

April 2021

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Recommended Citation

Hover T. Lentz, Drafting a Section 2503(c) Trust for a Minor, 38 Dicta 11 (1961).

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DRAFTING A SECTION 2503(c) TRUST FOR A MINOR**

BY HOVER T. LENTZ*

It is more blessed to give than to receive, and the more so, if the gift is blessed by the tax laws. Paradoxically, the very solicitude of the law in protecting minors and their property resulted in placing minors at a serious tax disadvantage insofar as the receipt of gifts was concerned. The Internal Revenue Code of 1954 has removed several of the curses which formerly plagued would-be donors and their counsel, and a favorable start has been made in fostering gifts to minors by the extension of a partial tax blessing to such gifts.

I. HISTORICAL AND CURRENT BACKGROUND ON THE FUTURE INTEREST PROBLEM

Before analyzing the new provisions of the 1954 Code relating to gifts to minors and attempting to draft a trust instrument qualifying for their benefits, it is necessary to examine the prior law, first, in order to appraise and interpret the new rules, and, second, because the new law merely extends and does not repeal the old, and therefore much of the old is still to be reckoned with today.

Since its inception in 1932, the Federal gift tax law has provided for the annual exclusion of certain amounts from the category of taxable gifts. Section 1003 (b) of the 1939 Code and Section 2503 (b) of the 1954 Code allow an annual exclusion from gift tax in the amount of \$3,000 for all gifts "other than gifts of future interests in property."

With the estate tax rates reaching as high as 77% and with income rates attaining a maximum of 91%, both in steep progression, the urge has been irresistible to reduce these tax burdens by gifts of property to those objects of the donor's bounty who have smaller estates and lower incomes. The objective becomes particularly attractive if the goal can be attained without incurring a gift tax. While the use of the \$30,000 lifetime specific exemption¹ available to every donor is important in avoiding gift tax, the full use of the annual exclusion greatly increases the benefits to be realized from gifts. Therefore, it is advisable, at least from the tax viewpoint, to make certain that a gift is not denominated a "future interest."

The problem is essentially one of definition. The meaning of the phrase "future interest" has gradually evolved through a long series of decisions, an unusual number of which have been rendered by the United States Supreme Court.

The Committee Reports under the Revenue Act of 1932 stated that the term meant "any interest or estate, whether vested or contingent, limited to commence in possession or enjoyment at a future

**This is a revision of an article by Mr. Lentz that appeared in the 1956 Major Tax Planning volume, sponsored by the University of Southern California, published by Mathew Bender & Co.

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¹ Int. Rev. Code of 1954, § 2521.

date." The reason for restricting the exclusion to transfers of present interests was said to be the "apprehended difficulty, in many instances, of determining the number of eventual donees and the values of their respective gifts."

In a leading case² the Supreme Court remarked:

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.

These various definitions, however, must be applied to specific factual situations. A veritable welter of cases has arisen, particularly when one considers that the question is relatively insignificant from a revenue standpoint. These cases dealing primarily with gifts in trust have resulted in an illogical pattern, much of which is still fully applicable under the 1954 Code.

It is the individual beneficiary, not the trustee, to whom the gift is made and the annual exclusion is applicable.³ Where the trustee was directed to accumulate the income and to distribute the accumulated income and the principal at a future time, the beneficiary's interest in both the income and the principal were deemed future and the exclusion was denied.⁴ Likewise, the exclusion was lost when the trustee was given discretion to use income or principal at any time for the benefit of the beneficiary.⁵

Where current distribution of income was mandatory and only the distribution of corpus was postponed to a later date, the courts valued the income interest separately and treated it as a "present" interest. The exclusion was allowed to the extent of the value of the income interest, even though the gift of the principal was deemed to be "future."⁶ The value of the income interest in such cases is determined by actuarial principles under tables provided in the Treasury Regulations.⁷

However, even in instances where all income was required to be distributed currently the exclusion was sometimes denied. Almost in vain, the donors sought for a magic formula for making a gift in trust, particularly for the benefit of minors, which would pass the "future interest" hurdle and at the same time avoid the donor's natural reluctance to vest full control of the property and the income in immature and inexperienced donees. One proposed solution to this dilemma, which for a brief time had some promise of success, was the inclusion in the trust instrument of a clause granting the minor beneficiary or his legally appointed guardian the absolute and unrestricted right to demand that the trustees pay over all accumulated income and corpus at any time and thereby terminate the trust in whole or in part. In the reported cases, not one legal guardian was actually appointed for a minor. This device

² *Fondren v. Commissioner*, 324 U.S. 18 (1945).

