Estate of Elmer F. Gooel, Deceased, Frances Gooel, Executrix, Petitioner v. Commissioner of Internal Revenue, Respondent, 68 T. C. 504 (1977); 1977 U. S. Tax Ct. LEXIS 83

A charitable remainder deduction is disallowed if there is a non-negligible risk that the trust corpus will be exhausted before the charitable remainder is distributed.

Summary

Estate of Gooel involved a testamentary trust where the surviving spouse, Frances, was entitled to receive net income and, if insufficient, corpus to meet a specified annual amount that increased over time. The trust's remainder was designated for charity. The key issue was whether the estate could claim a charitable deduction for the remainder interest. The court held that the risk of the trust corpus being exhausted before Frances' death was not so remote as to be negligible, thus disallowing the deduction. This decision was based on the projected invasion of corpus calculated using a 3. 5% rate of return, as per IRS regulations, and life expectancy tables showing a significant chance that Frances would outlive the trust.

Facts

Elmer Gooel died in 1970, leaving a will that established a trust for his wife, Frances. The trust required the trustee to distribute net income to Frances monthly, and if the income was less than $20,000 annually (increasing by 10% every three years), to invade the corpus to make up the difference. Upon Frances' death, the remaining corpus was to go to charitable organizations. The estate claimed a charitable deduction for the remainder interest, but the IRS disallowed it, arguing that there was a non-negligible risk the corpus would be exhausted before Frances' death.

Procedural History

The estate filed a Federal estate tax return claiming a deduction for the charitable remainder of the trust. The IRS determined a deficiency and disallowed the deduction. The estate petitioned the U. S. Tax Court, which upheld the IRS's position and denied the charitable deduction.

Issue(s)

1. Whether the 3. 5% net rate of return on the trust corpus, as specified in the IRS regulations, was at variance with the facts of this case.
2. Whether the possibility that the entire trust corpus would be invaded for Frances' benefit was so remote as to be negligible, thus allowing a charitable deduction for the remainder interest.

Holding

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1. No, because the estate failed to prove that a higher rate of return was appropriate based on the actual assets of the trust.
2. No, because the probability that the entire corpus would be invaded for Frances' benefit was not so remote as to be negligible, given her life expectancy and the projected depletion of the corpus.

Court's Reasoning

The court applied IRS regulations that required a 3. 5% rate of return for calculating the income of the trust. The estate's argument for a higher rate was rejected due to lack of evidence specific to the trust's assets. The court then calculated the likelihood of corpus invasion using life expectancy tables, concluding that there was a significant chance (10. 93% to 22. 02%) that Frances would outlive the trust, thus exhausting the corpus. The court emphasized that the risk of exhaustion must be "so remote as to be negligible" for a charitable deduction to be allowed. The court also noted that even if a charitable deduction were allowed for a partial remainder, the increased estate tax liability would further reduce the corpus, leading to its earlier exhaustion.

Practical Implications

This decision impacts how estate planners structure trusts with charitable remainders. It underscores the need to carefully consider the risk of corpus invasion when claiming a charitable deduction. Practitioners must use the IRS-prescribed rate of return unless they can prove a different rate is justified by the trust's specific assets. The case also highlights the importance of life expectancy in determining the risk of corpus exhaustion, requiring estate planners to consider the age of the income beneficiary. Subsequent cases have generally followed this approach, emphasizing the need for a negligible risk of corpus exhaustion to claim a charitable deduction.

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