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GIFTS TO MINOR CHILDREN—GUARDIANSHIPS VS. INTER VIVOS TRUSTS—IS THE KIECKHEFER TRUST THE ANSWER?

WILLARD J. WRIGHT*

Much comment has followed the recent decision of the Court of Appeals for the 7th Circuit in Kieckhefer v. Commissioner, with some encouragement for persons contemplating gifts in trust for minor children. The spectacular nature of the trust instrument in this case and the outspoken refusal of the Tax Court to accept the type of trust involved, at least for tax purposes, furnishes an occasion to reconsider the relative merits of a trust and a guardianship as a receptacle for gifts for the benefit of minor children. While the donor of gifts to minor children has had a difficult time escaping tax liability in recent years in the income and death tax field, these liabilities have become “relatively” crystallized. The judicial analysis of the Kieckhefer “trust” focuses attention upon the problems of the trust donor in the gift tax field. Its provisions reflect an attempt of the donor to avoid liability not only for income, estate, and inheritance taxes, but also for gift tax by taking advantage of the annual exclusion provisions of the law.

Tax trends and court decisions over the past five or six years have been responsible for some of the oddest trust provisions. This is true to such an extent that one wonders whether the obvious strain to satiate

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2 189 F. 2d 118 (C.C.A. 7th 1951).

3 Kieckhefer v. Commissioner, 15 T.C. 111 (1950); Willis D. Wood v. Commissioner, 16 T.C. No. 118 (1951); Stifel v. Commissioner, 17 T.C. No. 71 (1951); John E. Daniels v. Commissioner, 10 T.C.M. 147 (1951).
exacting tax interpretations is not defeating its purpose.⁴ Thus, in the Kieckhefer case a grandfather was induced to transfer certain property to a trustee for his minor grandson, aged two months. The trust instrument had the usual protective provisions for the benefit of the minor child and the usual broad trust powers invested in the trustee, but it also contained this unusual clause:

13. This trust has been created by the donor after full consideration and advice. Upon such consideration and advice the donor has determined that this said trust shall not contain any right in the donor to alter, amend, revoke or terminate it. The beneficiary shall be entitled to all or any part of the trust estate or to terminate the trust estate in whole or in part at any time whenever said (minor) or the legally appointed guardian for his estate shall make due demand therefor by instrument in writing filed with the then trustee, and upon such demand being received by the trustee, the trustee shall pay said trust estate and its accumulation or the part thereof for which demand is made over to said (minor) or to the legally appointed guardian for his estate who made such demand on his behalf.

Why should anyone take such pains to draw a trust instrument with all of the usual trust powers and provisions and then give his two-month-old beneficiary the exclusive unchallengeable right to terminate the trust estate and devour for his own purposes all or any part of the trust corpus and income? From time immemorial the primary function of such a trust instrument was to protect the beneficiary from himself, his immaturity, inexperience, or incompetence. It also provided a method of freeing the estate administration from the ordinary shackles of the law governing guardianships by granting broad powers of investment and management to an inter vivos trustee. For centuries considerable advantages have been found in the trust device over a legal guardianship. Yet here is a “thoughtful” grandparent providing at the end of his trust that if his two-month-old grandson demands in writing that the trustee turn over all of the estate to him, the trustee is compelled to do so. Why didn’t the grandfather put the entire estate directly in the hands of the grandson or of a legal guardian? Perhaps the answer lies in the fact that so long as the minor or his guardian does not exercise his power, all of the usual advantages of a trust over a guardianship can be enjoyed.

⁴Drexler, 29 Taxes, at page 748: “It might be asked why taxpayers have gone to such lengths to obtain a tax benefit which by its very nature is likely to save little, if any, tax. The answer lies partly in the fact that taxpayers have become so tax conscious in recent years that they often react favorably to almost any legitimate tax savings plan without full consideration of other consequences. This is especially true where the other consequences lie in a field with which they are generally not likely to be familiar, such as the field of trusts and guardianships.”
GIFTS TO MINOR CHILDREN

ADVANTAGES OF TRUSTS OVER GUARDIANSHIPS

In the state of Washington these advantages are considerable insofar as the management and control of the trust estate are concerned. The trustee, given the written authority, may exercise the broadest power over the management of the trust estate, while the legal guardian is subject always to "the general direction and control" of the Superior Court controlling his appointment. The guardian must obtain court approval of every sale of both real and personal property, while the trustee may keep his own counsel in the sale or disposition of any portion of the trust estate. The guardian is not allowed to use either income or principal from the estate for his ward's support and education without first obtaining court approval, and unless the parents of the ward are unable to maintain and educate him. The trustee could, in a trust instrument so providing, rely solely upon his own discretion in the application of both income or principal of the trust estate. Generally the right of the guardian to enter contracts even with court approval is so limited in some cases that if the contract proves to be detrimental to the estate, any loss incurred will be charged against the guardian personally.