³ *Helvering v. Hutchings*, 312 U.S. 398 (1941).

⁴ *United States v. Peltzer*, 312 U.S. 399 (1941).

⁵ *Commissioner v. Disston*, 325 U.S. 422 (1945).

⁶ *Fisher v. Commissioner*, 132 F.2d 383 (9th Cir. 1942).

⁷ *Treas. Reg.* §20.2031-7.

generally met with failure and the Commissioner continued to deny the exclusion.⁸ Recently, the Commissioner allowed the annual exclusion under the 1939 Code where the trustee was required to use trust income for the support, education and benefit of the minor as though the trustee were holding as a guardian.⁹

The case law had reached such a discouraging state from a prospective donor's viewpoint that text writers direly predicted,¹⁰ and the Commissioner contended, albeit unsuccessfully,¹¹ that even an outright gift to a minor was a "future interest," since the minor could not be said to presently possess and enjoy a stock certificate or the title to a parcel of real estate.

The taxpayer's plight clearly needed some attention, and since resort to the courts had only produced further confusion, legislative action was the alternative.

II. PARTIAL SOLUTION PROVIDED BY CONGRESS

In response to this widespread confusion and dissatisfaction and the accompanying demands for clarifying legislation, Congress acted on two fronts. It adopted Section 2503(c) dealing specifically with gifts to minors, and it added some language to Section 2503(b) to eliminate the incongruous result of the Evans and Brody cases.¹²

Section 2503(c) provides that a gift in a prescribed form to a minor is excluded from the future interest limitation. Congress failed to come directly to grips with the basic "future interest" problem, and merely delineated a certain limited type of transfer as an exception to the general rule. The pertinent part of the statute states that:

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 . . . if the property and the 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).¹³

The statute was not intended to provide an exclusive method of making gifts of present interests to minors. Therefore, prior law will continue to govern transfers which do not comply with the strict requirements of Section 2503(c).¹⁴

⁸ Rev. Rul. 54-91, 1954-1 Cum. Bull. 207.

⁹ Rev. Rul. 59-78, I.R.B. 1959-10, p.44 following *United States v. Baker*, 236 F.2d 317 (4th Cir. 1956).

¹⁰ Fleming, *Gifts for the Benefit of Minors* 49 Mich. L. Rev. 529 (1951).

¹¹ John E. Daniels, 10 CCH Tax Ct. Mem. 147 (1952).

¹² *Evans v. Commissioner*, 198 F.2d 435 (3rd Cir. 1952); *Jenny Brady*, 19 T.C. 126 (1952).

¹³ See generally: Rabkin and Johnson, *Federal Income, Estate and Gift Taxation*, §51.11(4); Mertens, *Law of Federal Gift and Estate Taxation*, §§38.02, 38.03 and 38.20 (1959).

¹⁴ Treas. Reg. §25.2503-4(c) provides: "(c) A gift to a minor which does not satisfy the requirements of section 2503(c) may be either a present or a future interest under the general rules of §25.2503-3. Thus, for example, a transfer of property in trust with income required to be paid annually to a minor beneficiary and corpus to be distributed to him upon his attaining the age of 25 is a gift of a present interest with respect to the right to income but is a gift of a future interest with respect to the right of corpus."

It will be observed that the statute covers all types of gifts, whether outright or in trust, to a guardian or otherwise, and that in some respects the case law has been modified. For instance, it is no longer necessary that income be distributed currently, as was the case under the *Fondren*¹⁵ decision. However, there must be provisions for invasion of principal, the payment of income alone not being sufficient. In this respect the former rule, exemplified by the *Fisher*¹⁶ and *Sensenbrenner*¹⁷ cases has been rejected.

Regulations interpreting this loosely drafted statute were very slow in forthcoming. Proposed regulations were not published until January 3, 1957, and these were not finalized until November 14, 1958.

