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ARTICLES
WHEN CHARITABLE GIFTS SOAR ABOVE TWIN TOWERS: A FEDERAL INCOME TAX SOLUTION TO THE PROBLEM OF PUBLICLY SOLICITED SURPLUS DONATIONS RAISED FOR A DESIGNATED CHARITABLE PURPOSE

Johnny Rex Buckles

INTRODUCTION

The horrifying images perhaps will never cease to visit us. The twin towers of the colossal World Trade Center collapse in sequence when airplanes the relative size of sparrows collide with its steely sides in blasts of fire and smoke. The fall of these monuments of commerce, terrible and forceful though it was, proved to be the catalyst for an equally dramatic rise. Literally before the dust from the crumbling towers could settle, the American people, more generous than ever before, responded with a deluge of gifts to charitable organizations soliciting funds to aid those most directly devastated by the dastardly deeds of September 11, 2001. That fellow Americans decided to help the immediate victims of that historically grim day was no surprise. But the magnitude of charitable contributions to donee organizations raising money to aid victims was nothing short of astounding.\(^1\)

\(^1\) According to The New York Times, approximately $2 billion was donated to charitable organizations for the purpose of aiding victims. Stephanie Strom, A Nation Challenged: Charities; Narrowly Drawn Rules Freeze Out Tens of Thousands of Indirect Victims, Report Says, N.Y. Times, April 23, 2002, at A9. For example, the American Red Cross reportedly received in excess of $900 million in donations following September 11. See Editorial, Truth in Charity, Times-Picayune, June 8, 2002, at 6; Red Cross Pitches to Get Specific; Ads to Clarify How Money Will Be Spent, Wash. Post, June 5, 2002, at B1 (reporting that the American Red Cross raised more than $967 million for its Liberty Fund); Jon Yates, Prejudice Also Claimed Victims in Sept. 11's Wake, Chi. Tribune, May 5, 2002, at 1. The September 11th Fund has reportedly collected in excess of $450 million in donations. Id.
Donors gave so liberally that the charitable sector, and those overseeing it, were forced to wrestle with a host of thorny legal issues. First, charitable donees found themselves puzzled and second-guessed over how to apply contributions. The American Red Cross, for example, at one time announced plans to set aside millions of dollars of donations for its Liberty Fund (which was established in response to the events of September 11) to relieve victims of future terrorist attacks and to meet general needs. But the public outcry over this announcement compelled the organization to reverse this decision (which clearly had marred its reputation). Faced with such difficulties, some donee organizations enlisted the office of the New York Attorney General in devising plans for deploying gifts.

Moreover, the gravity of concern with respect to the disposition of funds donated to charities such as the American Red Cross even sparked congressional hearings on the use of charitable contributions made in the wake of September 11. During these hearings, seemingly everyone wielded an opinion on how charitable donees of gifts designated for victims should dispose of donated funds. For example, the Director of Exempt Organizations in the Tax Exempt/Government Entities Division of the Internal Revenue Service (“IRS”) testified before Congress as to the federal income tax problems presented by this charitable outpouring. He received sharp

2. See Diana B. Henriques & David Barstow, Victims’ Funds May Violate U.S. Tax Law, N.Y. Times, Nov. 12, 2001, at B1 (stating that representatives of charity who met after the September 11 attacks to determine how to disburse contributions in accordance with federal income tax laws were “commiserating” and saying, “What are we going to do?”); Celeste Katz, Fire Union Bows, Frees Tower Funds, N.Y. Daily News, July 13, 2002, at 10 (“Blasted for sitting on more than $60 million in donations that flowed in after Sept. 11, the Uniformed Firefighters Association announced plans yesterday to give out most of the money immediately.”).


4. See Truth in Charity, supra note 1: Kasindorf & El Nasser, supra note 3; Red Cross Pitches to Get Specific; Ads to Clarify How Money Will Be Spent, supra note 1.


6. See, e.g., Katz, supra note 2 (stating that the Uniformed Firefighters Association sought assistance from the charities bureau within the office of the attorney general in developing a plan for distributing donations).


8. Id. (statement of Steven Miller, Director, Exempt Organizations, Tax Exempt/Government Entities Division, Internal Revenue Service).
criticism, however, for too narrowly interpreting the range of activities that a tax-exempt charity can perform without jeopardizing its exemption from federal income taxation. It soon became clear to Congress that existing law provided no solution sufficient to satisfy the perceived expectations of the donating public, on the one hand, and the limitations governing charitable donees on the use of donated funds, on the other. Thus, Congress promptly enacted special income tax legislation responding to the events of September 11, which the President signed into law. This legislation was designed in part to allay certain federal income tax concerns of charitable donees in receipt of vast sums of restricted funds.

Although the charitable reaction to the events of September 11 is an extreme example of the receipt by charities of more money than they may deem necessary to fulfill a specified charitable purpose, it is not an isolated phenomenon. A review of case reports reveals that charitable organizations frequently solicit money from the general public for a specified charitable purpose, and later sometimes find that they have received more funds than necessary to accomplish that purpose. What is a charity to do under these circumstances? Charities cannot sensibly hope for an act of Congress every time an unusual turn of events results in their receipt of surplus funds solicited for a designated charitable purpose. A more comprehensive legal solution to this problem is necessary.

Deriving this solution obviously requires a thorough understanding of the legal landscape involving surplus funds donated for a particular charitable purpose. In developing this understanding, one must ponder several questions. Does the law limit the options available to a charity that receives excess funds in response to an appeal identifying a particular charitable need, and if so, how? Do any limitations on the disposition of surplus funds pose difficulties for charitable donees and donors, or on the courts that must resolve the problems associated with surplus funds? Do current reform proposals adequately address any problems identified in this analysis? Is there a better way to reform existing law to improve the disposition of surplus...

9. See, e.g., Lee A. Sheppard, Was the IRS Reversal on Charity Necessary?, 93 Tax Notes 1138 (2001) (criticizing the original position articulated by the IRS in the congressional hearings on the use of charitable contributions made in response to the events of September 11 as “exceedingly narrow”).


11. The legislation provides that payments made by organizations described in section 501(c)(3) of the Internal Revenue Code by reason of the death, injury, wounding or illness of any person resulting from the terrorist attacks of September 11 (or the subsequent anthrax attacks) “shall be treated as related to the purpose or function constituting the basis for such organization’s exemption” in specified circumstances. Id. § 104. Such payments must be “made in good faith using a reasonable and objective formula which is consistently applied.” Id.

12. See infra notes 49-71 and accompanying text.
funds restricted for a particular charitable purpose? This article analyzes these difficult issues and proposes a federal solution to the numerous problems raised.

Part I discusses and analyzes the legal problems associated with a charitable organization's receipt of excess funds resulting from a public appeal for donations to accomplish a particular charitable purpose. Part I.A surveys the relevant issues raised strictly under state law, including the general legal consequences of accepting restricted gifts, and the legal implications of receiving restricted funds when it becomes impossible to accomplish the restricted purposes for which the gifts were made. Part I.B discusses two areas of federal income tax law that must be understood in conducting a thorough analysis under state law of the effect of receiving excess donations from the general public. The first area involves the legal requirements that a charitable entity must satisfy in maintaining its exemption from federal income taxation. The second area involves the element of "finality" that must largely characterize a charitable contribution for which a deduction is claimed.

Part II discusses and analyzes four prominent proposals offered by scholars for reforming the doctrine of cy pres, the most important doctrine of state law governing restricted charitable gifts. Each reform proposal is briefly discussed and then critically examined in the context of publicly solicited gifts restricted for a designated charitable purpose. Part II identifies potential advantages and disadvantages of each proposal, and concludes that no single proposal adequately addresses the unique issues presented under state law and federal income tax law in the context of publicly solicited gifts.

Part III advances an original solution to the problems identified in prior sections of this article. Part III.A briefly identifies the criteria that should characterize any proposal for solving the problem of surplus restricted funds raised through mass appeals by charity. Part III.B then explains and justifies my proposal: amending the Internal Revenue Code to include a new section 170(f)(11). The text of my proposed statutory addition is reproduced in Appendix A. Part III.B discusses the major elements of the proposed amendment, and explains why the proposal survives scrutiny under the criteria identified in Part III.A. I then summarize this article in Part IV.
I. LEGAL PROBLEMS ASSOCIATED WITH EXCESS CHARITABLE CONTRIBUTIONS

A. State Law Considerations

1. General Consequences of Restricted Gifts Under State Law

If a charitable organization accepts a gift pursuant to an instrument (such as a last will and testament or deed of gift) by which the donor restricts the donee's use of gifted funds, the restriction is generally legally binding on the charity, even if under state law the restriction does not give rise to a trust. The state attorney general can sue the charity to enforce the terms of the restriction imposed by the instrument of gift. Indeed, in many circumstances, the attorney general is the sole enforcer of the terms of a charitable gift. Courts often state that as a general rule, a donor has no standing to enforce the terms of a charitable gift, whether given in trust or outright to a corporate charity. A contributor will be granted such standing only


14. See Herzog Found. v. Univ. of Bridgeport, 699 A.2d 995, 997-98 (Conn. 1997); Restatement (Second) of Trusts § 348 cmt. f (1959); Scott, supra note 13, § 348.1.

15. See, e.g., Herzog Found., 699 A.2d at 998 (noting that at common law, a donor who has made a completed charitable contribution, whether as an absolute gift or in trust, had no standing to bring an action to enforce the terms of her gift or trust unless she expressly reserved the right to do so); Warren v. Bd. of Regents, 544 S.E.2d 190, 192-94 (Ga. Ct. App. 2001) (holding that plaintiffs' transfer in trust did not confer standing on them); Smith v. Thompson, 266 Ill. App. 165, 169 (Ill. App. Ct. 1932) (stating that "neither the donor nor his heirs have any standing in court in a proceeding to compel proper execution of the trust"); Baltimore Arts Festival v. Baltimore, 607 A.2d 1, 4 (Md. 1992) (stating that in the absence of an express reservation of rights, a donor may not sue); Hagaman v. Bd. of Educ., 285 A.2d 63, 67 (N.J. Sup. Ct. 1971) (stating that the heirs of a settlor generally cannot enforce a charitable trust); Paterson v. Paterson Gen. Hosp., 235 A.2d 487, 495 (N.J. Super. Ct. Ch. Div. 1967) (stating that the general rule denying standing to donors "is as applicable to the law of charitable corporations as to the law of charitable trusts"); Smithers v. St. Luke's-Roosevelt Hosp.Ctr., 281 A.D.2d 127, 145 (N.Y. App. Div. 2001) (Friedman, J., dissenting) (noting that "a limited standing rule is necessary to protect charitable institutions from vexatious litigation") (citing Alco Gravure v. Knapp Found., 64 N.Y.2d 458, 466 (N.Y. 1985)); McFarland v. Atkins, 594 P.2d 758 (Okla. 1978) (holding that a mere contributor to a charitable fund does not generally have standing unless he has some special interest in the trust, or a reversionary interest in the fund different from that of his fellow contributors); 15 Am. Jur. 2d Charities § 141 (2002) (stating that donors to a broadly supported charitable fund cannot hold trustees accountable for breach of trust without having some special interest in the fund distinct from the interests of fellow contributors); Scott,
Precisely what type of special interest a donor must retain in order to have standing to enforce the terms of a restricted gift is not clear. The theory behind the general rule is that charitable funds are held for the public, and enforcement on behalf of the public rests in the state attorneys general. If the donor lacks any reversionary or other special interest, a donor's interest in enforcing the terms of the gift is purportedly no greater than that of the representative of the general public (the attorney general). Although this general rule has been subject to some judicial erosion and a great deal of scholarly discussion, it remains the prevailing view of the courts.

Supra note 13, § 367.2 (stating that subscribers to a charitable trust cannot sue to modify the purposes of the trust). At least one court, however, has suggested in dicta that a donor may have a right to sue for reimbursement of contributions to a relief fund. See, e.g., Victims v. Funds, Third Parties, and Reeves County, Tex., 715 F. Supp. 178, 181 (W.D. Tex. 1989). See generally Kenneth L. Karst, The Efficiency of the Charitable Dollar: An Unfulfilled State Responsibility, 73 Harv. L. Rev. 433, 445-49 (1960) (discussing enforcement of charitable trusts by donors and founders).

16. See Paterson, 235 A.2d at 495 (citation omitted); George G. Bogert et al., The Law of Trusts and Trustees § 411 (Rev. 2d ed. 1991).

17. Some authorities suggest that such an interest exists not only when the donor explicitly retains a reversionary interest in the gift, but also when she expressly retains the right to redirect the gift for other charitable purposes. See, e.g., Herzog Found., 699 A.2d at 997. That a special interest sufficient to confer standing includes a right to redirect a charitable gift finds support in the monumental work of the late Professor Austin W. Scott of the Harvard Law School. According to Professor Scott, a settlor of a charitable trust has no power to compel or permit a deviation from trust terms, unless she has reserved the power to modify the trust. See Scott, supra note 13, § 367.2 (emphasis added). The power to redirect a restricted charitable gift is essentially the power to modify the terms of the gift. To confer standing on a donor to compel a deviation from trust terms, but to deny standing when a donor seeks to compel compliance with trust terms, would seem senseless.


19. A recent case that defies the conventional rule is Smithers v. St. Luke's-Roosevelt Hosp. Ctr., 281 A.D.2d 127, aff'd, 723 N.Y.S.2d 426 (N.Y. App. Div. 2001). In that case, a recovered alcoholic donated $10 million to St. Luke's-Roosevelt Hospital Center for the establishment of an alcoholism treatment center. Under the terms of gift, the hospital would expand its treatment of alcoholism to include, following five days of detoxification in the hospital, rehabilitation in a therapeutic community located away from the hospital itself. With an initial $1 million installment of the gift, the hospital purchased a building in Manhattan to house the rehabilitation program. The donor died twenty years later, and shortly thereafter the hospital announced plans to move the center into a hospital ward and sell the building. The donor's widow, unsuccessful in her attempts to persuade the hospital to honor the terms of the gift, sued to enjoin the hospital from disbursing the proceeds from the sale of the building and relocating the center. The court held that the express retention of rights was not necessary to confer standing on the donor's widow because the donor, "as the founder of the charity, has standing to appear in court to restrain the diversion of the property donated from the charitable uses for which it was given." Id. at 137 (quoting Mills v. Davison, 35 A. 1072, 1075 (N.J. 1896)). The court reasoned that "[t]he donor of a charitable gift is in a better position than the Attorney General to be vigilant and, if he or she is so inclined, to enforce his or her own intent." Id. at 139.

20. Some commentators have called for a change to the broad rule against donor
That restrictions on charitable gifts imposed by donors are generally enforceable must not be overlooked. In the following section, this article discusses an important doctrine that limits the extent to which the terms of a charitable gift will be enforced. The vast attention devoted to this doctrine in this article should not be read to mask the general rule of the enforcement of restricted charitable gifts. Likewise, that donors are usually denied standing to enforce the terms of charitable gifts must not be understood to mean that charities may disregard restrictions imposed by charitable donors. Donor-imposed restrictions on charitable transfers are legally binding on charities, and therefore they normally must comply with such restrictions upon accepting a restricted gift. Admittedly, the limited resources of the state attorneys general, coupled with the need to combat charitable abuses that are often more serious than diverting contributions from a specified charitable purpose to another charitable end, lead to a practical problem of enforcing restricted gifts to charity. The presence of this practical problem of enforcement, however, does not vitiate the legally binding effect of restricted charitable gifts, nor does it necessarily nullify the theoretical justifications for honoring donor-imposed restrictions.

2. When Restricted Purposes Cannot Be Fulfilled

Notwithstanding that restricted gifts are generally enforceable, if the restricted purpose of the gift can no longer be fulfilled, a court must be petitioned to determine the disposition of the funds. The enforcement. See, e.g., John T. Gaubatz, Grantor Enforcement of Trusts: Standing in One Private Law Setting, 62 N.C. L. Rev. 905 (1984) (arguing that the blanket rule is too broad and donor standing should be permitted in certain situations); see also Geoffrey A. Manne, Agency Costs and the Oversight of Charitable Organizations, 1999 Wis. L. Rev. 227 (1999) (suggesting the creation of private, for-profit monitoring companies to ensure donor intent is fulfilled or a solution based on contract law). On the other hand, courts and commentators have justified the denial of standing to donors on the grounds that allowing suits by small donors would create the potential for too many frivolous actions. See, e.g., In re De Long, 565 N.Y.S.2d 569, 570 (App. Div. 1991) (citations omitted); Karst, supra note 15, at 445-47.

21. See supra notes 13-14 and accompanying text.

22. Id.

23. See Lisa Loftin, Note, Protecting the Charitable Investor: A Rationale for Donor Enforcement of Restricted Gifts, 8 B.U. Pub. Int. L.J. 361, 382-84 (1999); cf. Evelyn Brody, Agents Without Principals: The Economic Convergence of the Nonprofit and For-Profit Organizational Forms, 40 N.Y.L. Sch. L. Rev. 457, 467 n.32 (1996) (citing authorities discussing the limited ability of state attorneys general to oversee charitable organizations); Karst, supra note 15, at 451-52 (discussing the lack of information available to state attorneys general); Manne, supra note 20, at 250-51 (discussing the inadequacy of enforcement of charitable obligations by state attorneys general on account of lack of resources and selective prosecution).

24. Although the trustees of a charitable trust normally petition the court for the application of cy pres, the state attorney general, and in some cases persons with an interest in the trust, can also do so. See Restatement (Second) of Trusts § 399 cmt. f (1959). According to the Restatement, unless either the donor has reserved a power
courts in most jurisdictions will be guided by the doctrine of cy pres. Understanding this doctrine is essential to an informed understanding of the legal options available for directing the disposition of surplus charitable gifts received through public solicitations. This section of the article summarizes the doctrine of cy pres, reviews its applicability to gifts to charitable corporations, and discusses its relevance in the context of mass solicitations for charitable donations.

a. The Doctrine of Cy Pres

Under the doctrine of cy pres, a court may direct the application of charitable trust funds to purposes similar to the original trust purposes when accomplishing the latter is or becomes impossible, impracticable, or illegal, provided that the transferor of the funds has manifested an intent to devote the funds to charitable purposes more general than the frustrated specific purpose of the gift. The court of modification or a state statute otherwise provides, a donor's consent is not required for applying cy pres. See id. § 399 cmt. g.

25. "Cy pres" is an abbreviated expression for the expanded "cy pres comme possible," which is Norman French for "as near as possible." See Bogert, supra note 16, § 431, at 95. The cy pres power may be exercised by the courts "in a great majority of the states," either through their equitable jurisdiction or by state statute. Id. § 433, at 113; see also Scott, supra note 13, § 399.2, at 490 ("In the great majority of states the cy pres doctrine has been accepted."). For an outstanding doctrinal discussion of cy pres, see Domenic P. Aiello & Tracy Adler Craig, Cy Pres: Reformation of the Charitable Trust, 81 Mass. L. Rev. 110 (1996).

26. Closely related to the doctrine of cy pres is the doctrine of deviation (or "equitable deviation"). Under this latter doctrine, a court may direct or authorize a trustee of a charitable trust to deviate from the administrative terms of trust if compliance with the original terms is impossible or illegal, or if compliance with the terms of trust would substantially impede the accomplishment of trust purposes on account of circumstances that the settlor did not foresee. See Restatement (Second) of Trusts § 381 & cmt. a (1959); see, e.g., MacCurdy-Salisbury Educ. Fund v. Killian, 309 A.2d 11, 13-14 (Conn. Super. Ct. 1973) (applying the doctrine of deviation to minimize adverse federal excise tax consequences of accumulating trust income; distinguishing the doctrine of deviation from the doctrine of cy pres). Whereas the doctrine of deviation purports to extend only to administrative terms of trust, the doctrine of cy pres results in deviating from the very purposes of a trust. See Restatement (Second) of Trusts, supra, § 381 cmt. a. As one would expect, distinguishing between "administrative terms" and terms governing trust "purposes" is a difficult, if not illusory, judicial enterprise. See Alex M. Johnson, Jr., Limiting Dead Hand Control of Charitable Trusts: Expanding the Use of the Cy Pres Doctrine, 21 U. Haw. L. Rev. 353, 375-76, 380 (1999); Roger G. Sisson, Relaxing the Dead Hand's Grip: Charitable Efficiency and the Doctrine of Cy Pres, 74 Va. L. Rev. 635, 648 (1988).

27. Although courts sometimes state that cy pres requires them to apply a failed charitable gift as nearly as possible to the original purposes, courts increasingly "seek . . . to frame a scheme which on the whole is best suited to accomplish the general charitable purpose of the donor," even if the court's disposition of funds is not necessarily as similar to the donor's design as that which is theoretically possible. Restatement (Second) of Trusts § 399 cmt. b (1959).