* Under Washington law, if the trustee's powers are not expressly granted in the trust instrument his powers generally are reduced to no more than are currently enjoyed by a legal guardian in the state of Washington. Rem. Rev. Stat. § 11548- to 11548-28 (1941 Supp.) require the trustee unless excused by the trust instrument provision, to file reports and accounts each year, an inventory of the estate, file distribution accounts, vouchers, and a final account. He must also file notice of appointment and a copy of the trust instrument, including a list of the names, addresses and dates of birth of beneficiaries, etc. In contrast, a legal guardian must file a report and account only every two years. Rem. Rev. Stat. § 1575(3).


* Rem. Rev. Stat. § 1572. The guardian must apply to and obtain the approval of the Superior Court whenever he desires to sell or transfer any assets of the guardianship estate. The sale of any property of the guardianship estate requires court approval "where . . . it is necessary to sell . . . any of the real or personal property of the estate of the ward for the purpose of paying debts or for the care, support, and education of such ward . . . or for the purpose of making any investments or for any other purpose which to the court may seem right and proper."

8 Rem. Rev. Stat. § 1575(6). "When any ward has no father or mother or such father or mother is unable or fails to educate such ward, it shall be the duty of his guardian to provide for him such education as the amount of his estate may justify."

In re King, 151 Wash. 121, 275 Pac. 82 (1929), where the Court said at page 124: "Where the guardian is also the parent of the infant ward, he will not be permitted to sell the ward's real estate for such purposes unless it is clearly shown that he is unable to support and educate him"; In re Rohne, 157 Wash. 62, 288 Pac. 269 (1930), where the Court observed at page 72: "It is the law that in proper cases minor wards may be supported from their own estate where it is shown that the parents have not the requisite ability to support the wards in a position and station commensurate with the ward's expectations and station in life. . . ." Confirmed and cited with approval in Goodwin v. American Surety Company, 190 Wash. 457, 68 P. 2d 619 (1937).

9 25 Am. Jur. 64.
Investment powers of the trustee prior to 1951 were vastly superior to those of a legal guardian in Washington. In 1951, however, the state Legislature removed existing doubts as to the applicability of the Prudent Man Investment Rule to the investment of guardianship funds. Although a written trust agreement may provide for unlimited powers of investment in a trustee, this appears to be of slight, if any, advantage over the Prudent Man investment power.

A trustee is not required to furnish a bond, but until 1951 all guardians were required to do so. Under another 1951 amendment to the Washington law any bank or trust company authorized to act as guardian may do so without bond. Likewise, certain individual guardians are exempted in limited estates which are invested in special ways, but in all other cases the legal guardian is required to furnish a bond to be fixed by the court.

**Advantages of Guardianships over Trusts in the Tax Field**

In general, therefore, the advantages of a trust over a guardianship for administration purposes cannot be challenged. However, state and

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10 Under the former Washington law considerable doubt existed as to the precise obligation of the guardian as to investments. *Jiskra Estate*, 108 Wash. 187, 182 Pac. 961 (1919); *Carlson's Guardianship*, 162 Wash. 20, 297 Pac. 764 (1931); *King v. Sells*, 193 Wash. 294, 75 P. 2d 130 (1938); *LeFevre Estate*, 9 Wn. 2d 145, 113 P. 2d 1014 (1941); and in any case, the statute required court approval. (REM. REV. STAT. § 1582). In 1943 considerable confusion ensued from the act passed by the Legislature (REM. REV. STAT. § 1583-1, 1943 Supp.) specifically restricting investments by guardians to "such bonds, securities, or other choses in action as are made by law, legal investments for trust funds by corporations doing a trust business or mutual savings banks doing business under the laws of the State of Washington..." At the same time the law (REM. REV. STAT. § 3255-1 et seq., 1941 Supp.) listed only very specific investments such as special Government obligations, first mortgages on real estate, public utility obligations and certain limited industrial bonds. No corporate stocks could be considered. The same limitations applied to mutual savings banks. (REM. REV. STAT. § 324 et seq.) In 1947 some endeavor was made by the Legislature to broaden trustees' rights to invest under the Prudent Man rule (REM. REV. STAT. § 3255-10a et seq., 1947 Supp.), but it was considered very doubtful that the definition of "fiduciary" under that statute actually included a guardian.