III. PROBLEMS

A necessary consideration in planning a proposed trust is the choice of a trustee. Since the corpus of a Section 2503(c) trust will, at least initially, be small, the use of a corporate trustee will generally not be practical. Of course, from the tax standpoint, a corporate trustee does not give rise to the many tax problems that present themselves if an individual trustee is named. There are no adverse income tax consequences if the donor is trustee. The only situation where a donor-trustee will be taxed on the trust income is when, and to the extent that, he actually applies trust income for maintenance of the beneficiary, whom he is legally obligated to support.¹⁸ The fact that the donor possesses the power as trustee to accumulate or distribute income does not result in taxing it to him.¹⁹ Nevertheless, the property will be included in his estate for estate tax purposes if the donor is the trustee. In order to qualify under Section 2503(c) the trustee must have full power to distribute all principal, and, therefore, to terminate the trust. Possession of such a power would sweep the corpus into the donor-trustee's gross estate under Section 2038(a)(1),²⁰ which taxes trusts with a retained power to terminate in the settlor. In common law states there are no tax dangers in naming the donor's wife as trustee, except that she may be taxed on the income actually used to support the minor child, if under state law, the wife has a legal obligation to support such child. In a community property state the wife should not be trustee because she would be considered as a donor. The selection of the minor beneficiary's adult brother or sister would present no tax problems.

Clearly, the trustees can possess the required discretion to expend the income and principal for the minor's benefit. Such discretion cannot be vested in someone in a non-fiduciary capacity, such as the minor himself, his parent, another relative, his guardian, or merely a friend.

An equally important consideration is the choice of property to be transferred to the trust. Often it will be desirable to transfer property which is currently non-income producing, such as closely

¹⁵ *Fondren v. Commissioner* 324 U.S. 18 (1945).

¹⁶ *Fisher v. Commissioner*, 132 383 (9th Cir. 1942).

¹⁷ *Sensenbrenner v. Commissioner*, 234 F.2d 883 (7th Cir. 1943).

¹⁸ Int. Rev. Code of 1954, §677(b).

¹⁹ Int. Rev. Code of 1954, §§674(b)(s), 674(b)(7) and 677.

²⁰ *Lober v. United States*, 346 U.S. 335 (1953).

held stock or land. This would appear to be permissible as long as the trustee is not directed by the terms of the trust to retain such property. Although urged to do so, the Treasury did not cover this point in the regulations. Previously the Service has issued favorable rulings to the effect that gifts to Section 2503(c) trusts of life insurance policies and subsequent cash gifts to pay premiums thereon qualify for the exclusion. Such rulings covered both policies on the trust beneficiary's life and policies on the life of the parent of the beneficiary. Recently the Service has decided to reconsider this position. The statute states that the trust property and the income therefrom "may be expended by, or for the benefit of" the trust beneficiary. The issue now troubling the Service appears to be whether a portion of the cash gifts attributable to the cost of pure insurance and not reflected in an increase in cash surrender value is an expenditure for the "benefit" of the beneficiary. It may be necessary to distinguish between situations in which the life insurance is on the life of the beneficiary's parent or on the beneficiary's life. In the former, it can be argued that the funds were expended for the benefit of the beneficiary, who is thereby protected against loss of his parent, while in the latter the benefit may be to the beneficiary's successors in interest or his heirs, rather than to the beneficiary himself.

What standards, if any, may be imposed upon the exercise of the trustee's discretion to distribute or accumulate income or to invade corpus? The statute merely states that the "property and the income therefrom may be expended by, or for the benefit of, the donee." There should be no limitations or fixed standards on the trustee's discretion. The proposed regulations would have allowed standards of "support, health or education" provided that the exercise of such discretionary authority by the trustee might not be exercised so as to deny the donee the right to the property or income in case of "need." This was changed in the final regulations to provide that a transfer will not fail to qualify under Section 2503(c) by reason of the fact that—

There is left to the discretion of a trustee the determination of the amounts, if any, of the income or property to be expended for the benefit of the minor and the purpose for which the expenditure is to be made, provided there are no substantial restrictions under the terms of the trust instrument on the exercise of such discretion.²¹

It is this failure to permit standards governing distribution that means it is not possible for the grantor to act as trustee without the trust being included in his gross estate under the *Lober* decision. It may be argued that a discretion to use income and principal for support of the minor inferentially relieves the father of his support obligations and, therefore, benefits the father as well as the minor. In such event the trust would not be solely for the minor's benefit, and the terms of Section 2503(c) would be violated. Further, if the father is trustee and in such capacity he has the power to use income and principal for his minor child's support, the father may be deemed to have a general power of appointment for estate tax purposes, since he can, by exercise of such power, discharge his obliga-

²¹ Treas. Reg. §25.2503-4(b)(1).

tion to support. The trust would therefore be includable in the father's gross estate under Section 2041.