28. See Restatement (Second) of Trusts § 399 (1959); see, e.g., Sharpless v. Medford Monthly Meeting of the Religious Soc'y of Friends, 548 A.2d 1157, 1160
will hear evidence of how the donor, at the time of making the gift, probably would have preferred the funds to be distributed had she known that the original trust purpose would fail. 29

In those states that do not recognize the cy pres doctrine, or when the doctrine, though recognized under state law, is not applied in a particular case, the failure of a charitable trust creates a resulting trust for the settlor or her successors. 30 In other words, in such instances, the person who executes a charitable transfer in trust has a reversionary interest in trust property, which becomes a private possessory interest when the original purposes of the charitable trust have failed.

In those states that recognize the cy pres doctrine, if property is conveyed for a particular charitable purpose which thereafter is accomplished in full, any remaining funds may be applied cy pres, provided that the settlor manifested general charitable intent. 31 This instance of cy pres is sometimes understood as merely one type of "impossibility" of fulfilling the original trust purposes. 32 Cy pres may be applied not only in the case of surplus principal from contributions, 33 but also when income from contributions comprising a permanent fund exceeds that amount which is necessary to accomplish

29. See Restatement (Second) of Trusts § 399 cmt. d (1959) (stating that a court will hear circumstantial evidence bearing on the donor's intent, in addition to the terms of the gift instrument).

30. See Bogert, supra note 16, § 433, at 125; see, e.g., Rohlff v. German Old People's Home, 10 N.W.2d 686, 690-93 (Neb. 1943) (finding no general charitable intent when the testator's will provided for a gift to create a home for elderly Germans in Omaha; stating that the failure of the trust results in a reversion of the funds).

31. See Restatement (Second) of Trusts § 400 (1959); 15 Am. Jur. 2d Charities § 162 (2002). If the donor or settlor lacked general charitable intent, surplus funds will revert to the donor or her heirs. See Holmes v. Welch, 49 N.E.2d 461, 463-64 (Mass. 1943); Restatement (Second) of Trusts § 400 cmt. b (1959); 15 Am. Jur. 2d Charities § 147 (2002).


33. See Restatement (Second) of Trusts § 399 cmt. k (1959) (stating that property given in trust for a purpose that is subsequently accomplished may be subject to cy pres); see, e.g., Jackson v. Phillips, 96 Mass. (14 Allen) 539 (1867) (applying cy pres to a trust fund established to influence the public to oppose the slavery of African-Americans when such purpose was rendered obsolete by the abolition of slavery).
the specified purposes of the fund.\textsuperscript{34} Thus, in \textit{Sharpless v. Medford Monthly Meeting of the Religious Society of Friends},\textsuperscript{35} the court was faced with deciding whether a portion of the income from funds held for the benefit of a local church for the maintenance of its cemeteries could be used for more general church purposes, when the fund consistently generated income in excess of cemetery-related expenses. The court concluded that the doctrine of cy pres applied to the excess income.\textsuperscript{36} The court considered the case before it as one of impossibility, because “there is an impossibility of using the excess income to advance the particular charitable purpose expressed by the donors.”\textsuperscript{37} The more difficult issue was whether the donors who contributed to the fund had manifested general charitable intent beyond the specific desire to maintain grave sites.\textsuperscript{38} The court inferred general charitable intent by reasoning that the donors logically would expect excess income to be used to support the institution (the church) which was expected to maintain the cemetery in the future.\textsuperscript{39} In other words, the donors could not have intended for the cemetery fund to grow while the existence of the church itself became threatened by lack of adequate funding.\textsuperscript{40}

Except in states which have statutorily modified the common-law rule, courts recognizing the cy pres doctrine will apply it only if the settlor had a general or broad charitable intent (i.e., an intent to further charity in general, rather than an intent to further charity \textit{exclusively} through the means specified in the trust instrument).\textsuperscript{41} The mere fact that a donor describes the charitable purpose of the gift with particularity, even if she states that the gift is to be used for no other purpose, does not necessarily establish the absence of general charitable intent.\textsuperscript{42} Similarly, a donor’s narrow description of the charitable class to benefit from her gift does not preclude a finding of general charitable intent.\textsuperscript{43} A donor will be found to have possessed

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\item See Bogert, \textit{supra} note 16, \S 438; Scott, \textit{supra} note 13, \S 400; \textit{see}, \textit{e.g.}, \textit{Estate of Puckett v. Bank of America}, 111 Cal. App. 3d 46, 52-53 (Ct. App. 1980) (applying cy pres to excess income of scholarship fund).
\item \textit{See id.} at 1160.
\item \textit{Id.}
\item \textit{Id.}
\item \textit{Id.}
\item \textit{Id.}
\item \textit{See id.}
\item \textit{See Bogert, \textit{supra} note 16, \S 436.} The requirement that a settlor have general charitable intent has been insightfully criticized. \textit{Id.}
\item \textit{See Restatement (Second) of Trusts} \S 399 cmt. c (1959). The Restatement, however, also states that cy pres does not apply if “the charitable purpose is confined to a particular project, objective, or institution.” \textit{See Restatement (Second) of Trusts} \S 153 (1959). Presumably, whether the charitable purpose is “confined” (within the meaning of section 153 of the Restatement) to the specific purpose is an issue that the court must decide.
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general charitable intent if a court determines that the donor, had she known that following the express terms of the gift would be impossible, would prefer that the gift be employed for a similar charitable purpose, rather than that the gift revert to the donor or her estate.\textsuperscript{44} If the donor's intent is not apparent from the terms of the instrument of gift, her general charitable intent may still be inferred from circumstantial evidence.\textsuperscript{45} As one may immediately suspect, distinguishing between a settlor's particular charitable intent and general charitable intent (if any) is at best an imprecise task.\textsuperscript{46}

\textbf{b. Application to the Law of Charitable Gifts}

The doctrine of cy pres generally applies to gifts to charitable corporations,\textsuperscript{47} although judicial opinions fail to articulate a consistent position on whether a gift to a charitable corporation constitutes a transfer in trust.\textsuperscript{48} For those courts that characterize gifts to charitable corporations as transfers in trust, the doctrine of cy pres obviously applies to such gifts, to the same extent that the doctrine applies to any transfer in trust for charitable purposes under state law.\textsuperscript{49} Other courts, which are more sensitive to the distinction between a charitable corporation and a charitable trust, have declined to find that a gift to a charitable corporation necessarily creates a trust.\textsuperscript{50} Nonetheless, if the doctrine of cy pres generally applies to charitable trusts under state law, such courts also apply the doctrine to gifts to charitable corporations.\textsuperscript{51} Thus, regardless of whether a charitable

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  \item 46. See Scott, supra note 13, § 399.2.
  \item 47. See Restatement (Second) of Trusts § 348 cmt. f (1959); Bogert, supra note 16, § 431, at 105; Scott, supra note 13, § 348.1; see, e.g., MacCurdy-Salisbury Educ. Fund v. Killian, 309 A.2d 11, 14 (Conn. Sup. Ct. 1973); In re Brundrett's Estate, 87 N.Y.S.2d 851, 852-53 (Sur. Ct. 1940).
  \item 48. See Paterson v. Paterson Gen. Hosp., 235 A.2d 487, 489 (N.J. Super. Ct. Ch. Div. 1967) ("To what extent a charitable corporation is to be governed by laws applicable to charitable trusts is a vexed question to which the authorities give irreconcilable answers."); Restatement (Second) of Trusts § 348 cmt. f (1959) (observing that some courts consider restricted gifts to a charitable corporation to be held in trust, whereas other courts do not); Scott, supra note 13, § 348.1 (stating that courts are split in characterizing gifts to charitable corporations as gifts in trust); Note, The Charitable Corporation, 64 Harv. L. Rev. 1168, 1171 (1951) ("Whether or not a charitable corporation should be said to hold the property it administers upon a trust is a question to which the authorities give irreconcilable answers.").
  \item 49. See 15 Am. Jur. 2d Charities § 8 (2002) ("A condition attached to a gift may be considered as tantamount to imposing a trust, and if the condition involves application for charitable purposes, a charitable trust will result.").
  \item 50. See, e.g., St. Joseph's Hosp. v. Bennett, 22 N.E.2d 305, 308 (N.Y. 1939) (stating that a gift to a corporation for a specific charitable purpose is not technically a gift in trust because the "trustee and beneficiary are one").
  \item 51. See, e.g., In re Brooklyn Children's Aid Soc'y, 55 N.Y.S.2d 323, 324 (App. Div.}

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transfer is made in trust or as an outright, restricted gift to a corporation organized for charitable purposes, courts in most states hold that the doctrine of cy pres potentially applies to a gift to a charitable corporation.

c. Application to Funds Received Through Mass Solicitations

A review of the voluminous case law on the subject suggests that express restrictions imposed by donors appear to be the most common type of restrictions from which charities seek to depart under the doctrine of cy pres. What is less obvious is that funds received by a charity may be restricted for a particular charitable purpose even when a donor has not expressly limited the charitable donee’s use of contributions to a specified purpose. This situation arises when a charity solicits funds from the general public and represents that donated funds will be used for a specified purpose of the donee. Case law supports the conclusion that contributions by donors in response to a public solicitation for funds for a specific charitable purpose likely constitute restricted gifts when accepted by the charitable donee.

A representative case is *Kerner v. Thompson*, in which the mayor of Chicago issued a proclamation appealing to the general public for donations to assist victims of the 1927 flood that ravaged the Mississippi Valley. Although nearly $140,000 was collected in the relief effort, only approximately $36,000 was expended to aid flood victims directly. The mayor thereafter transferred the balance of the flood relief fund to a newly formed flood control corporation, which disbursed in excess of $72,000 for purposes other than aiding flood victims directly. In discussing the application of cy pres to such funds, the court first concluded that the purpose of the fund held and

1945) (denying a charitable organization’s request to expend endowment funds for costs of operation because no evidence was offered as to impossibility or impracticability of observing the various terms of the gift); Knickerbocker Hosp. v. Goldstein, 41 N.Y.S.2d 32, 35-36 (Sup. Ct. 1943) (finding the gift was absolute and not in trust, then authorizing cy pres modification permitted by statute); Barnum v. D’Hendecourt, 28 N.Y.S.2d 143, 144 (Sup. Ct. 1941) (“That the bequests were not in trust but were outright gifts does not preclude the application of the cy pres doctrine.”); *In re Lawless’ Will*, 87 N.Y.S.2d 386, 394 (Surr. Ct. 1949) (“The charitable corporation is not bound by all the limitations and rules which apply to a technical trustee. It may not, however, receive a gift made for one purpose and use it for another, unless the Court applying the cy pres doctrine so commands.”) (internal citations omitted)).


53. *Id.* at 111. For an excellent discussion of the 1927 flood and its economic, social, and political consequences, see John M. Barry, *Rising Tide: The Great Mississippi Flood of 1927 and How it Changed America* (1997).

54. *Kerner*, 110 N.E.2d at 111.

55. The remaining funds were ordered in prior proceedings to be transferred to the American Red Cross for assisting future victims of flooding in the Mississippi Valley. *See id.* at 113. This portion of the lower court’s decree was not appealed.
later transferred by the mayor "was controlled by the proclamation and appeal for funds." Emphasizing that the public appeal referred specifically to the need to aid flood victims, the court held that the contributions were restricted for that very purpose, and that the mayor had no authority to expend surplus funds for any other purpose.

Under Kerner v. Thompson and similar authorities, contributions by donors in response to a public solicitation for funds for a specific charitable purpose constitute restricted gifts. Accordingly, if a charitable donee finds itself unable to devote such solicited funds to the specific charitable purpose on account of impossibility, illegality, or impracticability, a court may direct an alternative charitable use of such funds under the doctrine of cy pres if the funds were received from donors who possessed general charitable intent. Of course, the italicized phrase exposes a major difficulty in applying the traditional doctrine of cy pres to publicly solicited funds. The search for general charitable intent proceeds by examining the intent of the individual who donated the funds in question. In the case of funds received through mass solicitations, a court employing the traditional cy pres

56. Id. at 113.
57. Id.; see also id. at 115 ("[T]he object of the fund was determined and fixed by the appeal and the proclamation in 1927.").
58. See, e.g., Am. Nat'l Red Cross v. Felzner Post, Inc., 159 N.E. 771, 772-73 (Ind. App. 1928) (en banc) (stating that public donations raised specifically to aid men and women in the military comprised a "charitable fund to be administered for a specified purpose"); Loch v. Mayer, 100 N.Y.S. 837, 838 (Sup. Ct. 1906) (holding that funds donated to aid victims of a steamboat disaster were impressed with a trust for such purposes when the conduct, and oral and written declarations of all relevant parties, indicated that the donations would be so used); Proctor v. Mathers, 17 Ohio App. 118 (Ohio Ct. App. 1922) (holding that money raised to aid Ohio servicemen during the war was a charitable fund designated for a particular purpose, and deviation from the original purposes was appropriate only under the doctrine of cy pres); cf. Brown v. Concerned Citizens for Sickle Cell Anemia, Inc., 382 N.E.2d 1155, 1158 (Ohio 1978) (holding that funds received through bingo operations must be used for charitable purposes when the public was informed, through newspaper advertisements and an awards ceremony, that funds generated from the activity would benefit a charitable entity). Also of interest is National Foundation v. First National Bank of Catawba County, 288 F.2d 831 (4th Cir. 1961). In this case, the district court had found that funds collected by a local chapter of a national charity for the care and treatment of Catawba County victims of poliomyelitis were impressed with a public trust restricting their use to Catawba County. The district court reasoned that promoters in Catawba County had publicly emphasized that fifty percent of contributions would remain with the local chapter. Id. at 834. The Court of Appeals eliminated this restriction after finding no evidence that any donor whose contribution was accepted had imposed any condition upon her gift. See id. at 834-36. Although the court acknowledged that donors could be held to manifest an intent to restrict donated funds to a particular purpose when responding to special appeals for a specified, limited purpose, the court explained that the appeals at issue were made simply through annual campaigns supporting the general purposes of the national charity. See id. at 836.
59. See Edith L. Fisch, The Cy Pres Doctrine in the United States §§ 6.03-6.03(a) (1950) (discussing the application of the doctrine of cy pres to surplus funds, including those resulting from public donations).
approach would be required to hear evidence of the intent of hundreds, and even thousands, of persons who have contributed some amount of money (however small) to the soliciting charity. Attempting to determine the charitable intent of each and every donor in a massive, geographically expansive fundraising drive could easily prove to be a daunting judicial task.\footnote{60}

In view of this difficulty, it is readily understandable that courts deciding the fate of publicly solicited funds that cannot be used for the intended charitable purpose tend to take some liberty in applying cy pres through the use of presumptions, expressly or implicitly. Unfortunately, however, the decisions of these courts fail to provide charities, or donors, with clear guidance of the probable ultimate disposition of such funds. A survey of a few relevant cases will illustrate the unpredictable approaches of the courts.

Some courts appear to presume that donors who contribute to a fund of a charitable donee seeking broad public support for a designated purpose, such as disaster relief, intend to part permanently with their money; such courts will apply cy pres to excess funds (or funds subject to a restriction that fails for any reason).\footnote{61} For example, in \textit{Kerner v. Thompson}, the appellate court directed the trial court to order the mayor of Chicago to transfer the amount of funds not used to aid the victims of the 1927 Mississippi Valley flood to the American Red Cross for the purpose of aiding future flood victims in the Mississippi Valley (or for some other closely related purpose).\footnote{62} The court plainly reached its decision under the doctrine of cy pres, and even cited authority recognizing that a prerequisite to applying the doctrine is that the donor had a clear intention to devote the gift to a charitable purpose.\footnote{63} The court never directly addressed whether any evidence established the general charitable intent of any specific donor or group of donors. Rather, the court appeared to look solely

\footnote{60. \textit{Cf.} Frank Smithies Rowley, \textit{Disposition of Surplus Funds in Trusts Created by Public Contributions}, 2 U. Cin. L. Rev. 417 (1928) (stating that the proper disposition of surplus funds collected through public subscription depends upon the intent of donors, which is often “vague and uncertain”). Conceivably, a court could devise a proxy for actual donor intent, such as estimating the percentage of donors who have general charitable intent by surveying a sampling of donors. \textit{Cf.} Kralstein v. Comm’r, 38 T.C. 810, 815-19 (1962) (apportioning amounts received by a taxpayer in connection with a testimonial dinner held in his honor between sums intended as gifts and sums included in gross income). Of course, speculating on actual donor intent based upon statistical sampling does not technically comport with existing cy pres doctrine, which looks to the actual intent of each donor.}

\footnote{61. \textit{See} Bogert, \textit{supra} note 16, § 437 (citing numerous cases); \textit{see, e.g., In re Welsh Hosp. Fund}, 1 Ch. 655, 660 (1921), \textit{reprinted in} Bogert, \textit{supra} note 16, at § 431 (holding that funds raised through street collections and personal solicitations to aid the sick and wounded in World War I in excess of those needed to accomplish such purposes need not be returned to the donors; inferring an intent by donors to part irrevocably with their donated funds) (opinion of Lawrence, J.).}


\footnote{63. \textit{See id. at} 114 (citing Bruce v. Maxwell, 143 N.E. 82, 85 (Ill. 1924)).}
to the circumstances surrounding the donations—a broad public appeal for disaster relief—and inferred sub silentio general charitable intent by contributors to the fund.

Other courts, unwilling to apply cy pres to surplus contributions raised for a specified fund, have held or stated in dicta that donors do or may have a right to a pro rata return of any unused balance.\textsuperscript{64} To illustrate, in Sloan v. Robert Jack Post No. 1322, V.F.W.,\textsuperscript{65} committees of two veterans organizations solicited donations for the construction of a building for use by all veterans. However, the two organizations could not agree on the construction of a building that would be used in a manner precisely conforming to representations previously made to donors.\textsuperscript{66} Although the court recognized the validity of the cy pres doctrine, the court stated that the doctrine applies only when “the general objective is never lost sight of.”\textsuperscript{67} According to the court, because the plans contemplated by the organizations varied from representations made to donors, the veterans organizations failed to “perform the implied contract,” and the trust failed.\textsuperscript{68} Therefore, the court was unable to exercise its equitable powers and apply cy pres “when [the] dominant rights of contributors intervened.”\textsuperscript{69} Although the court did not expressly articulate its rationale in terms of presuming that the contributors lacked general charitable intent, such a presumption seems implicit in the court's analysis. The court emphasized the unwillingness of the veterans organizations to implement a plan that conformed precisely to representations made to donors, and characterized modest variations from the plan disclosed to donors as involving substantial alterations.\textsuperscript{70} In other words, the

\textsuperscript{64} See, e.g., Nelson v. Madison Lutheran Hosp. & Sanatorium, 297 N.W. 424, 426-27 (Wis. 1941) (holding cy pres inapplicable to contributions received from subscribers for the construction of a sanatorium when the subscription agreements did not demonstrate general charitable intent; affirming trial court's order to repay contributions to donors); cf. Honaker v. City of Princeton, 25 S.E.2d 772, 774-75 (W. Va. 1943) (finding a resulting trust in favor of the donors pro rata by subscription where the donee had procured equitable interests in land from a large number of donors for an unsuccessful plan to build a college and the largest donor objected to subsequent plans to use the land for an airport). At least one court has approved the application of cy pres to excess funds received in a charitable fundraising drive, but only because excess funds could not be returned to donors, whose identities were unknown. See, e.g., In re Distribution of Funds of Y.M.C.A. War Fund, 25 N.E.2d 956, 960 (Ohio Ct. App. 1939). The position that cy pres should be applied only because donors were unknown is puzzling. If the donors had general charitable intent (a prerequisite to the application of cy pres), funds should not have been returned to them even if their identities were known.

\textsuperscript{65} 239 S.W.2d 591, 591 (Ark. 1951).

\textsuperscript{66} See id. at 592.

\textsuperscript{67} Id. at 593.

\textsuperscript{68} Id.

\textsuperscript{69} Id. The court concluded, however, that the sum of $110 received in connection with a carnival sponsored by one of the organizations was “different from the donations and can not be refunded.” Id.

\textsuperscript{70} See id.
proposed plans violated the donors’ specific charitable intent. As discussed above, under the cy pres doctrine, when the specific charitable intent of a donor cannot be carried out, the trust fails in the absence of a finding that the donor possessed general charitable intent. Thus, the court’s opinion is probably best understood as presuming that donors had only a specific charitable intent to finance a building to be used precisely as represented to them in connection with the solicitation for funds.