11 Wash. Laws Regular Sess. 1951, ch. 218 § 1 provides that a "guardian of any estate is a fiduciary within the meaning of the Prudent Man Investment rule" set forth in REM. REV. STAT. § 3255-10b (1947 Supp.), which in part provides that a guardian may invest guardianship funds in "every kind of property, real, personal or mixed, and every kind of investment, specifically including, but not by way of limitation, deben-
tures and other corporate obligations and stocks, preferred or common, which men of prudence, discretion and intelligence acquire for their own account."

12 Wash. Laws Regular Sess. 1951, ch. 242. This same provision of the law also eliminates the necessity for a bond in special cases where the assets of the ward's estate do not exceed the sum of $5,000, and where certain special treatment is accorded such assets.

13 REM. REV. STAT. § 1573 requires a guardian to furnish "bond with sureties to be approved by the court."

In such a situation frequently a guardian would not be able to obtain satisfactory bond without agreeing to joint control of the guardianship estate by the bonding company, which would possibly double the inconvenience of the guardianship administration and frequently make it very difficult.
federal tax legislation and court decisions have in recent years taxed the "trust donor" as to income, gift, and estate and inheritance taxes in situations where the same donor, had he made his gift outright to a legal guardian for the minor child, would not have been taxed at all. These tax trends have gradually reduced the advantages of a trust over a guardianship to a point where the trust has become so expensive (and sometimes disastrously so) and so out of proportion to the incidental expenses and inconveniences of administration of a legal guardianship as to constitute almost complete discouragement to the donor against the use of a trust. Accordingly, what the trustor was endeavoring to do in the "Kieckhefer trust" was to rid himself of all possible controls over or interests in the trust property and to give all powers and rights to the infant so that no tax liability might be imputed to the trustor, yet still protect the infant with the advantages of broad managerial freedom and discretion of an inter vivos trustee.

A. Income Tax

In the trust field many donors painfully discovered after it was too late that they were liable for taxes in a bracket superimposed upon their own against income which they believed they had given to an inter vivos trust for minor children. The income tax liability of a donor making gifts to a trust for minor children is fairly well established under case and statutory law, and although there are still some disturbing factors, it was not in this particular category that the Kieckhefer problems lay. Mr. Kieckhefer's trust was drawn so that there might not be any income tax liability. There was no possibility of the trust estate revesting in the donor which would tax the income to him.\(^\text{14}\) He did not retain any controls which, under the Clifford doctrine,\(^\text{15}\) would tax income to him, and the trust income was not to be used to

\(^{14}\) **Int. Rev. Code** § 166: "Where at any time the power to revest in the Grantor title to any part of the corpus of the trust is vested in (1) the Grantor, either alone or in conjunction with any person not having a substantial adverse interest in the distribution of such part of the corpus or the income therefrom; or (2) in any person not having a substantial adverse interest in the disposition of such part of the corpus or the income therefrom; then the income of such a part of the trust shall be included in computing the net income of the Grantor."

\(^{15}\) *Helvering v. Clifford*, 309 U.S. 331 (1939). The Court said at page 792: "Where the head of the household has income in excess of normal needs it may well make but little difference to him (except income-tax-wise) where portions of that income are routed—so long as it stays in the family group. In those circumstances the all important factor might be retention by him of control over the principal. With that control in his hands he would keep direct command over all that he needed to remain in substantially the same financial situation as before." See also *Cushman v. Commissioner*, 153 F. 2d 510 (C.C.A. 2d 1946).
discharge any of the donor's legal obligations or for any other benefits of the donor which, under the Internal Revenue Code, would tax such income to him.  

These laws make it particularly difficult for parents to use the trust device for the benefit of their minor children, since any provision that the income may be used for the education or support or maintenance of the children did, prior to 1949, render all of the trust income taxable to the parent donor. This has been changed by an amendment to the code section taxing to the parent donor only the amount of the trust income actually used for this purpose.  

Such a situation would not occur under a legal guardianship device. Any income received by the legal guardian which was devoted to the education, care, or support of the minor child would not be taxable to the parent donor.  

It is generally recognized that the income from an estate which is given by the donor to a guardian of the minor beneficiary rather than to a trust is not taxable to the donor. The case of *Herberts v. Commissioner* furnishes a vivid contrast for income tax purposes of the effect of a guardianship and a trust where a father had made various gifts to or for the benefit of his children. Several were outright or held by him as a "guardian," and others were made in trust for their benefit.  