The most serious drawback of a 2503(c) trust is the necessity of completely distributing the trust estate to the beneficiary at age 21. Many donors will refuse to make such a gift, preferring the loss of the exclusion to the vesting of substantial sums in the beneficiary at that age. Consequently, there has been considerable thought devoted to various methods of circumventing this requirement. The statute provides that the property "pass to the donee on his attaining the age of 21 years." Final regulations rather clearly state that a transfer will not be disqualified because "the donee, upon reaching age 21, has the right to extend the term of the trust."²² However, hopes that this would solve the problem were dashed almost immediately by recent rulings.²³ These rulings dealt with a trust providing that upon reaching 21 the donee could either compel immediate distribution of corpus or elect to extend the term of the trust, in which case he would receive 1/3 of the corpus at 25, 1/3 at 29 and 1/3 at 33. It was originally held that the above quoted regulation was designed to permit extension by the donee only upon such conditions as the donee may freely choose. Therefore, the trust did not qualify. In the later ruling the rationale was switched to the theory that the donee had not been given "the unequivocal and unconditional right to receive the property without any necessity for affirmative action on his part." While these rulings are difficult to

²² Treas. Reg. §25.2503-4(b)(2).

²³ Rev. Rul. 60-218, I.R.B. 1960-23, p.12 superseding Rev. Rul. 59-144, 1959-1 Cum. Bull. 249.

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square with the regulation, they clearly indicate the dangers of including provisions extending the term of the trust after the donee attains his majority.

What provisions should the trust contain with respect to the disposition of the trust estate upon the minor's death prior to reaching 21? The statute merely tells us that to the extent the income and principal are not expended during the minor's lifetime, they must be "payable to the estate of the donee or as he may appoint under a general power of appointment." A provision for the payment of all accumulated income and principal to the minor's estate is clearly sufficient. It is doubtful whether a direct transfer to the minor's heirs or legatees, without actual administration of the assets in the minor's probate estate, is permissible. While the statutory language left room to argue that the grant of a general power to appoint by will plus a gift over to third persons in default of a valid exercise of the power would satisfy Section 2503(c)(2)(B), it was generally felt that such a result would violate the congressional purpose to insure that no other person has an interest in the property. In most states a minor can make a valid will, and thereby exercise a testamentary power of appointment, if at all, only on reaching a specified age, such as eighteen. Where the donee is under such age, therefore, the takers in default will always receive the trust estate at the minor's death. It was therefore feared that, where local law prevented a minor from validly exercising a general power of appointment by deed or will, no gift over to a third person in default of exercise of the power could be provided. Indeed, the proposed regulations adopted this construction. Fortunately, the Treasury heeded the many protests and the final regulations now contain the following sentences:

However, if the minor is given a power of appointment exercisable during lifetime or is given a power of appointment exercisable by will, the fact that under the local law a minor is under a disability to exercise an *intervivos* power or to execute a will does not cause the transfer to fail to satisfy the conditions of section 2503(c). Further, a transfer does not fail to satisfy the conditions of section 2503(c) by reason of the mere fact that . . .

- (3) The governing instrument contains a disposition of the property or income not expended during the donee's minority to persons other than the donee's estate in the event of the default of appointment by the donee.²⁴

Therefore, it is possible (and of course desirable) to give the minor donee a general testamentary power of appointment and then make provisions for gifts over to third persons in default of its exercise. These regulations do not permit any restrictions of substance by the terms of the instrument on the exercise of the power but do permit formal restrictions, such as a requirement that the will must specifically refer to the power being exercised, that the will must be

²⁴ Treas. Reg. §25.2503-4(b). In the only decision to date construing §2503(c) the court denied its application because the trust provided that the corpus would pass to the donee's descendants or his brothers and sisters if he died prior to 21; the donee was not given any power of appointment. *Bonnie M. Heath*, 34 T.C. No.59.

executed after the power was granted, that the document exercising the power be filed with the trustee, etc.