Unfortunately, the most authoritative non-judicial icons of trust law do not provide a clear answer as to how best to dispose of restricted funds solicited from the general public when the charitable donee believes that a surplus exists. A comment to the Restatement (Second) of Trusts states as follows:

If property is given to a charitable corporation to be applied to one of the purposes of the corporation, and the purpose is fully accomplished without exhausting the trust property, the court will direct the application of the surplus by the corporation to the other charitable purposes of the corporation, unless the settlor manifested an intention to restrict his gift to the particular purpose which he specified.”

While this statement is doctrinally correct, it is of limited value. When a charitable corporation solicits funds from the general public, one of the most difficult questions is whether, in the words of the Restatement, a donor has “manifested an intention to restrict his gift to the particular purpose which he specified.” The Restatement offers no real guidance in answering this question.

Nor does the Restatement offer greater insight in its comment specifically discussing the disposition of a charitable fund arising from numerous public donations:

If several persons contribute to a fund to be applied to a particular charitable purpose, and the purpose is fully accomplished without exhausting the trust property, and the doctrine of cy pres is not applicable, a resulting trust of the surplus will arise in favor of the contributors who will be entitled to share it in proportion to their contributions.72

As the previous discussion indicates, courts have struggled with how to apply the doctrine of cy pres when numerous donors contribute to a fund for a particular charitable purpose. Yet comment d to section 400 of the Restatement (Second) of Trusts completely dodges the question of when, and to what extent, the doctrine of cy pres applies to such a fund.

One of this country’s eminent trust law scholars, the late Professor George Gleason Bogert, opined that when funds raised through

71. Restatement (Second) of Trusts § 400 cmt. c (1959).
72. Id. § 400 cmt. d (emphasis added); cf. id. § 399 cmt. r.
public gifts fail for any reason (including partial failure attributable to excess funding), "it would seem that the contributors intend to part with their donations irrevocably and expect no return," so that donors have the requisite general intent necessary for the application of cy pres.\textsuperscript{73} Professor Bogert acknowledged, however, that courts have not consistently followed his reasoning,\textsuperscript{74} and he did not provide any further justification for his notion. Thus, both the case law and its leading expositors do little but join us in the quest to satisfactorily dispose of restricted surplus funds solicited by charities from the general public.

B. \textit{Federal Income Tax Law and the Doctrine of Cy Pres}

Most organizations conducting mass appeals for donations are exempt from federal income taxation under section 501(a) of the Internal Revenue Code (sometimes referred to herein as the "Code") as entities which are described in Code section 501(c)(3).\textsuperscript{75} This section describes organizations commonly known simply as "charities." Federal income tax law treats these charitable entities (and contributions thereto) with favor. Notably, the federal income tax laws governing charities, and contributions to charitable entities, can circumscribe the tax-advantaged activity of charitable donors and donees in a way that invites the application of the cy pres doctrine (or at least requires a court to grapple with whether the cy pres doctrine should be applied). How the federal income tax regime intertwines with the doctrine of cy pres is discussed in this section of the article.

Two areas of federal income tax law are relevant to a thorough cy pres analysis of excess donations received from the general public. The first is the set of legal requirements that a charitable entity must satisfy in maintaining exemption from federal income taxation.\textsuperscript{76} The second is the requirement of "finality" that must characterize a deductible charitable contribution.\textsuperscript{77} Each area is discussed in turn, followed by an analysis of how the substantive rules interact with the cy pres doctrine in the context of excess funds raised by charitable donees through public solicitations.

\textsuperscript{73} See Bogert, \textit{supra} note 16, § 437 at 144.
\textsuperscript{74} See id. (citing cases).
\textsuperscript{75} See I.R.C. § 501(a), (c)(3) (West 2001).
\textsuperscript{76} See infra notes 78-79 and accompanying text.
\textsuperscript{77} See infra notes 93-109 and accompanying text.

   a. In General

   Code section 501(c)(3) includes only entities that are both organized and operated exclusively for purposes considered beneficial to the community, such as charitable, educational, religious, or scientific purposes. Further, an organization qualifies under section 501(c)(3) only if "no part of the net earnings [of the organization] inures to the benefit of any private shareholder or individual." This prohibition against the use of a charity's earnings for private gain is known as the private inurement doctrine. It has been described as "the fundamental defining principle" of nonprofit organizations, a characterization that is especially true in the case of charitable nonprofit entities, the income tax exemption of which depends upon not running afoul of the doctrine.

   By its statutory terms, the private inurement doctrine prohibits only the inurement of a charity's net earnings to a "private shareholder or individual." Construed broadly, a "private individual" could include any legal or natural person. Under such an interpretation of the statutory language, an organization would fail the test of Code section 501(c)(3) if at any time its "net earnings" improperly enriched at least one person. Under such an expansive interpretation of the statute, a charitable organization could lose its exemption from federal income taxation simply by committing an isolated mistake in overpaying any provider of goods, services or facilities who in general has very little influence over the organization. Such a result would seem unduly punitive, and even irrational. Thus, quite reasonably, the phrase

79. I.R.C. § 501(c)(3). A transaction that violates the prohibition against private inurement also likely gives rise to excise taxes under section 4958 of the Internal Revenue Code. See I.R.C. § 4958 (West 2001). Code section 4958 imposes excise taxes on "excess benefit transactions" (generally, transactions in which an applicable tax-exempt organization conveys a benefit on a "disqualified person" that is greater than the consideration received by the tax-exempt organization). Id. In general, the taxes are imposed upon managers of organizations who intentionally participate in the decision to enter into the transaction, and upon the disqualified persons involved. Id. A disqualified person includes, in relevant part, any person who can exercise substantial influence over the affairs of the organization. See generally id.
81. Id. at 427.
82. The phrase "net earnings" is misleading, for private inurement may be found even when the charity does not make a distribution of profits to a private person. The private inurement doctrine essentially condemns transactions between a charitable organization and a controlling insider whenever the charitable entity receives less than fair consideration for what it provides the private individual. See id. at 428-31 (discussing the essence of private inurement and the meaning of "net earnings").
"private shareholder or individual" has been interpreted more narrowly by the IRS and the courts than is theoretically compelled by the statutory language. Only if a person has a "personal and private interest in the activities of the organization" will she be deemed a "private shareholder or individual." Case law supports the conclusion that a person generally has such an interest only if she can exert control over the charity's operations, although whether such control must be formal is not a settled issue.

Under this approach, of course, the class of people who may receive benefits from a charity in violation of the private inurement doctrine is to some degree limited, for the number of persons able to control the operations of a charitable organization is finite. Consequently, the prohibition against private inurement of net earnings is not implicated in many transactions that bestow benefits upon non-charitable persons. Nonetheless, a charity that confers a benefit on someone who is not a "private shareholder or individual" may still forfeit its income tax exemption. This conclusion follows from a doctrine related to, but theoretically distinct from, the private inurement prohibition. The doctrine is the prohibition against unlawful private benefit (the "private benefit doctrine").

The Treasury Regulations establish that an "organization is not organized or operated exclusively for purposes [described in Code section 501(c)(3)] unless it serves a public rather than a private interest." In interpreting this provision of the Treasury regulations, the Tax Court has held that an organization fails to qualify for income tax exemption when it benefits private interests more than insubstantially, relative to the general public benefits conferred.

83. See Treas. Reg. § 1.501(a)-1(c) (2002).
84. Compare United Cancer Council, Inc. v. Comm'r of Internal Revenue, 165 F.3d 1173, 1178-79 (7th Cir. 1999) (finding no private inurement when a professional fundraising firm that dominated a charitable entity could not formally control it), with Variety Club Tent No. 6 Charities, Inc. v. Comm'r, 74 T.C.M. (CCH) 1485, 1493 (1997) (finding that a person had the requisite private interest in a charity when he had a significant voice in its operations and formal and informal control over much of its income). The IRS's concept of the degree of "control" necessary to render a person a "private shareholder or individual" with respect to a charity appears to have evolved somewhat in recent years. To illustrate, in General Counsel Memorandum 39498 (Jan. 28, 1986), the IRS opined that physicians have a personal and private interest in the activities of a hospital (i.e., that physicians constitute "private shareholders or individuals") if they are employees of the hospital or have a close working relationship with the hospital (such as staff physicians). The IRS now appears to recognize that a staff physician is not necessarily a "private shareholder or individual" with respect to an exempt hospital if she does not have substantial influence over its affairs. See, e.g., Rev. Rul. 97-21, 1997-1 C.B. 121. See generally Hopkins, supra note 80, § 19.3, at 431-35 (discussing who qualifies as an "insider" for purposes of the prohibition against private inurement).
85. See generally Hopkins, supra note 80, at 460-62 (discussing the private benefit doctrine and observing that the doctrine is distinct from, yet to some extent subsumes, the private inurement doctrine).
thereby.\textsuperscript{87} For obvious reasons, the test can hardly be applied with great objectivity. Even more subjective is the approach of the IRS, which considers a private benefit “incidental” only if it is incidental in both a quantitative and a qualitative sense.\textsuperscript{88} According to the IRS, a private benefit is quantitatively incidental only if it is not substantial once the overall public benefit conferred by the activity is considered. A benefit is qualitatively incidental only if the benefit is a necessary concomitant of the activity which benefits the public at large (i.e., the benefit to the public cannot be achieved without benefiting certain private individuals).\textsuperscript{89}

Thus, an organization that advances purposes that are plainly charitable may forfeit its income tax exemption by conferring certain benefits upon private parties. Under the private inurement doctrine, the charity’s federal income tax exemption is jeopardized if it confers any net benefit upon a person who exercises control over its operations. Under the private benefit doctrine, a charitable organization will sacrifice its exemption if it confers a benefit upon any private party (even someone who lacks an ongoing relationship with the charity) that, relative to the overall public benefits provided by the charity, is not merely incidental.

b. Application to Mass Appeals for Restricted Charitable Gifts

A charitable donee that receives public donations restricted for a charitable purpose may risk its federal income tax exemption under the private benefit doctrine (or, less likely, under the private inurement doctrine) in some circumstances. The most readily envisaged scenario involves a geographically broad, well-publicized campaign to raise funds to provide direct financial assistance to a

\textsuperscript{87} See, e.g., Am. Campaign Acad. v. Comm’r of Internal Revenue, 92 T.C. 1053, 1067-79 (1989) (holding that an organization that trained people for careers in political campaigning substantially benefited private interests (the Republican party and its candidates) and therefore failed to qualify as a tax-exempt educational organization).

\textsuperscript{88} See Gen. Couns. Mem. 37789 (Dec. 18, 1978). In this General Counsel Memorandum, the IRS opined that the leasing of land by a hospital to members of its medical staff for $1.00 per year would give rise to more than incidental private benefit when the land could have been leased to the doctors at fair market value, and the benefit to the doctors was almost as great as the benefit to the public. Similarly, in General Counsel Memorandum 39498, discussed supra note 84, the IRS concluded that a salary income guarantee may fail scrutiny under the private benefit doctrine. In applying the “qualitative” test of incidental private benefit, the IRS lacked sufficient facts to determine whether an income guarantee was the sole means that a hospital could use to recruit a physician practicing in a field of medical specialization in order to enable the hospital to provide excellent health care services. Further, because the subsidies to the recruited physician were not capped (except by a total income guarantee), the contemplated financial incentives may not have been quantitatively incidental to the hospital’s attempt to further exempt purposes.

\textsuperscript{89} See id.
limited number of people who have suffered some catastrophe (whether a flood, fire, earthquake, tornado, or act of terrorism). Certainly, aiding the victims of disasters is a charitable purpose. Moreover, providing direct financial assistance (i.e., money) to victims is often entirely appropriate. However, as with all activities that further a charitable purpose, relief must not be conducted in a manner that runs afoul of the private benefit doctrine.

Consider the delivery of aid to the victims, and the surviving members of the families of victims, of the September 11 terrorist attacks. Literally billions of dollars have been raised by charitable organizations to assist these victims. Certainly, providing numerous forms of aid to those who have suffered so directly from this tragedy (including, for example, shelter, food, medical care, counseling services, and in some cases direct financial aid) is a charitable activity promoting extensive public good. However, after basic needs have been met, and funds to provide for the victims’ anticipated future needs have been set aside, expending more and more dollars for the benefit of the members of this limited charitable class will produce a proportionately lower increase in public benefit. At some point, albeit one that is not identified with ease, we must acknowledge that additional aid provided to or for the benefit of the members of this charitable class will very likely benefit them as individuals more than the community at large, especially if such aid is primarily financial. Had special legislation not been enacted, a charity that devotes increasingly greater resources to or for the benefit of the victims of the tragic acts of terrorism at some point likely would have jeopardized its federal income tax exemption under the private benefit doctrine.

Admittedly, the outpouring of charitable gifts following September 11 was extraordinary, as was the special tax legislation enacted in response to the unusual events. It is not at all inconceivable, however, that the same private benefit problem has arisen (and will arise) on a smaller scale on the heels of other disasters receiving less global (and less congressional) attention. The potential for the problem is real, for example, whenever a rather small community is devastated by a calamity that is publicized extensively. Further, the potential for private benefit seems especially acute when the tragedy results in harm which is not easily quantified, as in the case of a local epidemic that affects people who are not of income-earning age. Generous, empathetic people may desire to contribute money to organizations serving the survivors of such a tragedy, but in such cases money can help only to a limited degree. If the organization simply transfers contributed funds to the survivors, or even provides a wide range of services in kind to them, without considering the true community

90. See supra note 11.
benefit in doing so, once again the organization may benefit private persons more than incidentally, thereby jeopardizing its federal income tax exemption.\footnote{91} The potential for excessive private benefit is not limited to public appeals for victims of disasters. The problem may arise anytime a charity binds itself in public solicitations to use donated funds for a restricted purpose that necessarily confers a significant benefit on a private person. For example, consider a small, underfunded parochial school that has been unable to attract proficient teachers. In an effort to attract outstanding instructors, the school conducts an intense fundraising campaign targeting all state residents who are members of the religious denomination with which the school is affiliated. The school represents that contributions will be used to endow five (and only five) teaching chairs, and all income from the endowment will be distributed annually to the five teachers hired by the school. Endowing a chair in the educational profession is commonplace, and normally results in no excessive private benefit; the teacher holding the endowed chair is merely the necessary means for accomplishing the end of promoting the education of students.\footnote{92} Let us assume, however, that the school’s campaign is wildly successful, and the income from the endowment results in the receipt by each of the five teachers of a salary that is three times greater than the market rate. On these facts, one must inquire as to whether complying with the restriction would confer a private benefit that is more than incidental. Determining whether the benefit is quantitatively incidental would be difficult. At a minimum, however, if the evidence established that the school could have hired teachers some other way (such as by paying them a salary merely at the high end of the market, or offering less costly employee benefits), or that the students’ instruction could have been enhanced sufficiently by some other means, the organization’s activities would likely be found to confer a private benefit that is not qualitatively incidental.

It is also conceivable that public solicitations for a restricted charitable purpose could result in private inurement of the donee’s net earnings. Private inurement would arise if persons with some degree of control over the organization ultimately benefit from contributed funds without furnishing adequate consideration therefor. An organization should be able to avoid this problem, however, by not disbursing funds to or for those who exercise control over the organization. Thus, the greater concern for exempt organizations

\footnote{91. This observation is more than a purely hypothetical problem concocted by an overzealous academic. Indeed, the IRS’s official publication on disaster relief is sensitive to the issues raised in this discussion. \textit{See} I.R.S. Publication 3833, Disaster Relief: Providing Assistance Through Charitable Organizations 5-9 (2002).}

\footnote{92. \textit{See} Hopkins, \textit{supra} note 80, at 111.}
soliciting funds for a restricted purpose is probably the private benefit doctrine.

2. Qualifying for the Charitable Contribution Deduction

a. In General

Federal income tax law extends favorable treatment not only to the income of charitable entities described in Code section 501(c)(3), but also to taxpayers who make contributions to such entities. Subject to certain limitations, section 170(a) of the Code allows a deduction for any “charitable contribution” made by a taxpayer within a taxable year. A charitable contribution is “a contribution or gift to or for the use of” designated entities, including “a corporation, trust, or community chest, fund, or foundation... organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes” that meets certain requirements governing organizations described in Code section 501(c)(3).

An important element of a deductible “gift” is non-conditionality (or finality), although such non-conditionality is determined under a standard of improbability, rather than impossibility. Under the Treasury regulations, a gift is not deductible if the transfer “is dependent upon the performance of some act or the happening of a precedent event” before the gift is effective, unless “the possibility that the charitable transfer will not become effective is so remote as to be negligible.” Thus, a deduction may not be available to a taxpayer whose gift requires the charity to perform some act before receiving outright ownership of the property to be transferred. Similarly, a taxpayer who gives property to a charity subject to a condition subsequent (i.e., the subsequent performance of an act or occurrence of an event) may claim a charitable contribution deduction if the possibility that the condition subsequent will occur “appears on the date of the gift to be so remote as to be negligible.” Under the regulations, the obvious practical difficulty is determining whether the possibility of divestment of a charitable gift (or failure of such a gift to vest in the first instance) is “so remote as to be negligible,” particularly because such determination must be made at the time of the transfer to the charity. The case law and administrative rulings

94. Id. § 170(c)(2).
96. Id. The regulations illustrate this rule with a case in which a taxpayer donates land to a city to be used as a public park. Id.
97. Id.
98. See, e.g., 885 Inv. Co. v. Comm'r of Internal Revenue, 95 T.C. 156, 161-62 (1990) (holding that partners could not deduct their distributive share of a
of the IRS interpreting this rule illustrate its application.

For example, in *Briggs v. Commissioner of Internal Revenue,* the taxpayer donated land to a charitable corporation created to benefit Native Americans. An agreement between the parties required the property to be developed for use as a cultural, educational, and medical center, and imposed various other conditions and restrictions. Efforts to develop the property for its intended charitable use failed, and it was later transferred to another charity pursuant to an amended agreement. After concluding that the restrictions constituted conditions subsequent under state law (and therefore the taxpayer retained a right of reentry), the Tax Court held that the taxpayer was not entitled to a charitable contribution deduction. The court determined that the possibility that the conditions subsequent would occur did not appear on the date of the gift to be "so remote as to be negligible" within the meaning of the Treasury regulations. The court relied on precedent interpreting identical language in the estate tax regulations to refer to "a chance which persons generally would disregard as so highly improbable that it might be ignored with reasonable safety in undertaking a serious business transaction." According to the Tax Court, as of the date of partnership's donations of land to a city because such conveyances were subject to a condition (the development of the land as a scenic corridor), the occurrence of which was not so remote as to be negligible); Stotler v. Comm'r, 53 T.C.M. (CCH) 973, 979 (1987) (holding that there was no significant likelihood that a scenic easement donated to a governmental unit would revert to the donors pursuant to a contractual provision triggered upon condemnation of the subject property due to enlargement of a dam when (i) plans for such enlargement of the dam had never been approved, (ii) other alternatives had been considered, and (iii) enlargement of the dam would result in the condemnation of less than one-half of one percent of the property); see also Gagne v. Comm'r, 16 T.C. 498, 502-03 (1951) (holding that a charitable contribution made subject to the charitable donee's compliance with certain conditions was deductible in the year that the donee agreed to the conditions and accepted the gift). See, e.g., Rev. Rul. 79-249, 1979-2 C.B. 104 (holding that contributions to a political subdivision for a building project are not deductible until the donee transfers the sums to a building fund because the donee informed donors that all contributions would be refunded if sufficient funds were not raised; reasoning that such donations are subject to a precedent event, and the possibility that the charitable transfers will not become effective is not so remote as to be negligible).
the gift, there was a real possibility that the conditions specified in the
agreement might not be met.\textsuperscript{107} In relevant part, the court observed
that the taxpayer had not provided money for the construction of the
center, no financing was readily available, the administrators of the
charitable donee lacked experience obtaining funding, and thus the
center might never exist.\textsuperscript{108} Accordingly, "the possibility that the
property would not be used for the establishment of the center was
not so remote as to be negligible."\textsuperscript{109}

b. Application to Mass Appeals for Restricted Charitable Gifts

Let us assume that a tax-exempt charitable organization solicits
contributions from the general public and represents that all
donations will be returned to the donors if sufficient funds are not
received for accomplishing the specific charitable project identified by
the donee in advance of receiving donations. Does subjecting the
continued receipt of donations by the charity to this condition, which
is based upon the amount of funds collected, raise an issue of
deductibility under the Treasury regulation discussed above? More
precisely, are donors responding to the mass solicitation entitled to a
charitable contribution deduction for the year in which they transfer
funds to the charity because "the possibility that the charitable
transfer will not become effective is so remote as to be negligible,"
within the meaning of the regulations? Administrative authority
suggests that a deduction is not necessarily proper in the first year that
a donation is made.