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16 INT. REV. CODE § 167: "(a) Where any part of the income of the trust (1) is, or in the discretion of the grantor or of any person not having a substantial adverse interest in the disposition of such part of the income, may be held or accumulated for future distribution to the grantor; or (2) may, in the discretion of the grantor ... be distributed to the grantor ... then such part of the income of the trust shall be included in computing the net income of the grantor."  

17 *Helvering v. Stuart*, 317 U.S. 154 (1942), in which a father created a written trust for the benefit of his children naming himself, his wife and his brother as trustees, with power to devote so much of the net income as "to them shall seem advisable" to the education, support and maintenance of the minor beneficiaries.  

18 INT. REV. CODE § 167(c) : "Income of a trust shall not be considered taxable to the grantor under subsection (a) or any other provision of this chapter merely because such income, in the discretion of another person, the trustee, or the grantor acting as trustee or co-trustee may be applied or distributed for the support or maintenance of a beneficiary whom the grantor is legally obligated to support or maintain except to the extent that such income is so applied or distributed."  

19 *Heller v. Commissioner*, 41 B.T.A. 1020 (1940); *Miller Trust v. Commissioner*, 7 T.C. 1245 (1946), where the issue involved taxation on income to the donor if there were a trust, but not if there were a legal or natural guardianship. The Court stated at page 1249: "Although in strict contemplation of law it may have been more proper for them to apply for appointment as legal guardians to manage the estate of the children, their desire to avoid the expense and complication of such a procedure is understandable. As a practical matter, it is certainly not unusual for parents to manage the property and attend to the affairs of their minor children without such formalities." This case affords ample warning that it would probably be better to have a legal guardianship and avoid any of the tax problems which naturally ensue from some less formal arrangement. The same problem was discussed in *Pettus v. Commissioner*, 45 B.T.A. 855.  

20 10 T.C. 1053 (1948).
The Tax Court relieved the donor father from any income tax liability on the outright gifts, over which, however, he exercised "the rights of a natural guardian," and yet taxed the father on the income of the other gifts which he held in a trust capacity.

The donor thus found one of the "advantages" of a legal guardianship was the general indication of the courts that he would not be taxed on the income of the gift corpus if he gave it to a guardian for the minor child. Even though the guardian may use the income for the education and support of the child of the donor, no tax would ensue to the donor, and the fact that the donor as a parent of the child might find the corpus revesting in himself in the event of the child's death again would not tax the income to him under the provisions of Int. Rev. Code § 166.

It is submitted that the real test as to the proper taxability of the donor in these so-called family trusts should not be whether there has been a trust or legal guardianship, but whether or not the gift for the benefit of the children of the donor has been completed and the donor has in fact divested himself of all incidents of title. This was brought out in the recent case of *Visintainer v. Commissioner,* where the court said: "The test to be applied in a case of this kind (gifts from one member of the family to another which have the effect of reducing taxes) is whether good faith, bona fide gifts were made to the children, or the device was resorted to as a sham for evading income tax."

Certainly no question can be raised but that Mr. Kieckhefer divested himself of all the necessary controls and incidents of ownership in his trust so as to avoid any question of income tax liability.

The language in the *Kieckhefer* case and in other similar cases clearly puts the donor beyond the reach of the income tax collector.

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22 *Kieckhefer v. Commissioner, supra; Strekalovsky v. Delaney, 78 F. Supp. 556 (1948): "To pay any part or parts of his or her share(s) to him or her ... as if the interest of each said child were held by the Trustee herein as guardian for said child and as if the trustee were making payments and distributions in that capacity, for the benefit of each child respectively"; and in *Cannon v. Robertson, 98 F. Supp. 331 (June 25, 1951)* where the trustees were to pay all of the income to the minor and were instructed to "pay over to or use and apply for the support, maintenance, education and pleasures of the said (minor) from time to time such amounts of the principal of the property held in trust hereunder as may be approved and directed by the court ... ."

Stifel v. Commissioner, 17 T.C. 71 (October 10, 1951): "The trustee during the minority of settlor's daughter, may make payment of income or principal applicable to the use of the settlor's said daughter by paying the same to her mother, guardian, or other person having the care and control of such daughter ... as if the interest of said daughter in the trust property was held by the trustee as guardian for said daughter...."
B. Death Taxes

The trustor's problems in the death tax field are likewise fairly well defined, but require the same care in draftsmanship as in the income tax field. In the state of Washington any carelessness in this regard is doubly penalized, since the State Inheritance Tax statute is as broad in scope as the federal estate tax provision. This death tax liability can be devastating, as was found in the Estate of Speigel v. Commissioner where a grandfather had set up a trust for the benefit of his children and grandchildren and had not intended that any portion of the trust estate would revert to him. Under an interpretation of Illinois law there was a very remote possibility that the trust corpus would revert to him. This possibility had a value on the actuarial tables of $4,000. On his death the Commissioner and the United States Supreme Court found that the entire trust estate should be added to his estate, which resulted in an additional tax of $450,000! Although this unfair result was corrected by subsequent legislation, the damage had been done. Donors must be prepared for such decisions of the courts. It would not have happened if the donor had made his gift "outright" to the guardians of the minor children, but again he might then have sacrificed his desired result either of distribution or of management.