There must be a separate trust for each donee. Several separate trusts can, of course, be created by one trust instrument.

IV. SUGGESTED PROVISIONS FOR SECTION 2503 (c) TRUST

These provisions are drafted for a father who plans to create a 2503 (c) trust from his separate property for the benefit of his minor daughter. He desires to name his wife as the trustee. It is believed that the Service will rule that the following provisions meet all requirements of Section 2503 (c) and the regulations thereunder.

A. Dispositive Provisions

Section 1. The trustee shall hold, manage, invest and reinvest said property and any additional property which shall be added by any person at any time in any manner to the trust herein created for the sole benefit of _____ (daughter of the settlor, born _____). The trustee may distribute to, or apply for the sole benefit of, _____, until she attains the age of twenty-one (21) years, so much of the trust income or principal, or both, at such time or times and in such amounts and manner as the trustee, in her sole discretion, shall determine. Any amount which the trustee shall determine not to use may be accumulated as income or may be added to the principal, as the trustee shall deem best.

Section 2. When _____ attains the age of twenty-one (21) years, this trust shall terminate, and the entire property then remaining in trust (both principal and accumulated and accrued income) shall be paid over and distributed to her, free and discharged of all trust.

Section 3. Should _____ die before attaining the age of twenty-one (21) years, this trust shall terminate on her death, and the entire property then remaining in trust (both principal and accumulated and accrued income) shall be paid over and distributed to such person or persons (including her estate or the creditors of her estate) in such amounts and proportions and for such estates and interests, and outright or upon such terms, trusts, conditions and limitations as _____ may direct by her last will and testament. Such general testamentary power of appointment shall be exercisable only by her will which meets the requirements of a will in the State of _____ under the laws of such state in force at the date her will is executed, which will is duly admitted to probate by a court of competent jurisdiction, and which will refers specifically to such power. So far as is possible, the laws of such state shall govern the validity of interests created by the exercise of such power of appointment.

Section 4. Should _____ die before attaining the age of twenty-one (21) years and without validly exercising the general testamentary power of appointment granted to her under Section 3 above, the trustee shall pay over and distribute the entire property then remaining in trust (both principal and accumulated and accrued income):

(a) In equal shares free and discharged of all trust to the settlor's children who are then living; provided, however, that if any such child is then under the age of twenty-one (21) years, then in lieu of outright distribution of such share to such minor child, such share shall be added to the principal of a similar trust created by the settlor for the benefit of such child and shall be held, administered and distributed as a part thereof; and

(b) If none of such children is then living, then to the person or persons who shall be appointed to administer _____'s estate, to be disposed of as a part of such estate.

B. Irrevocable Trust

This trust is irrevocable and the settlor shall have no right whatsoever to alter, amend, revoke, or terminate this trust, in whole or in part. It is the settlor's intention that the trust income shall not be considered his income for income tax purposes and that no part of the trust shall be included in his gross estate for estate or inheritance tax purposes, and therefore, the settlor shall have the right at any time to release, renounce, or disclaim any right, power or interest which might be construed or deemed to defeat such intention. Neither the creation of this trust nor any distribution of income or principal hereof shall be deemed or considered to discharge or relieve the parents of _____ from their legal obligation to support and educate her.

C. Spendthrift Clause

The interest of any beneficiary in the income or principal of this trust shall be free from the control or interference of any creditor of a beneficiary or any spouse of a married beneficiary, and shall not be subject to attachment or other legal process or susceptible of anticipation or alienation.²⁵

D. Powers of the Trustee

In the interest of brevity the general powers of the trustee are not set forth. Commingling of trust assets with assets of other trusts should not be permitted, nor should the trustee be authorized

²⁵ Presence of spendthrift clause does not create a future interest. Rev. Rul. 54-344, 1954-2 Cum. Bull. 319.

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or directed to retain non-income producing assets or to invest in such assets. In order to avoid taxation of the income to the donor under Section 675 and 677, the following restrictions on the trustee's power are suggested:

The foregoing powers are subject to the following restrictions: no loans shall be made without full and adequate security being received and full current rates of interest being charged; all sales, purchases, exchanges or other dealings with trust property shall be made for full and adequate consideration in money or money's worth; and no part of the trust principal or income shall be applied to the payment of premiums on policies of insurance on the life of the grantor. No person, other than the trustee, shall have or exercise the power (a) to vote or direct the voting of any stock or securities of this trust, (b) to control the investment of property of this trust either by directing investments or reinvestments or (c) to reacquire or exchange any property of this trust by substituting other property of an equivalent value.