In Revenue Ruling 79-249,\textsuperscript{110} a municipal corporation sought
contributions from the public to finance ten percent of its costs in
constructing a new high school building. The corporation would hold
contributions until it had received sufficient gifts, at which time the
money would be transferred to a construction fund.\textsuperscript{111} The
corporation represented that if the contributions were not ultimately
sufficient, it would return the funds to the donors.\textsuperscript{112} If the
contributions were more than sufficient, the corporation would retain
such excess for general school purposes.\textsuperscript{113} The IRS ruled that
deductions for charitable contributions were allowable to donors only
disregarding as so highly improbable and remote as to be lacking in reason and
substance." See \textit{id.} at 657 (citing Estate of Woodworth v. Comm'r, 47 T.C. 193, 196
(1966)).

\textsuperscript{107} \textit{id.}
\textsuperscript{108} \textit{id.}
\textsuperscript{109} \textit{id.} The court further opined that other conditions caused the gift to fail under
the Treasury regulations. See \textit{id.} at 657-59.
\textsuperscript{110} 1979-2 C.B. 104.
\textsuperscript{111} \textit{id.}
\textsuperscript{112} \textit{id.}
\textsuperscript{113} \textit{id.}
when the donee transferred the contributions to the construction fund or retained them for general school purposes.\textsuperscript{114} The IRS reasoned that the building would be constructed only if the donee raised a specific amount of contributions, and concluded that as of the date of the gifts, an effective transfer for charitable purposes depended upon the performance of an act or the happening of a precedent event.\textsuperscript{115} The IRS further observed that the return of donations depended only upon whether sufficient donations were received.\textsuperscript{116} Accordingly, the possibility that the charitable transfer would not become effective was not so remote as to be negligible within the meaning of the Treasury regulations.\textsuperscript{117}

Revenue Ruling 79-249 involved a condition precedent (obtaining sufficient funding), the possibility of non-occurrence of which was not so remote as to be negligible.\textsuperscript{118} One can easily imagine a similar situation involving excess funding. Consider a tax-exempt charitable organization that solicits contributions from the general public for a restricted purpose, and represents that donations will be returned to the extent that they exceed the amount of funds needed to accomplish a specific charitable project identified by the donee in advance of receiving donations. In this case, the charitable donee and all donors rightly believe that donated funds will be accepted by the charity, at least some of the contributions will be used for charitable purposes, and only if the charity ultimately receives “too much money” will some contributions be returned. The problem is that this scenario involves a contingency similar to that in Revenue Ruling 79-249. Although the contingency in this scenario would probably best be characterized as a condition subsequent, such characterization is of no import under the Treasury regulations.\textsuperscript{119} What matters is that in this hypothetical, as in Revenue Ruling 79-249, whether any particular taxpayer-donor’s contribution ultimately will be used by the charitable donee (or instead returned to the donor) depends upon the amount of giving by other donors. In other words, whether a taxpayer-donor’s contribution will remain with the donee or instead be returned to the donor depends upon a “contingency”—the receipt

\footnotesize{\textsuperscript{114} See id. at 105.}
\footnotesize{\textsuperscript{115} Id.}
\footnotesize{\textsuperscript{116} Id.}
\footnotesize{\textsuperscript{117} See id.}
\footnotesize{\textsuperscript{118} Id.}
\footnotesize{\textsuperscript{119} In Revenue Ruling 72-194, 1972-1 C.B. 94, the IRS ruled that sums advanced by sponsors solicited by a state agency to pay any deficit incurred in the running of a steeplechase race to promote tourism are deductible as charitable contributions only to the extent used by the donee. The IRS stated that no portion of the advance constituted a “payment” until the net amount to which the state was entitled had been definitively determined by a final accounting. The ruling appears distinguishable from the hypothetical raised in the text, insofar as in the ruling, the parties did not agree that advanced sums would be owned by the donee prior to a determination of the donee’s deficit.}
by the charitable donee of contributions exceeding the amount necessary to accomplish a specified charitable purpose. In Revenue Ruling 79-249, the IRS ruled that a condition that depended upon the amount of giving by other donors resulted in disallowance of a charitable contribution deduction until the use of donated funds was finally determined. 120 Similarly, under the facts of the hypothetical raised in the text, the IRS (and a court) could find that the likelihood that a taxpayer's donation would be returned to her on account of excess funding is not "so remote as to be negligible" within the meaning of the Treasury regulations. If so, until a charity takes some action to preclude the return of the donated funds to the donor, she would not be entitled to claim a charitable contribution deduction for her transfer to charity.

If charities soliciting funds from the general public for a restricted purpose never return excess funds to donors, the problem raised in the previous hypothetical would have only academic appeal. But as the case law and media reports illustrate, the prospect that a charity may be pressured or even required to return excess donations to donors is grounded in reality. 121 Given this reality, under the Treasury regulations and Revenue Ruling 79-249, a taxpayer is not necessarily entitled to a deduction for a charitable contribution made in response to a public appeal for funds for a designated purpose that reasonably requires finite funding. A deduction is proper only if the probability of the condition giving rise to the return of the taxpayer's donation is "so remote as to be negligible." 122 If the charity's public appeal for funds is highly publicized, as in the case of solicitations for the relief of the victims of the attacks of September 11, or if the price tag of a specified charitable project is low relative to the pool of probable donors and other sources of compensation for losses (such as private insurance), the probability of the contingency giving rise to a return of the taxpayer's donation (i.e., the probability of excess charitable funding) may very well not be "so remote as to be negligible."

One should ask whether there is any real problem with the claiming of a charitable contribution deduction by a taxpayer, notwithstanding a substantial possibility that a contingency may occur that requires the

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121. See, e.g., Corey Kilgannon, Red Cross Offers To Refund Gifts for Sept. 11, N.Y. Times, Nov. 12, 2001, at B10 (reporting that the American Red Cross announced that it would return donations to contributors requesting refunds of their gifts); Cheryl Wetzstein, Watchdog Urges Accounting for all Sept. 11 Charity Funds; Says Groups Have Duty to Honor Donors or Refund Gifts, Wash. Times, Oct. 30, 2001, at A10 ("Charities... have an obligation to honor donors' wishes, and if they can't spend money raised for Sept. 11 relief on that issue, they should consider giving it back, a charity watchdog said yesterday."); cf. Wheaton College Agrees to Return Gifts to Donors Who Object to Co-Education, Chron. Higher Educ., June 15, 1988, at A1 (reporting that Wheaton College offered to return contributions to donors dissatisfied with proposed changes to its gender-based admissions policies).
122. See supra note 95 and accompanying text.
return of the contribution to the taxpayer. The argument that claiming such a deduction is not a substantial problem would likely rely on the tax benefit rule. In basic terms, under the tax benefit rule, a taxpayer who recovers an item deducted in a previous year must include the recovered item in income in the year of its recovery unless the deduction did not decrease the taxpayer's federal income tax liability in the previous year. Thus, a taxpayer who in a previous year wrongfully claims a deduction for a charitable contribution subject to a material contingency must report the item as income in a later year if and when the contingency occurs and the contribution is returned to the taxpayer.

The most important response to this argument is that the tax benefit rule ignores the time value of money. For example, a taxpayer who claims a charitable contribution deduction of $1,000 in year 1 (thereby removing $1,000 of gross income from taxation in year 1) and then recovers $1,000 in income in year 2 is in the same position as a taxpayer who is allowed simply to defer recognition of $1,000 of year 1 income until year 2. The value of deferring income tax liability is now so pervasively acknowledged that it merely need be noted herein. Suffice it to say that a taxpayer who achieves this benefit of deferral is receiving an interest-free loan from the government on his income tax liability attributable to the deferred item. Because of the time value of money, a taxpayer who wrongfully deducts a charitable contribution in one year and then recovers the item in a subsequent year is in a better position than a taxpayer who never claimed the deduction in the first place. Correspondingly, the government is in a worse position in the former case than in the latter. Thus, the tax benefit rule does not "solve" the problem created when a taxpayer

123. See, e.g., Hillsboro Nat'l Bank v. Comm'r, 460 U.S. 370, 383 (1983) (holding that under the tax benefit rule, a deduction previously taken must be recovered in income whenever a subsequent event occurs that is "fundamentally inconsistent with the premise on which the deduction was initially based"). For a thorough overview of the tax benefit rule, see Boris I. Bittker & Lawrence Lokken, 1 Federal Taxation of Income, Estates and Gifts § 5.7, at 5-42 to 5-64 (3d ed. 1999). The current statutory embodiment of the tax benefit rule is Code section 111. See I.R.C. § 111(a) (West 2001) (stating that gross income does not include income attributable to the recovery of a previously deducted amount "to the extent such amount did not reduce the amount of tax imposed by this chapter").

124. See, e.g., 885 Inv. Co. v. Comm'r, 95 T.C. 156, 164-68 (1990) (applying the tax benefit rule in a case to which an appeal would lie in the United States Court of Appeals for the Ninth Circuit). Although the Tax Court historically has not applied the tax benefit rule when the original deduction was erroneous, see id. at 165, several United States Courts of Appeal have done so, and the Tax Court must follow their lead in deciding cases appealable to those courts. See id. at 166.

125. This point, which is apparent from an examination of the authorities discussing the tax benefit rule, has been observed by others. See, e.g., Steven J. Willis, The Tax Benefit Rule: A Different View and a Unified Theory of Error Correction, 42 Fla. L. Rev. 575, 593-94 (1990).
erroneously deducts a charitable contribution subject to a condition requiring the later recovery of the item in income.


The foregoing discussion has laid the foundation for exploring the frontiers of the cy pres doctrine, and the common law of restricted gifts more generally, in relationship to the federal income tax laws discussed above. These frontiers will be explored in responding to the following questions:

(1) In a state that recognizes the cy pres doctrine, when, if at all, may a court authorize the charitable donee to depart from the terms of restricted gifts solicited from the public if literal compliance with such terms would jeopardize the donee’s exemption from federal income taxation?

(2) In a state that recognizes the cy pres doctrine, when, if at all, does a charity jeopardize its federal income tax exemption by returning publicly solicited restricted donations to donors without having obtained direction from a court to do so?

(3) In a state that does not recognize cy pres, may a charitable donee return publicly solicited restricted gifts to donors when complying with such terms would jeopardize the donee’s exemption from federal income taxation?

(4) Under what circumstances are contributors to a charitable organization that publicly solicited funds for a restricted charitable purpose not entitled to a charitable contribution deduction under Code section 170?

This section addresses each question in turn.

To facilitate analysis, these questions will be discussed in the context of a common fact pattern. Assume a hurricane, taking a course that narrowly bypasses several major metropolitan coastal cities, destroys a very small town on the Eastern seaboard. Grateful that they were spared from the hurricane’s fury, and eager to extend a helping hand to the people of the small town who weathered the storm, thousands of city dwellers generously respond to a local charity’s plea for assistance. The charitable donee represented to the public in all of its solicitations that all donations would be used exclusively to provide direct financial assistance to the victims of the storm. Accordingly, under the case law discussed above, the prevailing view is that the charitable donee holds such donated funds subject to the legal restriction that they be used as promised. Let us further assume that donations were so extensive that the charity received more than enough money to meet the emergency needs of the victims, and to rebuild adequate housing and business establishments for them. The charity is thus faced with deciding what
to do with the surplus funds. Let us also assume that transferring the surplus directly to the victims would significantly enhance their pre-hurricane standard of living. Because of the significant private benefit associated with transferring the surplus funds to the victims, it is quite conceivable that any such transfer would cause the local charity to forfeit its federal income tax exemption. So what can the charity do?

a. The First Question: When Does Cy Pres Apply?

Turning to the first question raised above, we must consider the applicability of the cy pres doctrine to the hypothetical facts. Specifically, in a jurisdiction that recognizes the cy pres doctrine, can our hypothetical charity petition a court to authorize deviation from the terms of the restricted gifts solicited from the public because literal compliance with such terms would jeopardize the donee’s exemption from federal income taxation? It will be recalled that under the cy pres doctrine, a court may direct the application of charitable trust funds to purposes similar to the original trust purposes when accomplishing the latter is or becomes impossible, impracticable, or illegal, provided that the transferor of the funds has manifested an intent to devote the fund to charitable purposes more general than the frustrated specific purpose of the gift. Under the hypothetical facts, the case law supports the conclusion that the funds received by the charity in response to its solicitations probably would constitute restricted gifts. Strictly speaking, compliance with the terms of the restricted gifts described in the hypothetical would not necessarily be “illegal.” Generally, the requirements of Code section 501(c)(3) (such as not running afoul of the private benefit doctrine or the private inurement doctrine) are not mandated for any organization. Rather, they are requisites for obtaining and maintaining federal income tax exemption. An organization may operate “legally” and still fail to satisfy Code section 501(c)(3), just as a person may legally make an expenditure that fails to qualify for an income tax deduction. In other words, it is conceivable that a charity may “legally” engage in activities that result in the loss of its federal income tax exemption. Moreover, compliance with the

128. See, e.g., Bob Jones Univ. v. United States, 461 U.S. 574, 592-605 (1983) (holding that a private school that denied admissions to, and expelled, students who engaged in or advocated interracial dating was not entitled to federal income tax exemption because such actions violated established national public policy against numerous forms of racial discrimination in education).
129. On the other hand, one could argue that engaging in activities that result in the loss of a charitable organization’s income tax exemption is “illegal” if either (i) the action is contrary to the charitable organization’s articles of incorporation (or other governing document), or (ii) the governing board’s authorization of the action constitutes a breach of their fiduciary duties to the corporation. Because cy pres
terms of the restricted gifts described in the hypothetical would not technically be "impossible."130 The charitable donee is capable of identifying every victim and transferring to each a share of all donations raised.

A stronger case supporting the potential application of cy pres to the facts raised in the hypothetical would rest on grounds of impracticability. As a threshold matter, it should be recalled that cases such as *Kerner v. Thompson*131 and *Sharpless v. Medford Monthly Meeting of the Religious Society of Friends*132 have applied cy pres to funds considered "excessive" quite apart from any federal income tax ramifications to the charitable donees.133 The problem of relying on these cases in situations like that raised in the hypothetical is the difficulty of determining whether the restrictions governing the publicly solicited gifts imply some level of gifts above which a court will be able to find the existence of "excess." If donors really intend that their contributions be transferred to or for the benefit of the victims of the small coastal town in our hypothetical, even if the victims thereby become wealthy, a court would be hard-pressed to find that any such funds constitute "surplus" apart from federal income tax considerations. I believe that a sensible approach for guiding a court in determining whether cy pres applies is to factor the federal income tax implications to the charitable donee into the analysis. Many, if not most, charitable donees that engage in public solicitations for funds rely heavily for their survival not only upon their own exemption from federal income taxes, but also upon the deductibility under Code section 170 of contributions made to them. A donee that violates the public benefit doctrine not only forfeits its income tax exemption, but also loses the benefit of receiving tax-deductible donations.134 For many charities, failing to qualify under

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130. Some charitable donees may have a credible argument that cy pres should apply on grounds of impossibility when compliance with the terms of a restricted gift would confer excessive private benefit. This argument would be available to a charitable organization having a governing organizational document (i.e., articles of incorporation, or whatever other document serves as its charter) that prohibits the charity from operating for the benefit of private parties. The charity could argue that complying with a restriction that would result in a violation of the private benefit doctrine is “impossible” because doing so contravenes its corporate charter. Some precedent supports the application of cy pres on grounds of impossibility when compliance with the terms of the restricted gift would violate the corporate charter of the donee. *See, e.g., Howard Sav. Inst. v. Peep, 170 A.2d 39, 46-48 (N.J. 1961).*

131. 13 N.E.2d 110 (Ill. App. Ct. 1938), discussed *supra* notes 52-63 and accompanying text.


133. Id. at 1161.

134. The language of Code section 170(c)(2)(B) mirrors the corresponding language of Code section 501(c)(3).
Code section 501(c)(3) would result in their dissolution. In such situations, a reasonable conclusion is that compliance with the restricted terms of publicly solicited gifts is "impracticable." Thus, when a court is petitioned to redirect the disposition of restricted gifts on the grounds that compliance with the restrictions would jeopardize the charitable donee's federal income tax exemption, the court should find that the cy pres doctrine applies, if the funds were donated with the requisite general charitable intent. Although this conclusion is entirely sensible, there is little judicial precedent to support it.

Moreover, the italicized phrase of the preceding paragraph presents no small difficulties. As has been observed previously, courts have reached inconsistent results in determining whether donors of publicly solicited funds had general charitable intent in addition to the specific intent to further the restricted charitable purpose of the gifts. Should the court hear evidence of the intent of each and every donor whose testimony is available? Should the court limit its inquiry to an analysis of the terms of the charitable donee's solicitation materials? Should the court presume general charitable intent because the average donor in a massive fundraising campaign would not expect a return of her contribution? Alternatively, should the court presume an absence of general charitable intent because the donee alone wrote the solicitation materials, and therefore the donee should not be allowed to depart at all from specified terms absent compelling evidence of donor intent to the contrary? Existing authorities do not provide us with clear, consistent answers. This predicament is

135. Some courts have been persuaded that when the failure to apply cy pres would threaten the continued existence of the donee, the doctrine should be applied. See, e.g., Sharpless, 548 A.2d at 1160; In re Estate of Othmer, 710 N.Y.S.2d 848, 852-53 (Sur. Ct. 2000). These courts reason that donors generally would not want to see their intended purpose thwarted by the cessation of operations of the charitable donee. This rationale makes good sense when the restricted gift is expected to remain with the charity in perpetuity, or at least for a great length of time. Unfortunately, that rationale does not apply as forcefully to our hypothetical charity. The charitable donee described in the hypothetical could literally comply with the restricted terms of the gifts by distributing all contributed funds to the victims, and then forfeit its income tax exemption. If donors lacked general charitable intent, they might be perfectly happy with this result. The real doctrinal issue, then, is whether the donors had merely a specific intent to benefit the victims of the hurricane, or the more general intent to further charity.

136. Some support for this position arguably appears in decisions of courts that have applied cy pres following changes in federal income tax law (although many of these cases are decided under the doctrine of equitable deviation, rather than under cy pres). For example, in Arner Estate, 65 Pa. D. & C.2d 421, 422 (Pa. Ct. C.P. 1974), a trust was established to pay the nursing home admission fee of one person selected in the future by a local church. According to the court, the Tax Reform Act of 1969, coupled with changed economic conditions, rendered the trust "impractical of fulfillment." Id. at 424-25. Thus, the court approved the termination of the trust, and the transfer of trust assets to the restricted endowment fund of the nursing home, to be used for purposes very similar to those designed by the settlor. See id. at 425.

137. See supra notes 58-63 and accompanying text.
attributable not only to the inherent vagaries of the cy pres doctrine, but also to the doctrine's awkward application to publicly solicited restricted gifts. Some mechanism, be it judicial or legislative reform of the doctrine or some other creative initiative, is necessary to increase the predictability of legal outcomes in this area.


Assuming that the jurisdiction recognizes the cy pres doctrine, when, if at all, does a charity jeopardize its federal income tax exemption by returning publicly solicited restricted donations to donors without having obtained direction from a court to do so? Consider the hypothetical charity raising excessive funds for hurricane victims. Let us assume that the charity astutely recognizes that distributing all funds would jeopardize its federal income tax exemption because doing so would confer more than incidental private benefit. Let us also assume that the charity wishes to avoid the legal fees and court costs of a judicial cy pres proceeding, as well as the negative adverse publicity that may arise from petitioning a court to depart from the restrictive terms of the solicited gifts. In an effort to appease donors who might object to the use of funds for any purpose other than that advertised in the charity's solicitation materials, the donee returns all excess donations to people who made gifts to the donee within a specified time frame following the hurricane, on a pro rata basis. Is the refund of such excess donations problematic?

Under current law, any such refund presents a private benefit problem. It will be recalled that under the cy pres doctrine, a donor owns a reversionary interest in a restricted gift only if he lacks general charitable intent. As discussed above, according to significant judicial authority, the funds received by the charity from the general public are restricted gifts. The relevant question is therefore whether the donors of the gifts had general intent to further charity, or only the specific intent to aid the hurricane victims of the small town. Under the traditional cy pres doctrine, this question must be answered by a court because a charity has no authority to determine the existence (or non-existence) of general charitable intent by itself.

Let us assume that the charity erroneously determines that the donors lacked general charitable intent prior to returning the excess contributions. Or even worse, the charity does not even think about the issue, and simply returns the surplus donations, notwithstanding the donors' general charitable intent. Because the donors had general charitable intent, they were not entitled to receive any surplus funds from the charity under the cy pres doctrine. In addition to whatever liability may be imposed by state law on the trustees of the charitable
organization for breaching their fiduciary duties, the organization itself may lose its exemption from federal income taxation. When the organization erroneously refunds surplus funds to donors, it directly confers an economic benefit (money) upon private parties. The return of the donations differs little from a charity’s decision to dole out cash to a crowd of people without regard to their need for assistance. The larger the surplus, the greater the probability that this private benefit is not quantitatively incidental. Moreover, because a charity may handle surplus restricted gifts more responsibly by other means (such as by seeking a court order for the disposition of the funds, or by carefully providing for their disposition in communications to donors ex ante), it is doubtful that the private benefit conferred through the return of the excess funds is qualitatively incidental.

