Estate of Nancy F. Crafts, Deceased, William A. Dicus, Personal Representative, Petitioner v. Commissioner of Internal Revenue, Respondent, 74 T. C. 1439 (1980)

A charitable deduction may be allowed for a portion of a trust if the trust is divided postmortem into a wholly charitable portion that meets the requirements of section 4947(a)(1).

Summary

The Estate of Nancy F. Crafts sought a charitable deduction for a trust established by her deceased husband. The trust provided income interests to various beneficiaries, including the Webb Institute, a charity, and a remainder interest split between the Webb Institute and another charity. After the IRS denied the deduction due to non-compliance with section 2055(e), the trustee divided the trust, setting aside 40% for the Webb Institute exclusively. The Tax Court held that section 2055(e) applied but allowed a deduction for the 40% portion under section 2055(e)(3) since it formed a wholly charitable trust by the estate tax return due date. This case highlights the potential for postmortem trust divisions to qualify for charitable deductions under specific conditions.

Facts

John Osborn Crafts established a testamentary trust under his will, naming his wife, Nancy F. Crafts, as the life income beneficiary with an inter vivos general power of appointment over the trust property. Upon Nancy's death, the trust was to provide an annual payment to Osborn Crafts (who predeceased Nancy), 40% of the income to the Webb Institute, and the remainder to other noncharitable beneficiaries. The trust's remainder was to be split 75% to the Webb Institute and 25% to Leicester Junior College. After Nancy's death, the estate requested a charitable deduction, but the IRS denied it due to non-compliance with section 2055(e). The trustee then divided the trust, setting aside 40% of the assets solely for the Webb Institute.

Procedural History

The estate filed a timely estate tax return claiming a charitable deduction for the Webb Institute's interest in the trust. The IRS issued a deficiency notice disallowing the deduction due to the trust's non-compliance with section 2055(e). The estate appealed to the United States Tax Court, arguing that the trust division allowed a deduction under section 2055(e)(3).

Issue(s)

1. Whether section 2055(e) applies to the trust established by John Osborn Crafts and includable in Nancy F. Crafts' estate due to her general power of appointment.
2. If section 2055(e) applies, whether the estate is entitled to a charitable deduction under section 2055(e)(3) for the 40% portion of the trust set aside for the Webb

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Institute.
3. Whether the estate is entitled to an award for attorney's fees and costs.

Holding

1. Yes, because Nancy F. Crafts had the power to modify the trust, making section 2055(e) applicable.
2. Yes, because the trustee's division created a wholly charitable trust for the Webb Institute by the due date of the estate tax return, qualifying for a deduction under section 2055(e)(3).
3. No, because the estate is not entitled to attorney's fees and costs under the applicable legal standards.

Court's Reasoning

The court determined that section 2055(e) applied because Nancy F. Crafts' inter vivos power of appointment over the trust allowed her to modify the charitable interests, as established in *Estate of Sorenson*. However, the court also found that the estate qualified for a deduction under section 2055(e)(3) due to the trustee's postmortem division of the trust, creating a wholly charitable trust for the Webb Institute. The division was authorized by the trust's governing instrument, and the resulting trust met the requirements of section 4947(a)(1) by the due date of the estate tax return. The court emphasized that section 2055(e)(3) is a relief provision intended to benefit charitable organizations and should be liberally construed to further charitable purposes without subverting congressional intent. The court rejected the IRS's arguments that the division did not qualify as a transfer by the decedent or that it required an amendment of the governing instrument, noting that the division was a ministerial act under the original trust provisions.

Practical Implications

This decision allows estates to claim charitable deductions for portions of trusts that are divided postmortem into wholly charitable trusts, provided the division is completed by the estate tax return due date and the resulting trust meets the requirements of section 4947(a)(1). Legal practitioners should consider the potential for such divisions when planning estates with charitable interests, especially in cases where the original trust does not comply with section 2055(e). This ruling may encourage the use of trustee powers to segregate charitable interests, potentially increasing charitable giving. Subsequent cases like *Estate of Edgar* have distinguished this case by emphasizing the importance of creating a separate trust through fiduciary action rather than relying on economic realities. This case also highlights the importance of understanding the interplay between different sections of the tax code when dealing with charitable deductions and trust administration.

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