In the recent case of Townsend v. Thompson a father gave certain property to himself as trustee for his minor sons with power to expend the trust income "for the education and maintenance of said beneficiary while a minor." After the father's death the District Court taxed the trust estate held for the minor son entirely in the estate of the father donor under Int. Rev. Code § 811(c). Retention by the donor of the right to use the income to the "discharge of a legal obligation of the decedent or otherwise for his primary benefit" was such right to enjoyment of the income as to tax the entire trust estate to the father. While this decision may be distinguished under the federal law on the ground that the father donor was also the trustee, the Washington statute carries a much broader interest in that it applies to property passing to "any person in trust."
Again, in the death tax field, the test appears to be whether or not the incidents of ownership were completely transferred by the donor to the donee. In the legal guardianship situation there would be no question. In the trust situation such questions naturally arise, depending upon the provisions of the trust instrument. These rules are fairly well settled and generally understood in the tax field, and again, the Kieckhefer trust provisions were so drawn as to avoid the incidence of these taxes to the donor.

C. GIFT TAXES

Having the benefit of previous settled cases in the income and death tax field, Mr. Kieckhefer's course was well charted. But in the gift tax field his trust device was pioneering. In this field of the tax law, both federal and state, the situation is in complete flux. Here the federal Tax Court openly opposes the decisions of other federal courts, and nothing but well considered legislation or the ultimate determination by the respective state and federal Supreme Courts can eventually settle the problems. This is caused by the provision, identical in both Washington State and federal law, allowing an exclusion from gift tax up to $3,000 per year per donee. To the Washington practitioner, therefore, the decisions of the federal courts construing this law are of moment on the local, as well as the federal level.

Anyone may make a gift without tax and even without having to make a gift tax return if the value of the gift does not exceed (under current law) the sum of $3,000. This exclusion applies to each gift to any number of donees. Thus, if the donor gave to five donees, he could give up to a total of $15,000 each year in $3000 shares to each donee without tax. So in any estate planning for one's child or children, consideration must be accorded these provisions.

The "joker" in this salutary exclusion provision is immediately

estate for inheritance tax purposes "all property . . . which shall pass . . . to any person in trust or otherwise . . . under which the grantor or donor has retained for his life . . . the possession or enjoyment of any part of the property or the right to all or any part of the income from the property. . . ."

29 REM. REV. STAT. § 11218-14(b): "(b) In the case of gifts, other than of future interests in property, made to any person by the donor during any calendar year, the first three thousand dollars ($3,000) of such gifts to such persons or body politic or corporate shall not, for the purpose of this Act, be included in the total amount of gifts made during such year."

30 INT. REV. CODE § 1003(b) (3). "In the case of gifts (other than gifts of future interests in property) made to any person by the donor during the calendar year 1943 and subsequent calendar years, the first $3,000.00 of such gifts to such person shall not, for the purposes of subsection (a), be included in the total amount of gifts made during such year."
question, but has recognized its existence.88

Thus, where the trust provides for the immediate and complete distribution of all the trust income to the beneficiaries, it does not necessarily follow that the entire gift is one of a present interest. As in the decision of the Supreme Court in the Disston case, and as discussed briefly by the 9th Circuit Court of Appeals in the Sharp case, the courts have eventually evolved another hurdle for Mr. Taxpayer to negotiate. It is said that a trust gift consists of two parts, income and principal. If all income goes to the minor beneficiary, that part of the gift is a present interest, and entitled to exclusion under the gift tax act, but if the principal is not distributable to the minor immediately, then that portion of the gift is a future interest, and the donor is not entitled to an exclusion as to that part.40

However, if the parent donor is too generous and provides in his trust agreement that the trustee shall pay not only all income to the minor children, but also portions of the principal, then the courts deny any exclusion to the donor on the ground that it can't be evaluated.