**c. The Third Question: When May Donations Jeopardizing Federal Income Tax Exemption Be Returned in a Non-Cy Pres Jurisdiction?**

As indicated above, some states do not recognize the cy pres doctrine. In those states, a third question is relevant: May a charitable donee return publicly solicited restricted gifts to donors when complying with the restrictive terms would jeopardize the donee’s exemption from federal income taxation? The legal analysis of this issue is much the same as that applicable to the previous questions. In states that do not recognize the cy pres doctrine, presumably a court must decide only whether the original restricted purpose no longer may be fulfilled; if so, donors are entitled to the return of excess funds. I would urge the courts in such states to adopt the position that when compliance with the original restricted purpose of the gifts would jeopardize the federal income tax exemption of the charitable donee, the donee is not bound to comply with such restrictions. In these states, the consequence of such a determination is that the donors would be entitled to receive the surplus funds.

Under current law, however, a charity in such a state should not unilaterally decide to refund excess restricted charitable donations.

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138. A charitable organization might attempt to justify the return of excess contributions under the theory that it is averting a costly lawsuit by donors who would be dissatisfied if the charity failed to do so. This justification would appear quite weak on the facts of the hypothetical. As discussed previously, most courts generally hold that donors have no standing to sue (absent some special reserved interest). Unless the charity reasonably believes that under state law donors likely have standing to sue for a return of excess donations, refunding surplus funds without obtaining court approval is unwise.

139. If, however, the donors lacked general charitable intent, no private benefit theoretically arises from the return of surplus funds. In such a situation, the donors are merely receiving the property to which they are entitled under state law. Of course, under the cy pres doctrine, a court, not the charitable donee, is the proper authority to decide the presence or absence of general charitable intent.
Let us assume that the charity in our hypothetical fact pattern concludes that transferring additional funds to or for the benefit of the hurricane victims would confer excessive private benefit upon them. If the charity is correct, a court should order the return of the excess funds to the donors. On the other hand, if the charity is mistaken, the donors are not entitled to the funds thought to be excessive. Refunding the funds erroneously thought to be excessive results in private benefit to donors. For the reasons discussed above, such benefit may be more than quantitatively incidental, and most certainly is not qualitatively incidental. A charity that reaches the wrong decision on this issue, and acts upon it, could forfeit its federal income tax exemption.

d. The Fourth Question: When Are Contributions Deductible?

When are taxpayers who have made gifts to a charitable organization that publicly solicited restricted funds not entitled to a charitable contribution deduction under Code section 170? The short answer to this question is supplied by the Treasury regulations (and the authorities interpreting them) discussed above.\footnote{140} These donors are entitled to deduct their charitable contributions unless the possibility that an event requiring the return of their contributions “appears on the date of the gift to be so remote as to be negligible.”\footnote{141} In our hypothetical, the event that would require the return of contributions is the receipt by the charitable donee of surplus charitable gifts for hurricane relief, provided that if the charity is in a cy pres jurisdiction, the donors had only specific charitable intent. As discussed above, the determination of whether surplus funds exist (or, stated alternatively in a cy pres jurisdiction, whether the distribution of additional funds for the restricted purpose would be “impracticable”), should be decided in part by determining whether the distribution of such funds would give rise to non-incidental private benefit (or to private inurement). Of course, other eventualities may result in surplus funds, such as a simple determination that all of the money that can be spent on the specified purpose has been spent (as in the case of a completed building project).

The preceding paragraph helps illuminate the complexity of the subtle interaction between the cy pres doctrine (or the law of restricted charitable gifts in general) and federal income tax law. A charity that receives funds through mass appeals to the general public for a particular charitable project or function may often be held to possess such funds as restricted gifts. In a jurisdiction recognizing cy pres, the charitable donee may depart from the terms of such gifts only if a court finds both that donors had general charitable intent,

\footnote{140. See supra notes 94-109.}
\footnote{141. Treas. Reg. § 1.170A-1(e) (2002).}
and that compliance with the restrictive terms of the gift is impossible, illegal, or impracticable. Whether compliance with the terms of the gift is "impracticable" should depend in part upon whether such compliance would jeopardize the federal income tax exemption of the charitable donee under the private benefit doctrine. If, at the time of making the gifts, donors have only specific charitable intent, and if there is more than a remote likelihood that the charitable donee will be unable to comply fully with the terms of the restriction because doing so would jeopardize the donee's federal income tax exemption under the private benefit doctrine, donors will not be entitled to deduct their contributions under Code section 170. Indeed, any time there is more than a remote likelihood that the charitable donee will be unable to comply fully with the terms of restricted gifts on account of the receipt of excess funds, the propriety of a deduction under section 170 is called into question. The same conclusion holds with respect to taxpayers donating restricted gifts to a charity in a jurisdiction that does not apply cy pres, quite apart from any inquiry into the specificity of such taxpayers' intent.

Reflecting upon this analysis, one can appreciate the incredibly difficult task of determining whether, and to what extent, a taxpayer who makes a gift to charity in response to a mass solicitation for restricted funds is entitled to claim a deduction for her contribution under Code section 170. That charities actually have sought to depart from the restrictive terms of such gifts should be evident from the discussion to this point. In contrast, the proper approach for determining the deductibility of these restricted charitable contributions in an actual case is far from evident. How can an individual taxpayer, much less the IRS or a court, accurately determine, as of the date of the taxpayer's gift, whether the charity's receipt of excess funds that will be returned to donors carries a risk "so remote as to be negligible?" Can any single decision-maker realistically make this determination, which hinges upon a contingency often beyond the control of the charitable donee, as well as any single donor? Further, even if one could predict the amount of the excess charitable funds, should every contributing taxpayer be permitted a partial deduction for her estimated pro rata contribution to the restricted funds that are used for the specified purposes? Or, in defiance of the principle that money is fungible, should the deduction be disallowed in full because no taxpayer can trace her contribution to the funds that are not refunded to donors? Should different rules of deductibility apply depending on when each contribution is made within a fundraising campaign for a specified purpose?

Existing authorities do not provide satisfying answers to these questions. In the shadow of these difficulties, and unlike the approach

142. Id.
of the IRS in Revenue Ruling 79-249, the law could simply abandon all attempts to apply the Treasury regulations' rule of non-deductibility of gifts on account of non-remote contingencies in the context of restricted charitable gifts solicited in mass appeals. While this “solution” would make life easier for taxpayers, the IRS, and the courts, it is probably not the best course of action. As explained above, because of the time value of money, allowing a current-year deduction for all such restricted gifts subject to contingencies is costly to the government. The rule of the Treasury regulations is theoretically correct. The key is to devise a theoretically defensible system that minimizes costs and simplifies administration.

C. Summary

Current law presents as many questions as answers in the attempt to determine the proper distribution of surplus gifts received by a charitable donee in a public appeal for donations for a particular charitable purpose. At the outset, a court must decide whether an appeal for funds to meet a specific need causes the attendant charitable gifts to be legally restricted. Several cases have ruled that such funds are restricted. If such funds are restricted for a particular charitable purpose, a charity may not do whatever it pleases with funds that it deems excessive, but must seek direction from a court. In a jurisdiction that recognizes the cy pres doctrine, a court must first determine whether a “surplus” of charitable gifts exists, such that compliance with the restriction has become illegal, impossible or impracticable. A good argument can be raised that a court should find the requisite impracticability whenever compliance with the terms of gifts would jeopardize the federal income tax exemption of the donee (for whatever reason, including the private benefit doctrine), but one finds little precedent on this issue. Further, even if the court finds that compliance with the restriction would be impracticable, cy pres will be applied only if donors are found to have possessed general charitable intent.

How a court arrives at such a finding is most problematic. Attempting to ascertain the intent of each and every donor responding to a mass appeal for funds is often simply not practical, although a pure cy pres analysis would require it. Consequently, courts must resort to examining the terms of the appeal and its surrounding circumstances to determine whether donors as a class had a charitable intent more general than advancing the specific purpose for which funds were solicited. In doing so, courts appear to adopt a presumption, either explicitly or implicitly, that donors as a class did or did not have general charitable intent. Courts have differed on the presumption adopted, and there is no discernable basis for predicting

143. 1979-2 C.B. 104.
which presumption (for or against general charitable intent) will be adopted in any given case.

The difficulty in predicting when surplus funds will be returned to donors presents yet another problem: determining whether a taxpayer is entitled to a charitable contribution deduction for donations made in restricted charitable gift campaigns. The problem arises in jurisdictions that apply the cy pres doctrine, as well as in those that do not. A default rule that simply grants taxpayers a deduction in all such cases is both theoretically unsound and potentially costly to the government.

A solution to these complex problems is needed. The next section of this article examines whether the solution may be found in existing proposals for reforming the doctrine of cy pres.

II. WHY CY PRES REFORM PROPOSALS DO NOT ADEQUATELY ADDRESS THE PROBLEM OF DISPOSING OF EXCESS CHARITABLE DONATIONS RECEIVED IN PUBLIC SOLICITATIONS

Numerous legal scholars have offered proposals for reforming the doctrine of cy pres. Many of these scholars concern themselves with the issue of "dead hand control" of sums donated to charity, and the resulting efficiency losses that may be perpetuated by the traditional doctrine of cy pres. Other scholars focus on particular elements of the doctrine that have proven confusing, unworkable, or even illusory. At least one has even questioned the theoretical justification for the foundational rule that restricted charitable gifts are generally legally enforceable. Some proposals from academics have been adopted by state legislatures. Although analyzing each and every proposal for reforming cy pres in detail is beyond the scope of this article, a brief critical review of the most prominent of these proposals reveals that the reform proposals are probably inadequate, or at least incomplete, measures for adequately disposing of excess charitable funds received through mass solicitations. This section of the article explains why existing proposals for reforming cy pres are not well suited for solving the problem of publicly solicited surplus funds donated to charity.

A. Presume (or Abandon the Requirement for Finding) General Charitable Intent

Professor Bogert advocated that in applying the doctrine of cy pres, courts should presume that donors had general charitable intent, or entirely dispense with the requirement of general charitable intent.\textsuperscript{144} Both the former\textsuperscript{145} and the latter\textsuperscript{146} suggestions of Professor Bogert

\textsuperscript{144} Bogert, \textit{supra} note 16, § 436. Similarly, section 413 of the Uniform Trust Code presumes that a settlor had general charitable intent. Unif. Trust Code § 413, 7C U.L.A. 69 (Supp. 2002).

\textsuperscript{145} Massachusetts now statutorily presumes general charitable intent by donors.
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have legislative parallels. Abandoning the requirement of finding general charitable intent by donors would surely ease administrative burdens on the courts. No longer would courts need to hear evidence of whether donors as a class, or any particular donor, would prefer that excess contributions be used for some charitable purpose or instead be returned to donors. Nor would judges expend valuable time engaging in judicial hair-splitting between general charitable intent and specific charitable intent when the evidence on the issue is scant (as it often will be).

Similarly, adopting a presumption that donors responding to mass solicitations for restricted charitable gifts had general charitable intent not only finds some judicial support, but also would tend to reduce the evidentiary burden on courts necessitated by a pure cy pres analysis (which theoretically requires an examination of evidence bearing upon how every donor actually would have preferred to dispose of her donation that could not be used precisely as initially intended). By adopting a presumption in favor of general charitable intent, courts could apply cy pres to surplus funds raised in mass solicitations unless the evidence plainly indicates that donors lacked general charitable intent. In most public appeals for funds by charities, it is doubtful that such evidence would often suffice to rebut the presumption in favor of general charitable intent. Most donors responding to public appeals for gifts probably either make no specific statement as to the desired use of donated funds, or simply note on their donations made by check the purpose identified by the charity for raising funds (such as “flood relief”). Such a notation of the purpose of the gift would not alone suffice to rebut the presumption of general charitable intent. Indeed, only if the solicitation by the charitable donee expressly stated that contributions would be used exclusively, and in all events, for the designated charitable purpose is it likely that a court would find that the presumption of general charitable intent is rebutted.

Abandoning the requirement of finding general charitable intent would also eliminate the possibility that restricted charitable


147. See supra note 61 and accompanying text.

148. Cf. Restatement (Second) of Trusts § 399 cmt. c (1959) (stating that the mere description of the charitable purpose of the gift with particularity does not necessarily establish the absence of general charitable intent).
contributions may be refunded to donors, unless the terms of the restricted gifts expressly require the return of surplus funds. Assuming that no such terms exist, no donor should be denied a charitable contribution deduction under the special provision of the Treasury regulations discussed above. Even if donations prove to be excessive, they will be devoted to some charitable purpose (rather than returned to donors), and therefore the charitable contribution deduction is entirely appropriate. Taxpayers may comfortably claim charitable contribution deductions, and the government need not suffer the revenue loss associated with the claiming of deductions by taxpayers for transfers that are later refunded.

Presuming that donors responding to mass solicitations for restricted charitable gifts had general charitable intent tends to decrease the probability that restricted charitable contributions may be refunded to donors, unless the terms of the restricted gifts expressly require the return of surplus funds. Assuming that no such terms exist, a donor usually should have a strong argument that she may claim a charitable contribution deduction for her publicly solicited gift. Because in most cases one would not expect a court to find evidence that rebuts the presumption of general charitable intent in the context of public appeals for donations, the likelihood that any donor would be entitled to a refund of a portion of her gift should often be quite remote. In such circumstances, the Treasury regulation discussed above does not operate to disallow the deduction under Code section 170. Notwithstanding this analysis, it remains true that the ultimate inquiry as to whether a restricted charitable gift is subject to a non-remote contingency is factual and case-specific. Therefore, the prospect that the presumption of general charitable intent may be rebutted renders the deductibility of charitable contributions under Code section 170 less conclusive than when the requirement of general charitable intent is abandoned.

Although abandoning the requirement of general charitable intent, or presuming general charitable intent, has the foregoing advantages in judicial economy and the administration of the charitable contribution deduction under federal income tax law, both alternatives may also be criticized, particularly in the context of restricted donations raised through mass solicitations. It is not clear that either of these two proposals truly produces a net efficiency gain. To understand why this is so, the analysis of Professor Jonathan Macey will prove salutary. Macey argues that a regime governing restricted charitable gifts will maximize societal welfare if it lowers the error, transaction, and agency costs of creating trusts. That system “would provide maximum incentives to create wealth, and facilitate

the creation of private trusts which provide for the creation of significant public goods.\textsuperscript{151}

Error costs include those costs attributable to mistakes in drafting and interpreting the terms of the governing donative instruments. Transaction costs are those associated with drafting the terms of the donative instrument precisely as intended by the donor (including provisions dealing with contingencies). Agency costs are those associated with monitoring and controlling those responsible for administering the trust following its establishment.\textsuperscript{152}

How "costly" by these standards is the proposal to presume that donors had general charitable intent, or to dispense entirely with the requirement of general charitable intent, in the case of publicly solicited funds? Let us first consider transaction costs. It will be recalled that when a charity solicits funds from the general public for a restricted purpose, the "donative instrument" that sets forth the restrictions is really the solicitation itself. Thus, the charity is typically the primary drafter of the donative instrument. If one considers the transaction costs to the charity alone, the proposal to presume general charitable intent by donors (or to dispense entirely with the requirement of general charitable intent) would not be costly. Indeed, a charity's silence as to what disposition is to be made if surplus funds are raised will suffice for many charities.\textsuperscript{153} However, one must not lose sight of whose intent as to the disposition of gifts is critical—that of the donors, not just that of the charitable donee. The inquiry should not look primarily to the minimal transaction costs of this proposal to charitable donees, but to the transaction costs incurred by the mass of contributors to charity.

The extent of these transaction costs to donors depends in part upon their intent. Let us first assume that donors as a class would prefer that the charity retain surplus funds and use them for some charitable purpose to be chosen by someone other than the donors, rather than return the surplus donations to them. If this assumption is correct, transaction costs to donors are low under the proposal to presume that donors had general charitable intent, or to dispense entirely with the requirement of general charitable intent. They can simply respond to the solicitation in silence, assured that there is no need to speak.

But let us assume that many donors care greatly about the use of surplus funds. If donors would actually prefer to receive a refund of their share of a surplus, for example, they would be required to condition their gifts on such terms. As a practical evidentiary matter,  

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{151} Id. at 299.
\item \textsuperscript{152} See id. at 298 & n.7, 299.
\item \textsuperscript{153} Silence will often suffice for the donees because if they say nothing, they will usually be entitled to keep donations, even if they must go to court for an alternative disposition of surplus funds under cy pres.
\end{itemize}
\end{footnotesize}
a donor would need to express this condition in writing. While the transaction costs of specifying that any surplus funds must be returned to one donor should be low, the costs increase as the number of donors desiring a refund of their share of the surplus increases, especially if these donors seek legal advice so as to ensure the desired consequences. Moreover, if donors do not desire a refund of any surplus, but instead prefer to retain the right to specify an alternative charitable use for their share of the surplus, the transaction costs of drafting instruments to effectuate these legal results donor-by-donor would be very high indeed.

Because of the expected high transaction costs associated with conditioning a gift on a return of any surplus, one may reasonably expect that most donors who give in response to public solicitations will not incur the costs of expressing their desired disposition of any surplus in writing. One may also reasonably posit that many donors are, and will continue to be, unaware of the legal effect of a charitable donee's receipt of surplus gifts following a campaign for donations, and that many donors also will be unaware of the significance of a presumption of general charitable intent (or, in the alternative, of the significance of abandoning the requirement of finding such intent before applying the cy pres doctrine). But even when, for one or more of these reasons, donors avoid the transaction costs of expressing their desires for the disposition of surplus funds, it is conceivable that error costs will be high.

As in the case of transaction costs, the extent of these error costs to donors depends in part upon their intent. If we assume that donors as a class would prefer that the charity retain surplus funds and use them for some charitable purpose to be chosen by someone other than the donors, there are no error costs associated with a presumption of general charitable intent (or with abandoning the requirement of general charitable intent). Under such an assumption, a court does not commit "error" in applying cy pres. But if we assume that, but for the transaction costs associated with expressing their wishes more particularly, or but for their ignorance of the law, donors would express their intent as to the disposition of surplus funds in a manner that differs from the disposition resulting solely from the solicitation materials publicized by charitable donees, we would expect error costs to be high.

It should also be observed that abandoning the requirement of general charitable intent, or presuming general charitable intent, probably does little to decrease agency costs (i.e., the costs of monitoring and controlling the trustees and directors of charitable donees) associated with the current legal regime governing restricted gifts. Certainly, the proposal does not directly do so. True, one could argue that because judicial time and energy will no longer be wasted in trying to discern the presence of general charitable intent under the
traditional application of the doctrine of cy pres, more judicial time can be devoted to framing an alternative disposition of surplus funds, and therefore proposals for such dispositions by charities perhaps would receive heightened judicial scrutiny. Such a conclusion, however, is highly speculative, and any benefits from such scrutiny seem rather attenuated.

Three other comments are in order in assessing the relative merits of the proposal to abandon the requirement of general charitable intent, or to presume general charitable intent. First, the proposal does not clarify whether the doctrine of cy pres may be applied when doing so is necessary to prevent a charitable donee from forfeiting its federal income tax exemption. Secondly, the proposal does not likely provide charities soliciting funds with an incentive to maximize disclosure to donors of how the charity plans to handle any surplus. As argued below, ideally, charitable donees would communicate their “contingency plans” for excess restricted gifts through their solicitation materials sent to donors well in advance of receiving the surplus. If charitable donees know that under the worst case scenario, all they must do is petition a court for an alternative disposition of restricted funds, they are probably less likely to concern themselves with communicating with donors concerning donors’ preferences as to the disposition of excess funds. Finally, the proposal does nothing to address the legal ramifications discussed above in the case of restricted gifts made to a charitable donee in a jurisdiction that does not recognize the cy pres doctrine.

B. Presume No General Charitable Intent

A polar opposite approach to the problem would be to presume that donors as a class have no general charitable intent. Charities would be entitled to retain surplus restricted gifts only if the solicitation materials plainly state that surplus funds may be used for charitable purposes other than the restricted purpose designated in the fundraising campaign. This approach is basically that suggested by Professor Jonathan Macey, who has argued that the traditional cy pres doctrine is no more efficient than a default rule under which property transferred in trust for specified charitable purposes would revert to the settlor’s heirs “whenever any significant aspect of the settlor’s intentions are thwarted, unless the settlor provides for a contrary result.”

Like the first proposal, this alternative has both advantages and disadvantages.