E. Manner of Making Distribution

The trustee may make any payments hereunder, directly to the beneficiary, or to her legal guardian, or to the guardian of her person, or to any other person deemed suitable by the trustee, or by direct payment of such beneficiary's expenses.

V. OBTAINING RULING ON TRUST

Generally, a 2503(c) trust will be used where the donor desires to embark on a long term program of small annual gifts. It would be most unfortunate for the donor to discover several years later that the Commissioner refused to allow the annual exclusion. Not only would back gift taxes and interest be due, but a new trust would be needed for future gifts and, in addition, it would be necessary to continue administration of the old trust. Therefore, cautious counsel may consider the advisability of making a nominal gift to the trust on its creation, and then requesting an immediate ruling as to whether the trust qualifies under Section 2503(c).

When making gifts of closely held stock, it might be advisable to make annual gifts in amounts slightly in excess of the \$3,000 exclusion and accordingly pay a small tax in order that protection may be claimed under 2504(c) against a subsequent revaluation of the transferred assets by the Service. This is particularly useful where values are susceptible of wide differences of opinion between the taxpayer and the government. Although the application of 2504(c) will not prevent a later claim by the government that no exclusion was allowable in the prior year, the necessity of filing a return if the gift exceeds \$3,000 would commence the running of the statute of limitations.

VI. SECTION 2503 (b) TRUSTS

In addition to treating gifts to minors in the 1954 Code, Congress repealed the rule of the *Evans* case by inserting the following sentence in Section 2503 (b):

Where there has been a transfer to any person of a present interest in property, the possibility that such interest may be diminished by the exercise of a power shall be disregarded in applying this subsection, if no part of such interest will at any time pass to any other person.

An example contained in the Finance Committee Report illustrates the application of this language. Suppose a trust is created with income payable to A for life, remainder to B, and the trustee is given uncontrolled discretion to pay all or any part of the principal to A at any time. Under the *Evans* decision, A's income right would be a future interest, since its value is indeterminate in view of the trustee's power to invade principal. Under 2503(b), however, this would be a present interest entitled to the annual exclusion. A's income interest may be diminished by exercise of the power to invade principal, but nothing passes to any third person. A possible unintended result of this change, though, is that a trust permitting discretionary accumulation of income will qualify in part as a present interest, so long as no other person has any interest in the property. Thus, the *Fondren* case may be legislatively overruled.

VII. NON-TRUST GIFTS TO MINORS

Persons who have made outright gifts to minors without intervention of a legal guardian, either in the face of or in ignorance of the legal disabilities of a minor under state law, have generally achieved favorable tax results.

Take the case of the father who gives shares of stock to his minor child and registers the stock certificate in the child's own name. It now has been settled that this transfer constitutes a present interest. The Internal Revenue Service has put an end to the uncertainty over outright gifts by ruling that "an unqualified and unrestricted gift to a minor, with or without the appointment of a legal guardian, is a gift of a present interest."²⁶ Since the child is the actual owner, the child, and not the father, will be taxed on the dividends and profits from sales, even though such income is used for the child's support. The child will receive the income tax benefits of his \$600 exemption and the new dividend exclusion and credit. The father can still claim the child as a dependent, if he continues to furnish more than one-half of the child's support, until the child is 19, and thereafter, so long as the child is a student.²⁷ These tax benefits should be balanced against (a) the inconvenience of handling the property; (b) the necessity of appointing a legal guardian in order to sell the stock; (c) the fact that the father may reacquire the property by inheritance if the child dies before attaining the age where he can make a will; and (d) the fact that the child will have complete control of the property at the age of 21.

Another father, in order to avoid putting title in the minor's name, might give shares of stock to his child and register them in the mother's name as agent or nominee for the child. Presumably, this would constitute a gift of a present interest, but it might be held to be a future interest if there are some conditions or limita-

²⁶ Rev. Rul. 54-400, 1954-2 Cum. Bull. 319; Beatrice B. Briggs, 34 T.C. No. 117.

