ("grantor-trust") apply to such an arrangement.⁷⁸ Moreover, no gain or loss shall be recognized to the donor on a transfer of property to a pooled income fund, to the extent that the donor retains for himself, or creates for the benefit of another, a life income interest in the property transferred. The fund's basis and holding period shall be determined as provided in sections 1015(b) and 1223(2).⁷⁹

In order for the pooled fund to qualify for special treatment under the new law⁸⁰ it must meet the strict rules contained in section 642(c)(5), which are as follows:

(1) The donor must contribute an "irrevocable remainder inter-

⁷⁶ Int. Rev. Code of 1954, §§ 170(f)(2)(A), 2055(e)(2)(A), 2522(c)(2)(A).

⁷⁷ Int. Rev. Code of 1954, § 642(c)(3). The fact that short-term gains will be taxed to the pooled fund must be considered by the trustee in making investment decisions.

⁷⁸ Proposed Treas. Reg. § 1.642(c)-5(a)(2), (a)(3), 35 Fed. Reg. 11476 (1970).

⁷⁹ Id. § 1.642(c)-5(a)(3), 35 Fed. Reg. 11476 (1970).

⁸⁰ Proposed Treas. Reg. § 1.642(c)-7 provides transitional rules for pooled income funds which do not meet all the requirements of the Tax Reform Act of 1969, but which possess certain initial characteristics, and are amended before January 1, 1971 to meet the new rules. (A special rule is provided regarding judicial proceedings to amend the governing instrument in Proposed Treas. Reg. § 1.642(c)-7(c)(1), 35 Fed. Reg. 11485 (1970)).

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est in such property to or for the use of" the charity.⁸¹ The income beneficiary shall receive income "determined by the rate of return earned by the trust" for each year.⁸² Accordingly, the proposed regulations preclude a deduction for contribution of a contingent remainder interest to the charity, even though based upon an ascertainable standard with the possibility of invasion so remote as to be negligible.⁸³

(2) The recipient charity must qualify as a "publicly supported organization," such as a church, educational organization, certain hospitals, and medical research organizations, and organizations which normally receive a substantial part of their support from the public, or a governmental unit.⁸⁴ The governing instrument may provide that, in the event such organization is not a public charity when the remainder interest is to be transferred to or for the use of such organization, such amount shall be transferred to or for the use of an organization which is a public charity.⁸⁵ Private operating foundations, community foundations and private foundations which pass-through all contributions within a specified period do not qualify for the special tax treatment granted to "pooled income" funds.

(3) Each donor must retain for himself for life an income interest in the property transferred to such fund, or create an income interest in such property for the life of one or more named beneficiaries, each of whom must be living at the time of the transfer of property to the fund by the donor. Thus, the donor may provide an income interest not only for himself but for one or more named beneficiaries.⁸⁶ In the event that more than one beneficiary of the income interest is named, such beneficiaries may enjoy their share of income concurrently and/or consecutively. However, the governing instrument must specify at the time of the transfer the particular person or persons to whom the income is payable and the share of income distributable to each such person so specified.⁸⁷

(4) The property transferred by each donor shall be "commingled with property transferred by other donors who have made or

⁸¹ Int. Rev. Code of 1954, § 642(c)(5)(A).

⁸² Int. Rev. Code of 1954, § 642(c)(5)(F); Proposed Treas. Reg. § 1.642(c)-5(b)(7), 35 Fed. Reg. 11478 (1970).

⁸³ Treas. Reg. § 20.2055-2(a), (b).

⁸⁴ Int. Rev. Code of 1954, §§ 170(b)(1)(A)(i)-(vi), 664(c)(5)(A).

⁸⁵ Proposed Treas. Reg. § 1.642(c)-5(b)(i), 35 Fed. Reg. 11477 (1970).

⁸⁶ The donor need not retain or create a life interest in all of the income from the property transferred to the fund provided any income not payable under the terms of the governing instrument to an income beneficiary is contributed to, and within the taxable year in which it is received is paid to, the same organization to or for the use of which the remainder interest is contributed. *Id.* § 1.642(c)-5(b)(2), 35 Fed. Reg. 11477 (1970).