Presuming that donors lacked general charitable intent would tend to reduce the evidentiary burden on courts necessitated by a pure cy pres analysis (which entails an examination of all sorts of evidence bearing upon whether donors would have preferred reversion or the

154. Macey, supra note 150, at 306.
advancement of charity for some purpose other than that initially intended). Unless the charitable solicitation materials plainly state that funds raised for the specified purpose may not be so used in some circumstances, it is unlikely that the presumption of no general charitable intent would be rebutted. Without such a statement, rebutting the presumption would likely require the admission of evidence that donors informed the charitable donee in writing that it could use the gifts however it so desired. Absent income tax motivations, donors would be unlikely to so inform the donee. Thus, a court's review of the relevant evidence could be fairly limited. Further, once a judge has found that the presumption of no general charitable intent stands, she would not be required to spend additional time framing an alternative scheme of disposition of charitable funds. Accordingly, ignoring the implications of federal income taxation on the behavior of taxpayers, one would expect some gains in judicial economy (relative to current law) if courts presume the absence of general charitable intent.

For reasons discussed above, one cannot be certain whether presuming no general charitable intent would be associated with higher transaction and error costs. The extent of these costs to donors depends in part upon their intent. If we assume that donors as a class would prefer that the charity retain surplus funds and use them for some charitable purpose to be chosen by someone other than the donors, rather than return the surplus donations to them, the proposal of presuming no general charitable intent would tend to heighten transaction costs to donors. They cannot simply respond to the solicitation and rest in peace. They must either inform the donee that it can keep the funds no matter what, send their contribution in some manner that does not restrict the gift, or receive their refund and then resubmit an undesignated gift to the charitable donee. If donors do not wish to incur the transaction costs associated with these actions, or if they simply are ignorant of the legal consequences of not taking these actions, we would expect the presumption of no general charitable intent to generate error costs—the costs of wrongly returning to donors funds that they would prefer be retained by the donee.

Of course, if we assume that donors care greatly about whether the donee uses the funds for restricted purposes precisely as represented, they can simply respond to the appeal for restricted funds in silence. Doing so does not inherently generate transaction costs or error costs.

The effect of the presumption of no general charitable intent on agency costs is more subtle. While one cannot be certain, it appears that the presumption may tend to increase agency costs. Under the traditional cy pres doctrine, a charitable donee who has received

155. See supra note 71.
restricted gifts may petition a court for an alternative charitable disposition of funds when the original purposes of the restricted gifts have been accomplished (assuming the other elements of the doctrine are established). The presumption of no general charitable intent would tend to decrease the instances in which cy pres would be applied. Thus, a charity that petitions a court for instructions is more likely to find itself refunding gifts to donors. A charity then would be faced with one of two choices: (i) determine that a surplus of restricted gifts exists, petition a court for instructions as to the disposition of the surplus, and incur a greater risk (relative to current law) that the funds must be returned to donors; or (ii) expend as much of the restricted funds as possible, thereby eliminating (or at least reducing) the "surplus." The latter option may indeed amount to charitable waste, but the charity may prefer waste to forfeiting the use of the funds.

Certainly, a charity may not choose to expend restricted funds wastefully if doing so subjects the trustees or directors to legal liability, or jeopardizes the federal income tax exemption of the charitable donee (for example, under the private benefit doctrine). But there are numerous situations in which a charity can act wastefully without practically subjecting itself or its governing board to liability. For example, consider a charity that raises $10,000,000 for a building that costs only $5,000,000 if built to the original specifications. Under the traditional doctrine of cy pres, the charity might well choose to implement its initial construction plans, and petition a court for an alternative disposition of the excess donations. If, however, the charity believes that a court would be likely to direct a refund of the surplus $5 million to donors, the charitable organization has an incentive to revise its plans and construct a building that costs $10,000,000. After all, that additional $5 million could be used not only to construct larger and more functional facilities for providing charitable services, but also to build more spacious, luxurious suites for officers and employees. Wasteful expenditures of what otherwise would constitute a surplus may indeed represent a form of agency cost. Such expenditures are not direct costs of monitoring and controlling trustees and directors of charitable organizations, but they are costs resulting from not being able to control effectively those entrusted with administering charitable organizations.

Moreover, at least in the context of publicly solicited gifts, the federal income tax implications of presuming no general charitable intent are troubling. Such a presumption tends to increase the probability that restricted charitable contributions will be refunded to donors. Relative to current law, a donor would have a weaker

156. See supra note 85 and accompanying text.
argument that she may claim a charitable contribution deduction for her publicly solicited gift. Because in most cases one would not expect a court to find evidence that rebuts the presumption of no general charitable intent in the context of public appeals for donations, the likelihood that any donor would be entitled to a refund of a portion of her gift may often not be so remote as to be negligible. In such circumstances, the Treasury regulation discussed above disallows a deduction under Code section 170. Of course, tax savvy donors would eventually understand this problem, and therefore they could be expected to make clear to charitable donees that they intend for the donees to retain their contribution even if the donees receive surplus, restricted gifts. However, expressing such general charitable intent increases transaction costs incurred by these donors. In other words, for donors who desire to maximize their success in claiming a charitable contribution deduction for a restricted gift, a presumption of no general charitable intent is more costly to them than either current law or the presumption in favor of general charitable intent.

Two additional comments may help in evaluating the proposal to presume the absence of general charitable intent. First, even if the presumption is rebutted in a particular case, the proposal does not clarify whether the doctrine of cy pres may be applied when doing so is necessary to prevent a charitable donee from forfeiting its federal income tax exemption. Secondly, the proposal does seem to provide charities soliciting funds with an incentive to maximize disclosure to donors of how the charity plans to handle any surplus. Charities have the greatest control in casting the terms of an agreement concerning restricted funds with donors, because charities write the solicitation materials. A charity desiring to decrease the likelihood that surplus funds will be returned to donors can plainly inform donors of how it will use any surplus funds. Heightening such disclosure to donors, however, does increase transaction costs to charitable donees. Further, current law does not contain any effectual mechanism for reducing such transaction costs associated with more extensive disclosure.

C. Factor in Inefficiency as a Criterion for Applying Cy Pres

Several scholars have proposed that courts apply the cy pres doctrine more expansively by ordering a deviation from the original purposes of the charitable trust or gift whenever compliance with such purposes would be inefficient (sometimes expressed as "inexpedient" or sub-optimal to society).\footnote{157. See, e.g., Lewis M. Simes, Public Policy and the Dead Hand 139 (1955) (arguing that cy pres should apply if the amount to be devoted to the original trust purposes is disproportionate to the associated value to society); Joseph A. DiClerico, Jr., Cy Pres: A Proposal for Change, 47 B.U. L. Rev. 153, 158, 166, 173, 175 (1967) (arguing that cy pres should be applied when considerations of community benefit} In other words, the traditional grounds
for applying cy pres—illegality, impossibility or impracticability—would be expanded to include inefficiency. Some of these scholars would permit deviation in such cases only after the passage of a substantial length of time following the effectuation of the charitable transfer (such as the period of the Rule Against Perpetuities), whereas others would not so limit the expansive use of the doctrine.

Applying cy pres when doing so would further charitable efficiency is a major reform proposal that merits comprehensive analysis, an enterprise beyond the scope of this article. Others have thoughtfully critiqued the proposal, and some of the most significant objections are summarized below. In addition, the proposal should be evaluated more specifically in the context of publicly solicited gifts received for a particular charitable purpose.

First, one should observe that incorporating inefficiency among the several grounds for invoking a court's cy pres powers does not facially address the problem of how to ascertain general charitable intent by donors. Aware of this obvious point, some advocates of factoring in the element of inefficiency in the cy pres analysis also recommend adopting a "presumption [of] 'general charitable intent.'" This recommendation is not surprising. If we conclude that a court's perception of charitable efficiency is a legitimate basis for deviating from the express terms crafted by the donor regardless of how much time has passed between the making of the gift and the filing of the petition for cy pres, it must be because we believe that a court's...
assessment of how the community benefits most is more important than how a donor intended her gift to be used for charitable purposes. If we decide that maximizing charitable efficiency is more important than following a donor’s intent, it would seem logically inconsistent to require a probing inquiry into the donor’s general charitable intent as a prerequisite to the application of cy pres. Why waste precious judicial resources in a difficult search for the probable intention of a donor whose intent does not ultimately matter most? A presumption of general charitable intent is therefore a natural corollary to the proposal to incorporate inefficiency as one of the grounds for applying cy pres. The relative merits of this presumption have been discussed above, and will not be repeated in this section.

Including inefficiency among the several grounds for invoking a court’s cy pres powers does appear to have an advantage not associated with the two reform proposals discussed above. The proposal tends to support the application of cy pres when doing so is necessary to prevent a charitable donee from forfeiting its federal income tax exemption under the private benefit doctrine. As discussed previously, a violation of the private benefit doctrine occurs when private persons benefit more than incidentally from the activities of the charitable organization. The benefit received by private persons must be incidental compared to the community benefit generated by the charitable activity. Stated more pointedly, an assessment of community benefit inheres in the private benefit analysis. Because a court considering charitable efficiency in applying cy pres is, by definition, inquiring into the community benefit associated with the restrictive terms of charitable gifts, as well as the community benefit that would result from an alternative disposition of funds, a court that concludes that compliance with the restrictive terms of publicly solicited gifts would violate the private benefit doctrine should also conclude that cy pres may be applied to redirect the charitable gifts to another purpose. Thus, although a credible case under current law can be made for applying cy pres to surplus funds raised through a public solicitation for restricted gifts when necessary to avoid the donee’s loss of income tax exemption under the private benefit doctrine, a very compelling case for cy pres in such circumstances can be made under the proposal to incorporate charitable inefficiency as an element of the cy pres analysis.

There are also disadvantages of the proposal (or at least reasons to question it). Most apparent are the added administrative costs incurred by the judiciary in hearing and evaluating evidence as to the community benefits (i.e., the charitable efficiency) of following or

161. Some advocates of liberalizing cy pres would respect a settlor’s express terms of trust that forbid the application of cy pres in all events. See, e.g., Johnson & Taylor, supra note 157, at 575.

162. See supra notes 144-53 and accompanying text.
deviating from the express terms of charitable gifts. Courts would be required to consider far more evidence than they are currently constrained to assess under the traditional doctrine of cy pres. Moreover, as Professor Rob Atkinson has argued, that courts can determine the most efficient use of charitable assets is debatable.\textsuperscript{163}

The proposal could also lead to especially undesirable results specifically in the case of publicly solicited funds for restricted charitable purposes. Unless the proposal is limited to gifts that were made long before the petition for cy pres is filed (a limitation suggested by Professor Alex Johnson),\textsuperscript{164} a rule that charities (with court approval) may depart from the terms of publicly solicited restricted gifts could have a major dampening effect on charitable giving. It is one thing to permit deviation when doing so is necessary to prevent the charitable donee from violating the private benefit doctrine, jeopardizing its federal income tax exemption, and thereby risking its very existence. It is quite another thing to permit a charitable donee in receipt of publicly solicited restricted gifts to petition a court for another charitable use of funds simply on the grounds that a more “efficient” charitable use has been discovered. The most rational explanation for solicitations for restricted charitable gifts from the general public is that the charitable donee believes that it will raise more money if the contributing public realizes that funds will be used for the specified purposes. If the law permits charities to petition a court for an alternative use of such funds (perhaps for a use that does not have wide public approval) on the grounds that such use is more efficient, those donors who would have given less (or nothing at all) to the donee had the solicitation materials not restricted the use of donations will have no legal assurance that their donations will be used as intended. Unless such donors can be assured adequately through non-legal forces that a donee will not employ a “bait and switch” policy with respect to restricted gifts, one would expect them to give less to charity (or at least less to that charitable donee) under the proposal.

Some proponents of including inefficiency among the grounds for applying cy pres have argued that doing so may actually appeal to donors, who would prefer that their gifts be used efficiently.\textsuperscript{165}

\textsuperscript{163} Atkinson argues that cy pres reform typically assumes that there is a method for determining charitable efficiency (i.e., the best use of a charitable dollar). \textit{See} Rob Atkinson, \textit{Reforming Cy Pres Reform}, 44 Hast. L.J. 1111, 1134 (1993). Atkinson alleges that not only does such a method not exist, but also expanding cy pres in the manner suggested by reformers could result in “standardless modification of charitable trusts.” \textit{Id.}; \textit{see also id.} at 1135-42 (arguing that there is no good measure of efficiency in this context and that permitting the courts to determine charitable efficiency will ensure no clear standards for doing so).

\textsuperscript{164} \textit{See supra} note 158.

\textsuperscript{165} For example, Professor Johnson argues that a settlor would likely prefer to have donated assets “put to their best use, as measured by the current state of
Whatever the force of this argument as applied to gifts made long before the filing of the petition for cy pres, it is less persuasive in the case of publicly solicited restricted gifts. A living donor can choose among numerous charitable causes to support. A donor who has responded to a public solicitation for funds to be devoted to a specified charitable purpose presumably does so because he prefers to subsidize precisely that cause. A donor who wants someone else to select the charitable use to which his donation will be used could be expected to donate sums to a charitable grant-making organization that supports multiple causes, such as a community foundation or the United Way. Alternatively, at a minimum, if the donor did not want to restrict the use of his funds for the specified purpose, he could be expected to contribute sums to the donee for its general charitable purposes. The more plausible position is that those who donate to a charitable donee seeking funds for a specified purpose prefer that the donee generally not decide, on its own accord or with the approval of a court, on an alternative use of donations under the banner of charitable efficiency.

Under this analysis, if the law were changed to include inefficiency among the grounds for applying cy pres, we should expect either transaction costs or error costs to increase in the context of publicly solicited funds for a restricted purpose. Because the typical donor probably would not want the charitable donee to be permitted to depart from the terms of the restrictions simply on grounds of inefficiency, she may expressly condition her gift on the donee's agreement not to seek an alternative charitable use of her donation upon a determination that such use is thought to be more efficient. If every donor takes the time (or hires legal counsel) to so condition her affairs," rather than having them tied up in the original purposes of the trust. Johnson, supra note 26, at 385; see also Sisson, supra note 26, at 650 (speculating that prospective donors might actually be encouraged to give if they could be assured that their donated funds would be used efficiently in the future).

166. Some advocates of including inefficiency among the grounds for applying cy pres recognize that doing so makes little sense in the case of recent gifts. See, e.g., Johnson, supra note 26, at 379-80.

It would be ludicrous to apply an expansive view of cy pres to a charitable trust one year after it is established, just as it is similarly ill-advised to hew strictly to the settlor's intent 200 years after the settlor's death. Time inexorably causes the interests to be benefited or represented in the trust to change.

Id.

167. In the terms of an economist, such donors likely derive significant "result utility" from their gifts. Professors Mark Hall and John Colombo have nicely explained the economics literature that distinguishes between a donor's "act utility" and her "result utility." See Mark A. Hall & John D. Colombo, The Donative Theory of the Charitable Tax Exemption, 52 Ohio St. L.J. 1379, 1407-10 (1991). A donor receives act utility merely from the activity of donating to charity (perhaps from a sense of self-righteousness), without regard to whether the charitable donee uses the donation for the social good. See id. at 1407. In contrast, a donor's result utility is her satisfaction derived "by bettering some social condition." Id.
gift expressly and in writing, donors as a class would incur significant transaction costs. Certainly, some donors may decide not to incur such transaction costs because they exceed the benefit to such donors of ensuring that donated funds will not be redirected. Other donors may simply be ignorant of the legal consequences of the proposal to incorporate inefficiency among the grounds for applying cy pres. Notwithstanding that donors in both cases will avoid incurring greater transaction costs, error costs will increase, because the intent of such donors will not be effectuated.

Thus, the proposal to invoke cy pres when compliance with the original restricted purposes of a gift would be inefficient is quite problematic as applied to publicly solicited funds restricted for a charitable purpose. Although the proposal purports to promote economic efficiency, it may very well lead to the inefficient reduction in charitable contributions made in response to mass appeals for donations. Even if the proposal does not do so, it would likely be associated with high transaction or error costs. Further, the proposal would impose additional burdens (and costs) on the judiciary.

D. Abandon Legal Enforcement of Restrictions on Charitable Gifts

One of the most creative and thoughtful proposals for overhauling the doctrine of cy pres has been suggested by Professor Rob Atkinson. Rejecting proposals to liberalize (i.e., to expand the grounds for applying) the doctrine, Atkinson argues that a better approach would be to “[e]liminate legal enforcement of dead hand control and leave the disposition of charitable assets to the discretion of their trustees.” Atkinson’s argument rests in part on the theory that non-legal sanctions imposed by donors will prevent charities from routinely dishonoring the terms of restricted gifts, and therefore donors will not be unduly discouraged from making charitable gifts. Faced with the threat of losing future donations and incurring damages to their own reputations, trustees of charitable donees could be expected to continue to honor commitments to donors, at least those that seem to carry present moral force.

168. See Atkinson, supra note 163.
169. Id. at 1115-16. Professor Atkinson’s views on the enforcement of charitable gifts follow from his broader conception of how the charitable sector does and should operate. For an excellent discussion of this conception, which Professor Atkinson refers to as the “sectarian model,” see Rob Atkinson, Unsettled Standing: Who (Else) Should Enforce the Duties of Charitable Fiduciaries?, 1998 J. Corp. L. 655, 686-99.
171. See Atkinson, supra note 163, at 1124-34. Atkinson’s argument that trustees are not likely to disregard donors’ wishes routinely because of the consequential damage to their own reputations borrows from the scholarship of Professor Macey. See Macey, supra note 150, at 320.
As a threshold matter, it should be observed that this proposal would eliminate most of the federal income tax concerns raised previously. Donors would have no legal right to a refund of their restricted contributions if the restricted purposes fail (or if the charity simply decides to use the donations for other purposes), so donors generally should be entitled to claim a deduction under Code section 170 for their contributions when made. Further, because a charity would not be legally bound by restrictions imposed on gifts, a charitable donee would clearly be able to divert the donated funds to another purpose if necessary to avoid a violation of the private benefit doctrine (and the consequent loss of federal income tax exemption).

Moreover, the proposal would eliminate burdens on the judiciary and related litigation costs. Not only would courts no longer expend time struggling to ascertain whether donors had general charitable intent, but also courts would not even need to consider whether the other elements of the cy pres doctrine—illegality, impossibility and impracticability—justify a departure from the original purposes of the gifts. The removal of cy pres proceedings from dockets would of course also eliminate the private legal fees associated with such petitions, as well as the costs incurred by the state attorneys general in appearing in such actions and evaluating the merits of such cases. On the other hand, we would expect the costs of non-legal enforcement mechanisms to increase if the enforcement of charitable gifts were abolished, so whether there is a net efficiency gain on account of cost reduction is unclear.

What effect the proposal of abandoning legal enforcement of restricted charitable gifts would have on charitable giving is an intriguing question, especially in the case of publicly solicited funds for a restricted purpose. The proposal would seem justified under the following conditions: (i) information on how a donee has used (and can continue to use) contributions is available, complete and accurate; (ii) donors (and potential donors) will be provided such accurate, complete information; (iii) donors (and potential donors) perceive that such information is complete and accurate; (iv) the costs of ensuring that the first three conditions exist are not excessive relative to the costs of the current legal regime; and (v) the “community” in which the trustees have a reputation that matters to them includes many of the donors (or potential donors) who respond to public solicitations for restricted funds, or at least people who empathize with such donors.

The first condition may be satisfied, at least if the charitable donee’s financial statements are audited by an independent accounting firm.172

172. Of course, as illustrated by the recent Enron fiasco, even an audit by an independent accounting firm does not ensure that the reporting entity has provided accurate financial statements.
Someone within the charitable organization (namely, a clerical employee) should be recording accurately how funds have been expended. Similarly, someone (an employee or officer) knowledgeable of the donee's affairs should know whether the continued use of charitable funds for the restricted purpose is "practicable" (as the concept is understood under the traditional cy pres doctrine).

The second and third conditions are more problematic. Intuitively, one would expect charitable donees to communicate more extensively with donors concerning the use of donated funds under the proposal to abandon legal enforcement of restrictions on gifts, for such communication would be necessary to instill confidence in donors that funds have been, and will be, properly used. Such communication between donors and donees is actually a positive factor in the abstract. Good communication between donors and donees may lead to more stable relationships between the two, thereby increasing long-term commitments to advancing charitable causes and facilitating the exchange of ideas for better serving the public in the future. The notion that such communication will be constructive, however, must not be taken for granted. The information conveyed by charities in a world in which restrictions are not legally enforced will be somewhat suspect.