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88 Fondren v. Commissioner, 324 U.S. 18. The Court observed: "Finally it is urged that unless these gifts are to be taken as conferring the right to immediate enjoyment, no gift for the benefit of a child of tender years can be so regarded since in any such case 'some competent person must be the primary judge as to the necessity and extent of reasonable requirements of the beneficiary.' The argument is appealing insofar as it seeks to avoid imputing to Congress the intention to 'penalize gifts to minors merely because the legal disability of their years precludes them for a time from receiving their income in hand currently'—but we think it is not applicable in the facts of this case..." The Court had previously observed in this case as follows: "The statute in this respect purports to make no distinction between gifts to minors and gifts to adults. If there is deferment in either case the exemption is denied. Consequently in this case the donors' laudable desire to make provision for their grandchildren in case of future need cannot nullify the deferment which the recited absence of present need, coupled with the terms of the trust, brought about."

40 Again, one of the leading cases on this subject is in the 9th Circuit, Fisher v. Commissioner, 132 F. 2d 383 (C.C.A. 9th, 1942). Mrs. Fisher created a trust for her six grandchildren. The trustee was to distribute all of the income in equal shares directly to such of the grandchildren as were over twenty-one, and to the parents of those who were not. The principal was to be held for distribution when the grand-
In 1949 the *Kniep* case laid down this rule which was followed by the Tax Court in *Evans v. Commissioner* in 1951. The courts admit that the right to encroach upon the corpus when coupled with the immediate right to income is considerably larger than the mere right to income. Still the courts deny any part of the statutory gift tax exclusion on the sole ground that valuation is either too difficult or impossible.

On the other hand, it is held that if a parent makes the gift to the guardian of the minor child, there is no question but that the exclusion may be applied.

children attained certain ages from time to time. The Board of Tax Appeals held the gift of income to be one of a present interest and the gift of corpus to be one of a future interest. In a thorough analysis of the cases decided to that date our Court of Appeals affirmed the Board of Tax Appeals decision saying, "The Taxpayer's assertion that there could be only one gift to each beneficiary and that that gift could not at the same time be both a present interest and a future interest in property, is erroneous. Whether each beneficiary is considered as having received one gift or two, there can be no doubt but that under the terms of the trust agreement each was given two distinct kinds of interests." The Court cites the case of *Charles v. Hassett*, 43 F. Supp. 432 (D.C. Mass., 1942), which very clearly expounds the anomaly of this double property interest in one gift, at page 434. "Historically, lawyers have treated gifts of income beginning at once and lasting for life or for a period of years as a 'present interest,' and gifts of principal at a future date as a 'future interest'; Congressional committees and the Treasury appear to have had some such distinction in mind; ... this and other Courts in construing the gift tax statute have used that line of distinction in cases where the gifts of income and of principal were to different persons. *Commissioner v. Brandegee* (C.C.A. 1), 123 F. 2d 58; *Welch v. Paine* (C.C.A. 1), 120 F. 2d 141; *Helvering v. Rubinstein* (C.C.A. 8), 124 F. 2d 969; *Commissioner v. Taylor* (C.C.A. 3), 122 F. 2d 714. See 2 PAUL, FEDERAL ESTATE AND GIFT TAX § 15.11, 976, 977. No historical reason justifies abandoning the distinction in cases where the gifts of income and of principal are to the same person and are therefore regarded by donor and donee as one gift."

41 *Kniep v. Commissioner*, 172 F. 2d 755 (C.C.A. 8th, 1949) which held that trusts wherein all income was payable to the beneficiaries when they reached the age of sixty-five but where the trustee was also authorized to encroach upon the principal of the trust estate for the benefit of any beneficiary, the Court, though admitting the present interest nature of the gift of the income, did not permit any exclusion from gift tax for the reason that the taxpayer was not able to prove the amount of the value of the present interest, the Court presuming that the right of the trustee to encroach upon the corpus reduced in equal measure the value of the present interest of the right to receive income.
So the persevering donor, still wanting the benefits (so hard to come by) of a written trust agreement, and still demanding freedom from any tax consequences, conceived the remarkable product reflected in the Kieckhefer, Cannon, Strekalovsky, and Stifel cases.

The Commissioner and the Tax Court have stoutly maintained that any gift of corpus in trust for a beneficiary is a gift of future interest. In Jessie Phillips the court observed: “The mere fact that the distribution of the corpus is postponed is enough to make the gift a gift of a future interest.”

The majority opinion in the Tax Court decision of the Kieckhefer case ruled in essence that the minor beneficiary has not the capacity to “presently enjoy” income or principal, and hence the postponement by legal fiction makes the gift one of a future interest.