⁸⁷ *Id.*

make similar transfers."⁸⁸ The pooled income fund shall not be disqualified because any portion of its properties is invested or reinvested jointly with other properties not part of the pooled income fund, which are held by, or for the use of, the organization which maintains the fund, for example, securities in the general endowment fund of the organization.⁸⁹ Where such joint investment or reinvestment of properties occurs, detailed accounting records must be maintained specifically identifying the assets included in the pooled income fund and the income earned by, and attributable to such assets. Such a joint investment or reinvestment of properties shall not be treated as an association or partnership for purposes of the Code.⁹⁰

(5) The pooled fund may not have investments in securities which are exempt from tax.⁹¹ The governing instrument must contain specific prohibitions against accepting or investing in such securities.⁹²

(6) The fund must be maintained by the recipient charity and no donor or beneficiary of an income interest may be a trustee of the fund.⁹³ The requirement of maintenance will be satisfied where the charitable organization exercises control directly or indirectly over the fund. For example, this requirement of control shall ordinarily be met when the organization has the power to remove the trustee or trustees of the fund and designate a new trustee or trustees.⁹⁴ The Treasury has interpreted the language of the statute to allow a donor or beneficiary under ordinary circumstances to participate in the maintenance of the fund in the capacity of a trustee, officer, director or other official of the charitable organization, but not the fund.⁹⁵

L. Valuation of Remainder Interest in Property Transferred to a Pooled Income Fund

In order to prevent manipulation to overstate the appropriate charitable contribution deduction in cases of this type of gift, the language of section 642(c)(5) provides that the amount of the charitable contribution deduction allowed the donor upon the transfer of property to the pooled income fund is to be determined by valuing the income interest on the basis of the highest rate of return earned by the particular pooled income fund in any of the three taxable years preceding the taxable year of the fund in which the transfer occurs. Where a fund has not been in existence for this period of time, the

⁸⁸ Int. Rev. Code of 1954, § 642(c)(5)(B).

⁸⁹ Proposed Treas. Reg. § 1.642(c)-5(b)(1), 35 Fed. Reg. 11477 (1970).

⁹⁰ Id.

⁹¹ Int. Rev. Code of 1954, § 642(c)(5)(C).

⁹² Proposed Treas. Reg. § 1.642(c)-5(b)(2), 35 Fed. Reg. 11477 (1970).

⁹³ Int. Rev. Code of 1954, § 642(c)(5)(E).

⁹⁴ Proposed Treas. Reg. 1.642(c)-5(b)(5), 35 Fed. Reg. 11477 (1970).

⁹⁵ Id. § 1.642(c)-5(b)(6), 35 Fed. Reg. 11477 (1970).

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rate of return is to be assumed to be 6 percent, unless a different rate is prescribed by the Secretary of the Treasury or his delegate.⁹⁶

The value of the income interest is, in effect, a unitrust computation, based on an historical rate of return, discounted to present value at the historical rate based upon the new bi-sex mortality tables. This amount will then be subtracted from the total value of the property transferred to arrive at the charitable deduction. Any claim for deduction in any return for the value of a remainder interest in property transferred to a pooled income fund must be supported by a statement attached to the return showing the computation of the present value of such interest.⁹⁷

III. CONCLUSION

Under the rules of prior law, the amount of a charitable contribution deduction in the case of gifts of remainder interests in trust did not necessarily have any relation to the value of the benefit which the charity ultimately received. The Tax Reform Act of 1969 provides new rules wherein a deduction will not be allowed for a charitable gift of a remainder interest in trust where there is a non-charitable income beneficiary, unless the trust is in a specified "annuity" or "unitrust" form. This requirement will remove the incentive to favor the income beneficiary over the charitable remainder man by manipulating the trust's investment. In this way, it will provide a better means of assuring that the amount received by the charity will be in accord with the charitable deduction allowed to the donor upon creation of the trust. The charitable contribution deduction is also available for contributions to a pooled income fund, an arrangement which resembles a charitable remainder trust with reserved income for life. In the pooled fund, however, the donor's irrevocable gift must be commingled with similar gifts and be maintained by the charitable organization to which the remainder interest is contributed.

⁹⁶ See also S. Rep. No. 91-552, 91st Cong., 1st Sess. 88 (1969); Proposed Treas. Reg. § 1.642(c)-6(b)(2), 35 Fed. Reg. 11479 (1970).

⁹⁷ Proposed Treas. Reg. § 1.642(c)-6, 35 Fed. Reg. 11478 (1970).