²⁷ Int. Rev. Code of 1954 §151(e).

tions on the mother's holding of title or on the application of the income.²⁸

In the past few years a great deal of interest has been engendered by acts concerning gifts of securities to minors. The Model Gifts of Securities to Minors Act originally sponsored by the New York Stock Exchange and the Uniform Gifts to Minors Act have been adopted in almost every state. Briefly, they create a form of statutory trust and eliminate the necessity of a legal guardianship. If the securities are in registered form, the donor makes the gift by registering the stock in his own name "as custodian for _____, a minor" followed by the citation of the statute. With bearer securities, such as many types of bonds, the donor delivers the bonds plus a deed of gift containing similar language to another family member who will act as the custodian. Under the act the custodian is granted full managerial powers. Generally speaking, the custodian has powers and duties similar to a guardian of the minor's property, but of course, without the necessity of posting bond or of accounting to a court or of obtaining court approval of purchases and sales and expenditures for the minor.

Transfers under these custodian statutes will qualify under Section 2503(c) for the gift tax exclusion, and the income from the custodianship property will be taxed to the minor. If the donor is also custodian, the property will be included in his gross estate if he dies before the minor attains 21.²⁹

By their terms, the application of such statutes is limited to transfers to a minor by gift made after adoption, and their use is limited to securities. (The Uniform Act also permits cash gifts). In view of their simplicity, they may well prove more popular than Section 2503(c) trusts. However a properly drafted trust has the following advantages:

- (1) initial gifts and later investments are not limited to securities;
- (2) a broader choice of trustees and successor trustees is afforded;
- (3) investments are not limited to the prudent man rule;

²⁸ Madeleine N. Sharp, 3 T.C. 1062 (1944) (acq.); see Katherine Schuhmacher, 8 T.C. 453 (1947) (acq.).

²⁹ Rev. Rul. 59-357, I.R.B. 1959-44, p.18, holding that the income, estate and gift tax consequences of the Model Act and the Uniform Act are the same.

WANTED TO BUY

The Following Colorado Reports

48, 49, 52, 56, 58, 60, 76, 80, 81, 82, 83, 84, 85,
90, 92, 98, 99, 100, 101, 102, 104, 111, 112, 113, 114, 115.

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(4) provision can be made for a gift over to third persons rather than to the minor's estate should the minor die before reaching 21, thus avoiding probate administration and possible return of the property to the donor-parents through inheritance from the minor;

(5) accumulated income is taxed to the trust, not to the child; and

(6) the uncertain application of various state laws (i.e. state of the present or future domicile of the minor, donor or custodian or state of incorporation of the company the stock of which is donated) to the custodianship status are avoided.

Further, the cost of a 2503(c) trust is not significant. The well-advised donor will generally choose the trust for the reasons mentioned and its greater flexibility and individuality.

VIII. CONCLUSION

Although Sections 2503(b) and (c) represent an improvement in the gift tax exclusion area, there is a need for further legislation.

The chief criticism against Section 2503(c) has been directed to its requirement that the property must pass outright to the donee at twenty-one. There would appear to be no valid social or legal reason compelling the selection of this age, and it is certainly contrary to the normal and understandable desires of most donors. Some people feel that gifts to minors have now been granted an undue advantage over gifts to adults.

The new language in Section 2503(b) presents the anomalous result that the longer the ultimate payment of principal is postponed, the larger the annual exclusion. For example, a trust granting income to A for life with remainder to B will have a larger exclusion than a transfer where A receives the income for only one year and then receives the principal, although obviously A has a more valuable right in the latter case.

One possible solution is to grant an exclusion to all gifts where no third person has an interest in the property. If such were the rule, the donor would be free to fix the time for ultimate principal distribution at any future date, whether the beneficiary be a minor or an adult.

To accomplish this result, the American Bar Association has suggested the following language in lieu of present Section 2503(c):

(c) *Certain Transfers not Considered Future Interests*

No part of a gift shall be considered a gift of a future interest in property for purposes of subsection (b) if the property and the income therefrom will, to the extent not distributed to or expended by, or for the benefit of, the donee during his life, be payable on his death to his estate, or as he may appoint under a general power of appointment as defined in Section 2514(c).³⁰

In spite of this criticism, Section 2503(c) with the liberal interpretations of the regulations gives the lawyer a handy form of trust for modest gifts.

³⁰ H.R. R-p. No. 10591 §61, 86th Cong., 2d. Sess. (1960).