Other federal tribunals, however, have recently injected new hope for Mr. Taxpayer and take a more practical view of the nature of the beneficiaries’ rights over trust principal. The Court of Appeals for the 7th Circuit in reversing the Tax Court in Kieckhefer v. Commissioner held that not only the gift of income to the trust, but also the gift of the corpus, constituted a present interest, and the entire gift qualified for the exclusion under the Act.

Mr. Kieckhefer’s attorney argued that since the child or his legal guardian could demand all or any part of the trust, and could terminate the trust at any time, there was no “postponement of enjoyment of its trust corpus”; that the minor had the right to obtain at any moment the full use and enjoyment of the corpus, and thus the entire gift, though in trust, was of a present interest.

The Commissioner argued that the enjoyment or use of the corpus was necessarily postponed because (1) the infant beneficiary, being of tender years, could not make an effective demand, and (2) the minor had no legally appointed guardian at the time of the execution of the trust or since its establishment.

guardians of the children, there could be no question but that the exemption would apply.”

45 Supra, note 22.
46 12 T.C. 216 (1949).
47 Id. at 221. See also Willis D. Wood v. Commissioner 16 T.C. § 118, May 4, 1951.
48 Nor can the minor be saved under the Tax Court theory by a legal or a natural guardian. The Tax Court said at page 116: “Even where a gift is made directly to the fathers of minor donees, and as the guardians of such donees without the intervention of a petition in court for the appointment of a legal guardian, it does not necessarily follow that the gift is a gift of a present interest.” Citing Schumacher, 8 T.C. 453, which sustains this fiction that “Gifts to minor children made directly to their fathers as guardians were gifts of future interests.”
49 189 F. 2d 118 (1951).
The Court observed that "the Commissioner's reasoning reduces to a myth his concession that 'gifts to minor beneficiaries are placed on an equality with gifts to adults.'" It requires that the "beneficiary must have the actual, physical use, possession or enjoyment of the property, in other words, that the beneficiary occupies the same position relative to the gift that a boy sustains to his top or a girl to her doll."

"It is not, however, the use, possession or enjoyment by the beneficiary which marks the dividing line between a present and future interest, but it is the right conferred upon the beneficiary to such use, possession or enjoyment." (Italics supplied) "...the fallaciousness of the Commissioner's contention is the failure to distinguish between restrictions and contingencies imposed by the donor (in the case of the trust instrument) and such restrictions and contingencies as are due to disabilities always incident to and associated with minors and other incompetents."

The Court in a 2 to 1 decision reversed the Commissioner and the Tax Court, and granted Mr. Kieckhefer the right of the annual gift tax exclusion to the principal held in trust.

Following the Kieckhefer decision, the federal District Court of North Carolina in Cannon v. Robertson⁴⁹ held to be a present interest both income and principal given in trust for a minor where the trustee was directed to use so much of the principal for the minor "as may be approved and directed by the court vested with jurisdiction of the person and estate of the said" minor.

This appears to put more "discretion in the trustee than was actually contemplated in the Kieckhefer decision. It is submitted that if the Kieckhefer doctrine is right at all, its correctness rests upon the right of the minor or his legal guardian to demand the corpus, whereas in the Cannon case the trustee has no legal compulsion to deliver the corpus unless he in his discretion elects to do so.

But though some district courts will follow or even go farther than the Kieckhefer case, it seems certain that the Tax Court will simply refuse to recognize it.

There is no question but that the U. S. Tax Court will not approve the application of the federal gift tax exclusion law to gifts in trust as set out in the Kieckhefer case. In the most recent case of Stifel v. Commissioner⁵⁰ decided October 10, 1951, a father created trusts for

⁵⁰ Stifel v. Commissioner, 17 T.C. No. 71.
his three minor children and made gifts to the trust, of which a bank was named trustee. The income was to be applied for the benefit of the minors during their lives. On the death of any minor beneficiary, the accumulated income and principal, if any, were to be paid to the administrators or executors of the respective minors’ estates. As in the Kieckhefer case, the trust instrument contained the usual provisions and trust powers and again included the unusual provision in Article 11 to the effect that “the settlor’s daughter shall have the right . . . at any time to terminate this trust, either in whole or in part, and during minority to demand payment of all or any part of any unexpended income in which event such part or all of the principal of the trust or any accumulated income of the trust as to which the trust is so terminated or such part or all of the income so demanded, as the case may be shall be paid over to the settlor’s said daughter, or if she be a minor, to her general guardian or to such special guardian, but in no event to the settlor.” The Tax Court, despite its previous reversal by the Circuit Court, ruled that a gift through this type of trust was a gift of a future interest, and that the donor was not entitled to the gift tax exclusion, saying: “The petitioner not only knew there was no guardian in existence or in contemplation, but also that there was no present reason for or likelihood of the exercise of any right to terminate the trust or demand income as it might later accumulate. He must have anticipated that there would necessarily be a substantial lapse of time before any occasion to terminate the trust or to demand the accumulated income would arise. . . . If the reversal in the Kieckhefer case is in point, then with all due respect, we decline to follow it.”