More precisely, accurate information on how a donee has used contributions will likely be communicated to donors, at least if they request it, if the donee has arranged for an audit of its financial statements (assuming that the auditors report favorably upon such statements). If the donee has not arranged for an independent audit of its financial statements, or if the auditor's report suggests reporting abnormalities, we have no assurance that information pertaining to the use of restricted contributions is accurate. Accurate and complete information on how a donee can continue to use restricted contributions arguably is even less likely to be communicated to donors under the proposal to abandon legal enforcement of restricted gifts, regardless of whether the donee has arranged for an independent audit of its financial statements. Consider a donee that sincerely has determined that there is a superior use for funds that were donated for a restricted charitable purpose. If the donee has reason to believe that the donating public may disagree with its assessment of the relative utility of the alternative disposition of funds, the donee will surely be tempted to represent to donors that the continued use of charitable funds for the restricted purpose has become "impracticable," in an effort to appease donors who otherwise would be disgruntled over the redirection of restricted gifts. A donee that is not legally bound to comply with donors' restrictions may have much less difficulty making its case for "impracticability" to the donating public than it would in making its case to a court. A
typical donor responding to a mass appeal for contributions simply is not likely to be willing to spend a great deal of time and intellectual energy testing the merits of a donee's assessment of impracticability, particularly if the donor has not contributed a large sum. Although a donor of a large gift may have a significant incentive to make certain that her donation was used as intended, donors of small sums are in many cases unlikely to expend great efforts monitoring the donee. For such donors, monitoring the donee is simply too costly. The donee controls the information, and it would be difficult for donors to penetrate biased opinions, or even half-truths, carefully crafted by donees.

The problem arises in part because of the nature of the relationship between trustees of charities and the public. In the words of Professor Evelyn Brody, charitable trustees are in some sense agents without principals. Their control of information contributes to this phenomenon. Professor Brody explains as follows:

"The law grants plenary authority to the nonprofit board of directors to manage the affairs of a nonprofit corporation. Those who govern a nonprofit firm can exercise discretion to maximize different goals. Because of the presumed information asymmetry between the nonprofit and the patrons, the nondistribution constraint alone cannot assure the patron that his donation will achieve his intent. If the public cannot tell what is happening inside the nonprofit, the patron cannot know whether the nonprofit is using his or her money to maximize the quality of the charity's services, to reduce their cost to the public, to augment pecuniary and nonpecuniary compensation of the charity's workers, or even to save for the benefit of future patrons."

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173. It is not a sufficient answer to assert that charities will be sure to provide the donating public with complete and accurate information because of the oversight function of charitable "watchdog" organizations. These entities, limited by resources, must be selective in their oversight. Moreover, it is not clear that such organizations are necessarily the most reliable assessors of other charities; they, too, may rely on donations for their existence, and their existence is never more justified (so it would appear) than when they find that their targets have acted improperly. In contrast, a court of law is not beholden to donors, and therefore is a more neutral overseer of charitable entities.

174. Professor Atkinson has suggested precisely the opposite potential problem with his proposal—namely, that charitable donees will behave too responsively to donors in an effort to build a reputation for honoring donor-imposed restrictions. See Atkinson, supra note 163, at 1152-53. I am unconvinced that Atkinson's proposal would pose this asserted problem. Charitable donees would not necessarily be more inclined to coddle donors under Atkinson's proposal than they already do under current law. Under current law, donors are free to pursue just as many informal enforcement tactics as they may pursue under Atkinson's proposal, and donees must compete just as aggressively for donations.

175. Brody, supra note 23, at 463-64.

176. Id. at 466.
The proposal to abandon enforcement of restrictions governing charitable gifts appears to render these charitable agents even more detached from the oversight of a principal than is the case under current law. At least under current law, the threat of a lawsuit by the state attorney general (however unlikely that may be), and the resulting review of the trustees’ actions by a court, provides some additional check on trustees.

Problems with the second condition logically lead to problems with the third condition described above. Because charities can be expected to interpret, and perhaps sometimes even taint, the facts so as to satisfy their preferences as to the disposition of “restricted” funds, donors can be expected to doubt whether their “restricted” contributions will actually be used exclusively for the intended charitable purposes. One may predict two possible consequences. First, some donors may curtail their charitable giving, for they realize that their intended disposition of charitable funds may not occur. Thus, the charitable sector may directly suffer. Alternatively, or perhaps in addition, donors may establish new and more effective “watchdog” organizations to monitor charities. Although doing so may help alleviate some of the problems identified above, such “watchdog” entities are not a panacea, and creating and funding them entails additional costs. This is another way of saying that the agency costs of the proposal are likely quite high. How extensive these costs would be (a proper inquiry given the fourth condition listed above) is anybody’s guess. This article does not attempt to answer whether the costs of monitoring charities by those with no legal powers over them will be greater or less than the costs of monitoring charities under current law.

The proposal does likely fare satisfactorily under the fifth condition set forth above. In the case of local or regional charities, the “community” in which the trustees have a reputation that matters greatly to them likely does include many of the donors (or potential donors) who respond to public solicitations for restricted funds. The trustees can be expected to live, work, socialize, worship, and volunteer in the same locality in which donations are solicited. In general, trustees presumably care about their reputations in such communities. In the case of national charities, trustees of charitable organizations may not necessarily care about their reputations in every locality from which funds are solicited. But trustees do probably care about their national reputations. Because a local scandal involving a charity with national operations may very well be reported in the national media, it is no stretch to conclude that even trustees of national charities care about their reputations enough to attempt not to alienate donors who live in localities other than those

177. See supra note 173.
in which the trustees live and work. Thus, to the extent accurate information can be provided to donors, the desire of a trustee to uphold her reputation in the community tends to constrain her from deviating greatly from restrictions imposed by donors. Of course, this does not alleviate the concerns raised in discussing the second and third conditions, for there the concerns relate to informational asymmetries.

A final observation on the proposal to abandon the legal enforcement of restricted charitable gifts is that it appears to prove too much in the context of publicly solicited gifts for restricted charitable purposes. Professor Atkinson anticipated this objection in its broad form, and elegantly articulated it as follows:

If moral force and the other extralegal enforcement mechanisms previously described would in fact ensure that donors’ wishes are heeded, then has my argument proved too much? If donors’ wishes will invariably be obeyed without legal enforcement, removal of legal recourse would not only do no harm; it would also do no good.¹⁷⁸

Professor Atkinson answers this objection by arguing that the breaking of commitments is often morally justified, and that enforcing commitments that have lost their moral force is generally not terribly important to donors.¹⁷⁹ He argues that in three contexts likely to arise in the case of restricted gifts, commitments have little moral force, with the result that donors who witness the breaking of such commitments should not be deterred from giving to the charitable donee in the future.¹⁸⁰ First, commitments are less morally compelling if they are not actively sought by the charitable donee.¹⁸¹ Second, dishonoring restrictions imposed by the dead is less morally troubling than dishonoring restrictions imposed by the living.¹⁸² Third, the moral force of commitments often decreases with the passage of time.¹⁸³ What is striking about Professor Atkinson’s three situations is that they have very little application in the context of publicly solicited restricted gifts. The first situation does not apply, for by definition, a donee who has publicly solicited funds for a restricted purpose has actively bargained for such gifts. The second situation is unlikely to apply, because those who respond to a charitable donee’s plea for donations to meet a specific, current need are usually living. The third situation may arise in this context, but only when the donee is soliciting funds for a long-term charitable project. In many cases, public appeals for funds have immediate charitable uses as their

¹⁷⁸. Atkinson, supra note 163, at 1130.
¹⁷⁹. See id. at 1130-31.
¹⁸⁰. See id. at 1131-33.
¹⁸¹. See id. at 1131.
¹⁸². See id. at 1131-32.
¹⁸³. See id. at 1132-33.
objects. Accordingly, in the case of publicly solicited restricted gifts, Atkinson's proposal may indeed prove too much unless one supplies an answer not yet articulated by Professor Atkinson.\textsuperscript{184} I do not mean to suggest that Professor Atkinson's proposal is inherently weak because of its lack of compelling application to publicly solicited gifts. Quite like other scholars,\textsuperscript{185} Atkinson is primarily concerned with addressing the problem of control by the "dead hand."\textsuperscript{186} Academic focus on remediating the problem of "dead hand control" by reforming the doctrine of cy pres is legitimate and beneficial. However, just as the doctrine of cy pres applies somewhat awkwardly to publicly solicited restricted gifts, so do the current reform proposals inadequately resolve the difficult and unique problems that surface in this context. Further innovation in the law is needed in this realm in which control is manifested by numerous "living hands." The next section of this article suggests one possible reform.

III. A FEDERAL INCOME TAX SOLUTION TO THE PROBLEM OF SURPLUS, RESTRICTED GIFTS RECEIVED THROUGH PUBLIC SOLICITATIONS

A. Criteria for Reform

The previous section of this article discusses several advantages and disadvantages of current cy pres reform proposals as applied to the disposition of surplus funds generated through public solicitations for restricted gifts. No single proposal appears to solve completely the problems surfacing in this context. Indeed, no proposal even purports to do so. In analyzing these proposals, the foregoing discussion has highlighted several criteria for evaluating the effectiveness of any

\begin{itemize}
  \item \textsuperscript{184} The best response is probably one based on impracticability. If compliance with the original terms of the restricted gifts becomes impracticable, honoring the original commitment is less morally compelling. If donors witnessing the breaking of the commitment by the charity can be persuaded that compliance with the restrictions truly was impracticable, future giving should not be deterred. In such circumstances, Professor Atkinson's argument would not "prove too much," for under current law, a court (rather than donors) has the sole authority to decide the existence of impracticability. The weakness with this response is its necessary assumption that donors witnessing the breaking of the commitment by the charity can be persuaded that compliance with the restrictions truly was impracticable, when donors realize that they have little expedient means for critically assessing the claim of impracticability asserted by a charitable donee. For the reasons discussed in the text, the probable tendency of charities to reach biased determinations of impracticability will likely breed skepticism in donors.
  \item \textsuperscript{185} See, e.g., Johnson, \textit{supra} note 26, at 391 ("By employing the same temporal limitations on dead hand control over charitable trusts, I propose bifurcating judicial review and modification of charitable trusts.").
  \item \textsuperscript{186} See, e.g., Atkinson, \textit{supra} note 163, at 1115 (proposing to eliminate legal enforcement of "dead hand control").
\end{itemize}
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First, the proposal should not unduly discourage charitable giving (and ideally would even promote it). Second, the proposal should not compromise the integrity of the charitable contribution deduction under Code section 170. Third, the proposal should facilitate deviation from the original purpose of publicly solicited restricted gifts when necessary to prevent the donee from losing its exemption from federal income taxation under the private benefit doctrine (or any other doctrine, for that matter). Fourth, the proposal should promote the flow of reliable information between donors and charitable donees. Fifth, the proposal should accomplish the foregoing objectives with minimal costs to donors, donees, and the judiciary.

In the following subsection, I offer one approach for tackling the issue presented. I do not presume that my proposal solves all of the problems raised thus far in this article. But I do believe that it represents an advance in current academic thought in the context of publicly solicited restricted gifts, and satisfies the criteria for evaluation better than does any other current reform proposal in this specific context.

B. Proposed Amendment to the Internal Revenue Code

I propose amending the United States Internal Revenue Code to include new section 170(f)(11), as set forth in the Appendix to this article. My proposed addition to the Code generally would disallow a charitable contribution deduction for any contribution that is restricted for one or more particular purposes of the donee organization if the taxpayer reserves in any private person (including herself) the right to receive (or otherwise control the disposition of) her contribution (or any part of it) should the donee organization fail to use the contribution for the restricted purposes. A contribution would be considered "restricted" for particular purposes in either one of two cases. The first case involves a taxpayer who has expressly required the donee organization to use the contribution for one or more particular purposes (e.g., the taxpayer executes a deed of gift requiring that her donation be used to construct a new law center). The second case is broader, and reaches all situations in which, under all of the facts and circumstances, the donee organization has represented or implied that it will use the contribution for one or more particular purposes. Such facts and circumstances would include statements made by the donee organization in soliciting or accepting

187. The general rule does not apply to any contribution that, when aggregated with all other contributions made by the taxpayer to the donee within the same taxable year, does not exceed a de minimis amount, to be determined by Congress.
the contribution, such as representations that all donations designated for a particular fund of the donee will be used for assisting victims of recent mountain fires in the Western United States.

This general rule is designed first to meet the second criterion identified above—maintaining the integrity of the charitable contribution deduction for federal income tax purposes. No longer would taxpayers be permitted to exact the cost of the time value of money on the government on account of contributions that survived the test of deductibility under the current Treasury regulations yet later wind up back in the taxpayer’s hands upon the occurrence of some contingency that was once deemed remote. No longer would courts expend time (a consideration under the fifth criterion for reform identified above) trying to determine whether the probability of the contingency giving rise to a reversion is not so remote as to be negligible. Under the general rule, if the taxpayer retains a reversionary interest in the contribution, the deduction is denied—no matter how “remote” the contingency triggering the reversion may be. This conclusion holds whether the taxpayer’s reversion is explicitly reserved or instead arises by operation of law—such as when property reverts to a donor under the cy pres doctrine because she lacked general charitable intent when the gift was made.

What about the first criterion described above? Would my proposed amendment to the Code significantly curtail charitable contributions? I doubt it. Under a special exception, a deduction that otherwise would be disallowed under the general rule is actually still available in the following limited circumstance: when the taxpayer reserves the right to direct the disposition of the contribution (or any part of it) to a “qualified entity” upon the failure of the donee organization to use the contribution for the restricted purposes. A qualified entity is essentially any entity that can receive deductible contributions under Code section 170 and that has the same status as the original charitable donee for purposes of applying that section’s special deduction ceilings.188 A qualified entity also includes the donee organization itself. Thus, the effect of the special exception is to enable a taxpayer to retain the power to direct an alternative charitable disposition of her donation (if the charitable donee becomes unable to carry out the original purpose of the gift) with no adverse federal income tax consequences.189 Further, there is no

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188. See I.R.C. § 170(b)(1)(A)-(F) (West 2001) (limiting the charitable contribution deduction for transfers to specified classes of donees based upon the taxpayer’s “contribution base”).

189. Some authorities suggest that a taxpayer who retains such a right is entitled to a charitable contribution deduction under existing law. See, e.g., Barber v. Edwards, 130 F. Supp. 83, 86-87 (D. Ga. 1955) (holding that contributions to a family-controlled charitable trust are deductible for federal income tax purposes); Rev. Rul. 68-417, 1968-2 C.B. 103 (holding that the retention of the power to change beneficiaries of a charitable remainder unitrust does not defeat the deduction otherwise available).
requirement that the qualified entity be named at the time of the original gift. A taxpayer who has reserved the right to select an alternate charitable use of her donation may do so well into the future, when the original purposes of the gift are incapable of being fulfilled. I also would recommend enacting a companion amendment to the Code providing that a charitable donee’s transfer to a qualified entity pursuant to a donor’s exercise of her reserved right will be deemed to have been made in furtherance of the donee’s tax-exempt purposes.

Allowing a taxpayer to retain such a right provides the taxpayer with a substantial voice in the use of her donation. A taxpayer who retains this right will have significant assurance that, even if her original purpose for making the gift fails, she still may decide its charitable use. How does this fact relate to the first criterion identified above (the incentive to give)? The likely effect on the incentive to give in a jurisdiction that follows the cy pres doctrine depends upon whether the donor has general charitable intent. The proposal could serve as a disincentive to give by those who have no general charitable intent at the time of making the gift, but only if such persons assume, at the time of initially making the gift, that, at the time that the original purpose of the gift becomes impossible to fulfill, they would rather recover the property than specify an alternative charitable use. That those donors would so assume is not clear, for even they may realize that as time progresses, they themselves (as opposed to a court with cy pres powers) may decide that another worthy charitable purpose has surfaced. Further, under existing federal income tax law, a donor who lacks general charitable intent may not deduct her contribution unless the probability of the contingency giving rise to a return of her contribution is so remote as to be negligible. As discussed above, this probability has been interpreted to mean “a chance which persons generally would disregard as so highly improbable that it might be ignored with reasonable safety in undertaking a serious business transaction.” Under this standard, a donor lacking general charitable intent who lawfully deducts her contribution for federal income tax purposes may not place a high value on her reversionary interest, for the probability

The proposed special exception clarifies that a deduction in such cases is appropriate for federal income tax purposes. My proposal does not address the analogous issue of whether the retention of such a right would render the gift incomplete for federal transfer tax purposes.

190. Hence, a taxpayer who retains this right of disposition has rights analogous to one who contributes to an advise and consult fund. The analogy is not perfect, of course. A taxpayer under my proposal can direct charities on how to dispose of funds not used for the original purposes of the gift.

that she may exercise it is so remote that it would be disregarded in a business context. If such is the case under existing law, my proposal would not likely serve as a major disincentive for charitable contributions by any such donor.

The proposed amendment to the Code probably creates incentives to give with respect to taxpayers who have general charitable intent. Under the cy pres doctrine, upon the failure of the charitable purposes of the gift, a court decides what to do with funds donated by those having general charitable intent. But if a donor states how donated property must be used upon the failure of the original charitable purposes, the donor’s terms are controlling. Thus, when a donor is concerned with how her gift will be used, her ability to retain the right to redirect funds upon the failure of the original purposes of the gift would likely increase her incentive to give in the first instance. In other words, a donor with general charitable intent is probably more inclined to give if she can identify precisely not only the original restricted purposes of the gift, but also any subsequent use of such gift should the original purposes fail.

Of course, under current law, a donor is free to “opt out” of cy pres by specifying that she has the right to redirect her contribution if the charitable purposes of the gift fail. How, then, does the proposed amendment improve the status quo? The answer lies in the substantiation requirements and safe harbors of my proposal. The new statutory provision would permit a deduction for a contribution that is restricted for one or more particular purposes of the donee organization only if the taxpayer substantiates the contribution by one or more contemporaneous written statements of the donee organization that contain specified information. Such information must suffice to establish the taxpayer’s entitlement to a deduction for the taxpayer’s contribution under the proposed amendment. As a general rule, the statement(s) of the charitable donee must contain the following information: (1) The amount of cash contributed, or a description of any property other than cash contributed; (2) A statement that no deduction is allowed under federal income tax law for a contribution that is restricted for one or more particular purposes of the donee organization if the taxpayer reserves (expressly or by operation of law) the right to receive, or direct the disposition of, the contribution (or any part of it) upon the failure of the donee organization to use the contribution for such purposes, unless the sole

192. See Scott, supra note 13, § 399.2.
193. A similar analysis applies in the case of donations made to donees subject to the laws of a jurisdiction that does not apply cy pres. The proposed amendment would encourage contracts of gift that eliminate the need to follow the default rule in such jurisdictions (i.e., the rule of reversion in the event of a failed gift). The likely effect on giving by donors in such jurisdictions depends upon their preferences. The discussion in the text need not be repeated with respect to that point.
persons that can receive the contribution are qualified entities; (3) A statement that the donee organization will use the contribution for one or more particular purposes of the donee organization, and a good faith description of any such purposes; (4) A good faith description of the circumstances (if any) under which the taxpayer's contribution may or shall not be used exclusively for the restricted purpose(s); (5) A description of any right that the taxpayer, with notice to the donee organization, has expressly reserved to receive, or direct the disposition of, the contribution (or any part of it) upon the failure of the donee organization to use all or any portion of such contribution for the restricted purpose(s), or a statement that the donee has not received notice from the taxpayer of having expressly reserved any such right; and (6) Whether the donee organization has received from the taxpayer any contemporaneous written statement, the terms of which are set forth in the suggested statutory amendment.

A charitable organization that accommodates a taxpayer's substantiation requirements under the statutory proposal can assist the taxpayer in availing herself of several “safe harbors.” These safe harbors are designed to facilitate the flow of very useful information from donee to donor. Under one safe harbor, a taxpayer will be deemed to have satisfied the need to substantiate her contribution with the charity's good faith description of circumstances under which the taxpayer's contribution may not be used exclusively for the restricted purpose(s) if the description sets forth the following information: (1) A statement that the taxpayer's contribution may (or shall) not be used exclusively for the designated restricted purpose(s) if doing so becomes illegal, impossible, or impracticable; (2) A statement of the person(s) or entity (such as a court, or the charitable donee's board of trustees) whose reasonable determination of such illegality, impossibility, or impracticability will suffice to alter the purpose(s) for which the contribution may be used; and (3) A statement of whether the reasonably foreseeable loss of the donee's exemption from federal income taxation will constitute grounds for altering the purpose(s) for which the contribution may be used. It is important to emphasize that the statutory proposal does not necessarily compel the statements set forth in the safe harbor. A charitable donee can dispense with restricted funds in whatever lawful manner it selects. However, one may expect that a typical charitable donee will realize that the safe harbor helpfully prompts the donee to disclose the circumstances that may prevent fulfillment of the original restricted purposes of the gift in broad outline. Moreover, although the first statement of the safe harbor merely mirrors the grounds for applying the cy pres doctrine, the second two statements add flexibility and clarity not present under current cy pres case law. The second statement prompts the charitable donee to consider vesting in
its board of trustees the contractual right to alter the purposes of the
gift if doing so becomes necessary for articulated reasons. Because
the solicitation materials in mass appeals for funds comprise the
"instrument" of gift, a charity that expressly reserves the right to alter
the restricted purposes of the gift in specified circumstances need not
petition a court in cy pres proceedings in order to do so. The third
statement of the safe harbor prompts charitable donees to expressly
think about the utility of naming the potential loss of federal income
tax exemption among the grounds for deviating from the restrictions
governing a gift. Again, by expressly incorporating into the
"instrument" of gift a provision stating that the reasonably
foreseeable loss of federal income tax exemption constitutes grounds
for deviating from the original restrictions, a charitable donee has
added assurance that it will not be forced to choose between honoring
donor instructions and forfeiting its exemption (or petitioning a court
to avoid this catastrophe). This safe harbor therefore scores high
under the third criterion for reform identified above.