Three of the judges on the Tax Court dissented from this opinion. The majority decision cites the Fondren and Disston decisions which ruled that an interest is a future interest if the donee does not have the right to immediate use, possession and enjoyment. The decision in the Stifel case seems to inject an additional requirement in that although the donee may have the right to immediate possession, it is still a future interest if any time is required to exercise the right!

Viewing the problem as objectively as a parent can, it would seem that “future interest” should be redefined either by the Supreme Court.

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51 It is to be noted here that in Stifel v. Commissioner the Tax Court was sitting in the jurisdiction of the U.S. Court of Appeals for the 2nd Circuit. The Kieckhefer decision was rendered by the U.S. Court of Appeals for the 7th Circuit. Therefore, if Mr. Stifel chooses to appeal the Tax Court decision and the 2nd Circuit Court affirms the Tax Court, a direct issue between the two Courts of Appeal having coordinate jurisdiction will be joined. This may force the U.S. Supreme Court to resolve the issue.
GIFTS TO MINOR CHILDREN

or by new legislation. Surely if one takes literally the language of the regulations as approved in the Fondren and Disston decisions "any postponement of the right" to enjoy could be practically any slight delay. The Tax Court in Stifel seems to imply, if not decide, that a mere act of demanding the corpus by the minor or the unnecessary delay in appointing a guardian for the minor who could not otherwise demand was a postponement enough to create a future interest. Again even in the case of a legal guardianship, the rule in the Fondren case would cause trouble under the Washington law of guardianship. For in Washington a guardian may not use guardianship funds for the support or education of a child if the parents can make adequate provision. This seems to have been the same restraint laid down by the trust provisions in the Fondren case which prompted the Court to declare it a gift of a future interest.

Under the laws of Washington guardianship the restraint on sale—dependent on the discretion of both the guardian and then the Court—the restraint on contract, and the restraint on use of funds for the minor are certainly, under the gift tax law, not only a postponement, however momentary, but also in many cases a complete denial to the child of the right of enjoyment of the property during minority.

Nice legal points can be made to distinguish a legal guardianship from a trust principally on the basis that in the former the property has really passed to the minor but the law protects the estate from his indiscretion, while in the latter, the property has not actually passed to the minor, but certain rights have been suspended in the trustee. Such reasoning begs the question. In both cases the guardian or bona fide trustees are intended to be mere custodians for the benefit of the minor. As a practical matter, under almost every trust the minor beneficiary receives more benefits, rights and enjoyment from the trust property during minority than under a legal guardianship. Yet oddly enough, under a more generous type of trust where a trustee may give income and principal, our courts have recently denied any exclusion. Whereas, if only income is allowed, exclusion is permitted in part; but in a guardianship where neither principal nor income may, in many cases be used for the minor's benefit, the full exclusion is granted! It is submitted that any real distinction is nonexistent. It is hoped that

52 Efforts are being made by the American Bar Association Committee on Federal estate and gift taxes to amend the gift tax exclusion provision so that it will except from the future interest definition any gifts to minor beneficiaries.

53 See Kniep v. Commissioner, supra.
the U. S. Supreme Court will rule on the problem, but perhaps it is wiser to hope that Congress and the Washington State Legislature will amend the law applying the gift tax exclusion to gifts in trust for minor children.

Pending favorable action by Congress and the Legislature or by the Supreme Court, the gift-minded antecedents of minor children had best employ the accepted form of trust and pay the tax or make their gifts to a legal guardian. The *Kieckhefer* trust is "neither fish nor fowl." It is a trust only so long as the legal guardian chooses not to exercise his right to the trust estate. It is transformed into a legal guardianship with all its encumbrances and limitations, once this right is exercised. The time tested advantages of a trust over a guardianship still remain worthy of serious consideration by the provident persons who desire to establish estates for their minor progeny and who wish to afford the most workable form of protection for both estate and minor. It seems unfortunate to cast out the trust form in those cases where to do so will avoid only a slight tax liability. Yet, on the other hand, perhaps the inconveniences and minor expenses of legal guardianships are easier to endure than the constant hammering of the income, death and gift tax collectors against the generous donor!