Under another safe harbor, a taxpayer is deemed not to have
reserved a disqualifying right with respect to her contribution if the
taxpayer acknowledges to the donee organization in a timely
delivered written statement her agreement that in no event will the
taxpayer (or her heirs, legatees, or assigns) be entitled to receive or
direct the disposition of her contribution (or any part of it) should the
donee fail to use the contribution for the restricted purposes. A
special rule provides that this written statement may take any form,
including a writing provided by the donee organization in which the
taxpayer manifests assent to the content of the agreement just
described. Thus, a charity which asks the taxpayer to “check the box”
on a form containing boilerplate language of the described agreement
would readily facilitate the taxpayer’s compliance with this safe
harbor.

Similarly, under yet another safe harbor, a taxpayer is deemed to
satisfy the special rule permitting the reservation of a right to direct
the disposition of the contribution to any qualified entity if she
acknowledges to the donee organization in a timely delivered written
statement her agreement that the sole right reserved by the taxpayer,
with respect to all or any part of her contribution, is the right to direct
the disposition of the contribution (or any part of it) to a qualified
entity upon the failure of the donee to use the contribution for the
restricted purpose(s) of the gift. Once again, a special rule provides
that this written statement may take any form, including a writing
provided by the donee organization in which the taxpayer manifests
assent to the content of the agreement just described (such as a
“check the box” form containing boilerplate language of the
agreement).
The substantiation requirements, coupled with the safe harbors, should greatly facilitate both the flow and clarity of information between donors and charitable donees, and the drafting of concise contracts of gift between such parties, even in the context of publicly solicited gifts. I believe that a major advantage of the statutory substantiation requirements (and the related safe harbors) is the following: although the ultimate burden to substantiate restricted contributions rests with donors, charitable donees can be expected to provide all of the necessary information to donors in order to ensure their continued stream of tax-deductible donations. As between donors as a class and charitable donees as a class, the latter are much more efficient “drafters” of contractual terms governing publicly restricted gifts, if for no other reason than there is one charitable donee for every public appeal to hundreds, or even thousands, of prospective donors. Moreover, the text of the statements required under the proposed substantiation rules, as well as the statements facilitated by the safe harbors, can be expected to serve as boilerplate language that charities incorporate in the correspondence that they already send donors in their solicitation materials and in their acknowledgments described in current Code section 170(f)(8)(B). In other words, by providing a sampling of sufficient communications, the proposed amendment reduces the transaction costs to be incurred by charitable donees.\textsuperscript{194} The substantiation requirements, coupled with the safe harbors, provide an incentive for charitable donees to convey necessary information and obtain contractual representations from donors in an efficient manner that simply does not now occur consistently and pervasively. Thus, the proposal seems to fare well under the fourth criterion (promoting the flow of information) and fifth criterion (accomplishing the goals of reform with minimal costs) identified above.

Why, under current law, do charities not provide this type of detailed information, and why do they not facilitate precise (yet concise) agreements with donors, in the manner likely to occur under the proposed amendment to the Code? One plausible explanation is that many charities simply do not appreciate the quagmire of legal issues raised by public appeals for funds. As this article demonstrates, the relevant legal issues are obtuse, and perhaps non-intuitive. Another explanation is that charities who must “start from scratch” prefer not to incur the costs of investigating the law and drafting

\textsuperscript{194} Admittedly, charities will incur transition costs as they seek legal advice to ensure that their communications will adequately serve donors for purposes of meeting the new substantiation rules governing restricted contributions. In a short time, however, one would expect charities to develop forms that comply with the requirements for substantiation, and to use these forms repeatedly with little revision. Once the forms are developed, there should be few marginal costs associated with my proposal.
solicitation materials that precisely define the rights of donors and donees. Admittedly, a few charities may even prefer to keep donors uninformed of the consequences of restricted gifts. Whatever the explanation, the proposed amendment to the Code should greatly improve the way that charitable donees and donors reach an understanding of the consequences of restricted gifts, and would do so fairly efficiently.

This increased flow of information between charitable donees would likely prove beneficial in several respects. At a minimum, it should install greater donor confidence in the charitable sector. Recent events following September 11 confirm that donors are likely to lose confidence in charities when they feel they have been misled.\textsuperscript{195} My proposal should go far in encouraging open communication concerning the use of donations made in response to public solicitations for restricted funds. The likely improvement in donor confidence should itself promote charitable giving (a positive result under the first criterion for reform).\textsuperscript{196} Moreover, as I have observed elsewhere, the charitable sector would probably benefit in other respects from greater accountability to donors.\textsuperscript{197} The information that donors must obtain from charities under the substantiation requirements should facilitate such accountability in general. More particularly, the required disclosure concerning whether the donor has retained the right to redirect her contribution (or any part of it) to a qualified entity (if the original restricted purposes of the gift fail) will tend to place some pressure on charities to provide this option to donors, who under the proposal will be informed that they can reserve that right without incurring adverse federal income tax consequences.\textsuperscript{198}

\textsuperscript{195} David McLaughlin, chairman of the board of governors of the American Red Cross, has confirmed this point by stating that the failure of the institution to subject itself to public scrutiny would prevent it from securing the trust of the general public. See Levine, supra note 5, at 28.

\textsuperscript{196} Cf. Karst, supra note 15, at 434-35 (observing that some degree of regulation should be welcomed by “[f]riends of private philanthropy,” for the sustained viability of the charitable sector depends upon public confidence that charities are operating efficiently).

\textsuperscript{197} See Johnny Rex Buckles, The Case for the Taxpaying Good Samaritan: Deducting Earmarked Transfers to Charity Under Federal Income Tax Law, Theory and Policy, 70 Fordham L. Rev. 1243, 1325-32 (2002). The American Red Cross has begun to recognize this fact. See Red Cross Pitches to Get Specific; Ads to Clarify How Money Will Be Spent, supra note 1.

\textsuperscript{198} My proposal does not directly impose disclosure requirements on charitable donees, nor does it assess any fine on charitable donees who fail to supply information to donors. Instead, following the model of existing Code section 170(f)(8), the proposal places on taxpayers (donors) the burden of obtaining the required statements from charitable donees. Further, my proposal contains an exception to the substantiation requirements if the donee reports the necessary information on a return filed with the IRS, as does Code section 170(f)(8)(D). These and other elements of my proposal are designed to enable it to survive scrutiny under judicial precedent interpreting the First Amendment to the United States Constitution. For a
Ultimately, my proposal should encourage efficient extra-judicial resolution of how to dispose of surplus funds. Through the proposed substantiation requirements and safe harbors, donors and donees would be expected to enter into semi-standardized contracts of gift by which they sketch the circumstances that justify a departure from the original restrictions governing donations. Donees that desire to maximize contributions from the public would, through a safe harbor, be able to facilitate taxpayers' reservations of rights to designate alternative charitable uses upon the failure of the original purposes. Less frequently would donees need to resort to the courts in costly, unpredictable cy pres proceedings. Donors and donees could simply agree to alternative dispositions of funds once the original purposes have failed. Because my proposal does not eliminate the legal enforcement of restricted gifts, the looming oversight of charities by the state attorneys general (and the threat of litigation to curb abuses of the public trust) should help to minimize the dissemination of misinformation to donors by donees with respect to the existence of circumstances justifying a deviation from the original restrictions.

In short, my statutory proposal should help effectuate the goals of the most prominent cy pres reformers by promoting efficiency in the charitable sector through cost-effective, private agreements between donors and donees.

IV. CONCLUSION

Under existing law, a charitable organization that publicly solicits funds for a designated purpose generally must use such funds for the purpose specified in the solicitation materials. Deviation from the restricted purpose may be permitted in certain circumstances if the governing jurisdiction recognizes the doctrine of cy pres. The doctrine of cy pres, however, is not easily applied to surplus restricted gifts raised through public appeals. Federal income tax law renders the application of the doctrine of cy pres to publicly solicited surplus funds especially complex. Current proposals to reform the doctrine of cy pres do not adequately resolve, or even address, the legal problems raised by publicly solicited surplus donations.

My solution to the problems created by publicly solicited surplus contributions to charity is to amend the Internal Revenue Code by enacting a new provision that limits the charitable contribution deduction for contributions made for particular charitable purposes of the donee. My proposed amendment denies a charitable contribution deduction in most cases in which a taxpayer reserves rights (explicitly

sampling of the constitutional issues raised by the regulation of charitable solicitation, see Riley v. National Federation of the Blind, 487 U.S. 781 (1988). A comprehensive constitutional justification of my proposed amendment is beyond the scope of this article.
or by operation of state law) in contributed sums. In addition, a
taxpayer otherwise entitled to a charitable contribution deduction
may not lawfully claim it unless she substantiates the contribution
with one or more statements of the donee organization that contain
prescribed information.

Although my proposal takes the form of an amendment to the
Internal Revenue Code, I do not believe that the proposal’s viability
depends upon quantifying the revenue loss associated with the current
rules for deducting restricted charitable gifts that are subject to a
contingency. That a real federal income tax interest is served by the
proposal is sufficient to justify an amendment to the Internal Revenue
Code. Far more important than the proposal’s revenue effect is its
likely effect on the way that charitable donees and donors will “do
business” in raising funds for a designated charitable purpose. The
probable effect of the proposed amendment is an efficient increase in
the exchange of information between donors and donees, and added
clarity in how surplus funds raised through public solicitations will be
directed. In essence, the proposal should encourage charitable donees
and donors to enter into gift agreements that largely avoid many legal
problems arising under the doctrine of cy pres. The proposal should
benefit donors, charitable donees, the courts and the public at large.

APPENDIX

ADDITION OF NEW INTERNAL REVENUE CODE
SECTION 170(f)(11)

Sec. 170. CHARITABLE, ETC. CONTRIBUTIONS AND GIFTS.

(f) DISALLOWANCE OF DEDUCTION IN CERTAIN CASES
AND SPECIAL RULES. —

(11) RESTRICTED CONTRIBUTIONS WITH RESERVED
RIGHTS. —

(A) IN GENERAL.— No deduction shall be allowed under
subsection (a) for any contribution that is restricted for one or more
particular purposes of the donee organization if the taxpayer reserves
(expressly or by operation of law), in the taxpayer or any person other
than the donee organization, the right to receive, or direct the
disposition of, all or any portion of such contribution upon the failure
of the donee organization to use all or any portion of such
contribution for such purposes.

(B) EXCEPTION FOR CHARITABLE DISPOSITIONS.— No
deduction shall be disallowed under subparagraph (A) solely because
the taxpayer reserves, in the taxpayer or any other person, the right to
direct the disposition of all or any portion of such contribution to a
qualified entity upon the failure of the donee organization to use all or
any portion of such contribution for such one or more purposes of the
donee organization for which the contribution is restricted. For
purposes of this subparagraph (B), a taxpayer’s reservation of a right,
in the taxpayer or any other person, to direct the disposition of all or
any portion of such contribution to a qualified entity —

(i) shall include the right to restrict such contribution (or portion
thereof) for one or more particular purposes of such qualified entity,
and

(ii) shall include the right to direct the disposition of all or any
portion of such contribution to more than one qualified entity.

(C) SUBSTANTIATION REQUIREMENT.—

(i) IN GENERAL.— Notwithstanding subparagraphs (A) and (B), a
deduction otherwise allowable under subsection (a) for a contribution
that is restricted for one or more particular purposes of the donee
organization shall not be allowed unless the taxpayer substantiates the
contribution by one or more contemporaneous written statements of
the donee organization that meet the requirements of clause (ii).

(ii) CONTENT OF WRITTEN STATEMENTS OF DONEE.—
The contemporaneous written statement or statements of the donee
organization shall meet the requirements of this clause if they
collectively set forth facts sufficient to establish the taxpayer’s
entitlement to a deduction for the taxpayer’s contribution under this
paragraph. Such facts shall include the following information:

(I) The amount of cash and a description (but not value) of any
property other than cash contributed,

(II) A statement that no deduction is allowed under Federal income
tax law for a contribution that is restricted for one or more particular
purposes of the donee organization if the taxpayer reserves (expressly
or by operation of law), in the taxpayer or any person other than the
donee organization, the right to receive, or direct the disposition of,
all or any portion of such contribution upon the failure of the donee
organization to use all or any portion of such contribution for such
purposes, unless the sole person or persons that can receive all or any
portion of such contribution satisfy the definition of a qualified entity
(as defined in section 170(f)(11)(C)(ii)),

(III) A statement that the donee organization will use the
contribution for one or more particular purposes of the donee
organization, and a good faith description of any such purposes,

(IV) A good faith description of the circumstances (if any) under
which the taxpayer’s contribution may or shall not be used exclusively
for the purpose or purposes referred to in subclauses (II) and (III),

(V) A description of any right that the taxpayer, with notice to the
donee organization, has expressly reserved, in the taxpayer or any
person other than the donee organization, to receive, or direct the
disposition of, all or any portion of such contribution upon the failure
of the donee organization to use all or any portion of such
contribution for the purpose or purposes referred to in subclauses (II) and (III), or a statement that the donee has not received notice from the taxpayer of having expressly reserved any such right,

(VI) Whether the donee organization has received from the taxpayer a contemporaneous written statement described in paragraph (H)(i)(I), and

(VII) Whether the donee organization has received from the taxpayer a contemporaneous written statement described in paragraph (H)(ii)(I).

(iii) CONTENT OF GOOD FAITH DESCRIPTION OF CIRCUMSTANCES.— Any good faith description required by paragraph (C)(ii)(IV) need not specify in detail every contingency under which the taxpayer’s contribution may or shall not be used exclusively for the purpose or purposes referred to in subclauses (II) and (III) of paragraph (C)(ii). Such good faith description will satisfy the requirements of paragraph (C)(ii)(IV) if it contains the following information:

(I) A statement that the taxpayer’s contribution may or shall not be used exclusively for the purpose or purposes referred to in subclauses (II) and (III) of paragraph (C)(ii) if doing so becomes illegal, impossible, or impracticable,

(II) A statement of the entity, person or persons whose reasonable determination of such illegality, impossibility, or impracticability shall suffice to alter the purpose or purposes for which such contribution may be used, and

(III) A statement of whether the reasonably foreseeable loss of the donee’s exemption from federal income taxation shall be sufficient grounds for altering the purpose or purposes for which such contribution may be used.

(iv) COORDINATION WITH SECTION 170(f)(8) AND SECTION 6115.— The information specified in clause (ii) may appear in any contemporaneous written statement or statements of the donee organization, including (but not limited to) a contemporaneous written acknowledgment described in section 170(f)(8)(A) and a written statement described in section 6115(a).

(v) SUBSTANTIATION NOT REQUIRED FOR CONTRIBUTIONS REPORTED BY THE DONEE ORGANIZATION.— Clause (i) shall not apply to a contribution if the donee organization files a return, on such form and in accordance with such regulations as the Secretary may prescribe, which includes the information specified in clause (ii) with respect to the contribution.

(D) RESTRICTED PURPOSES.— For purposes of this paragraph, a contribution is “restricted for one or more particular purposes of the donee organization” if

(i) the taxpayer has expressly required the donee organization to
use the contribution for one or more particular purposes of the donee organization, or
(ii) under all of the facts and circumstances (including, but not limited to, statements made by the donee organization in soliciting or accepting such contribution), the donee organization has represented or implied that it will use the contribution for one or more particular purposes of the donee organization (other than such purpose or purposes as the donee may unilaterally select after accepting the contribution).

(E) QUALIFIED ENTITY.— For purposes of this paragraph, a “qualified entity” is any entity described by the same subparagraph of section 170(b)(1) as is the donee organization. The term “qualified entity” shall also include the donee organization.

(F) CONTEMPORANEOUS.— For purposes of this paragraph,
(i) written statements of the donee organization are “contemporaneous” if the taxpayer obtains them on or before the earlier of the dates specified in section 170(f)(8)(C), and
(ii) any written statement from the taxpayer to the donee organization is “contemporaneous” if the taxpayer delivers it to the donee organization on or before the earlier of the dates specified in section 170(f)(8)(C).

(G) CRITERIA FOR SUFFICIENCY OF FACTS THAT MUST BE SUBSTANTIATED.—

(i) GENERAL RULE.— For purposes of paragraph (C)(ii), the contemporaneous written statement or statements of the donee organization shall be deemed collectively to set forth facts sufficient to establish the taxpayer’s entitlement to a deduction under this paragraph if such facts, considered under all relevant law, would justify the claiming of a deduction under this paragraph, assuming all other requirements of a deduction under section 170 have been satisfied.

(ii) SPECIAL RULE FOR RELINQUISHMENT OF RIGHTS.— Notwithstanding clause (i) of this subparagraph and paragraph (C)(i) and (ii), the contemporaneous written statement or statements of the donee organization shall be deemed collectively to set forth facts sufficient to establish the taxpayer’s entitlement to a deduction under this paragraph if they—

(I) set forth the information required by subclauses (I) through (V) of section 170(f)(11)(C)(ii), and

(II) acknowledge that the taxpayer has delivered to the donee organization a contemporaneous written statement described in paragraph (H)(i),
assuming all other requirements of a deduction under section 170 have been satisfied.

(iii) SPECIAL RULE FOR RESERVATION OF RIGHT
SOLELY TO DESIGNATE QUALIFIED ENTITIES.—
Notwithstanding clause (i) of this subparagraph and paragraph (C)(i) and (ii), the contemporaneous written statement or statements of the donee organization shall be deemed collectively to set forth facts sufficient to establish the taxpayer’s entitlement to a deduction under this paragraph if they —

(I) set forth the information required by subclauses (I) through (V) of section 170(f)(11)(C)(ii), and

(II) acknowledge that the taxpayer has delivered to the donee organization a contemporaneous written statement described in paragraph (H)(ii),

assuming all other requirements of a deduction under section 170 have been satisfied.

(H) SPECIAL RULES.—

(i) SPECIAL RULES IN THE CASE OF RELINQUISHED RIGHTS.—

(I) For purposes of this paragraph, a taxpayer shall be deemed not to have reserved, in the taxpayer or any person other than the donee organization, the right to receive, or direct the disposition of, any portion of a contribution restricted for one or more particular purposes of the donee organization, if the taxpayer acknowledges to the donee organization in a contemporaneous written statement delivered to the donee organization the taxpayer’s agreement that in no event shall the taxpayer or the taxpayer’s heirs, legatees, or assigns be entitled to receive or direct the disposition of all or any part of such contribution upon the failure of the donee organization to use all or any portion of such contribution for such purposes.

(II) A written statement described in subclause (I) need not take any particular form, and may consist of a writing provided by the donee organization in which the taxpayer manifests assent to the content of the agreement described in subclause (I).

(ii) SPECIAL RULE IN THE CASE OF RESERVED RIGHTS TO DESIGNATE QUALIFIED ENTITIES.—

(I) For purposes of this paragraph, a taxpayer shall be deemed to have satisfied the requirements of paragraph (B) if the taxpayer acknowledges to the donee organization in a contemporaneous written statement delivered to the donee organization the taxpayer’s agreement that the sole right reserved by the taxpayer, in the taxpayer or any other person, with respect to all or any part of the taxpayer’s contribution, is the right to direct the disposition of all or any portion of such contribution to a qualified entity upon the failure of the donee organization to use all or any portion of such contribution for the purposes for which the contribution is restricted.

(II) A written statement described in subclause (I) need not take any particular form, and may consist of a writing provided by the donee organization in which the taxpayer manifests assent to the
content of the agreement described in subclause (I).

(iii) SECTION NOT TO APPLY TO DE MINIMIS CONTRIBUTIONS.—This paragraph shall not apply to any contribution which, when aggregated with all other contributions made by the taxpayer to the donee organization within the same taxable year, does not exceed [§XX].