of the interest and "adequacy" of the security provided for in donor-foundation loans. Anglo-American trust law has long recognized the impossibility of insuring that a trustee who is permitted to deal with himself will act fairly to the trust. As a result, the courts have refused to inquire as to the fairness of dealings between a trustee and a trust and have generally barred such transactions.

Because of the potential private benefit which may result from self-dealing, it is imperative that the Internal Revenue Service examine such transactions in detail in order to determine whether there has been a violation of the existing rules. However, such examinations require the skill of highly trained revenue agents and are both time consuming and expensive. The Internal Revenue Service has estimated that the "cost" (both direct costs and the amount of revenue which would be produced if the agent were free to spend his time on matters involving the collection of taxes) of 1 man-year of an experienced revenue agent's time exceeds $320,000.

Much of the Service's problem in policing self-dealing transactions is traceable to concepts such as "reasonableness" and "adequacy" and measures such as "substantial" which are contained in the existing self-dealing rules. The administrative problems created by the use of such terms are severe in the foundation area. This is largely attributable to the fact that often no one is looking over the shoulder of the trustee of a private foundation to make sure that the transaction is, in fact, at arm's length. Indeed, the "arms" involved may both belong to the same person who is both donor and trustee. Moreover, the possibility of arranging transactions with a foundation to suit the needs of the donor are more numerous than in other areas. For example, if a donor wishes to obtain the use of the foundation's funds at a minimum cost he will arrange for the loan to bear a low rate of interest. On the other hand, if a donor wishes to make a deductible contribution to his foundation which is in excess of the generally applicable percentage limitation, it would be possible for him to set a high rate of interest.

The following examples indicate the types of self-dealing cases which are being entered into and the difficulty which the Internal Revenue Service has in applying the arm's length test contained in existing law:

Example 1.—The A foundation made a loan to a business corporation controlled by its donor. The security for the loan consisted of an oral promise made by the donor as an officer of the corporation to execute a mortgage on certain of the real property owned by the corporation, but only if the foundation requested such a mortgage. The foundation, however, never requested the donor's corporation to execute such a mortgage. The Internal Revenue Service challenged the exemption of the foundation on the grounds that the organization had made a loan without the receipt of "adequate" security. The Service argued that if the corporation were to become insolvent, the foundation, with only an unrecorded promise to execute a mortgage in the future, would be in the same position as any other unsecured creditor. However, the court, although recognizing that the security interest of the foundation would be ineffective if the corporation disposed of the real property, felt that a mere promise to execute a mortgage in the future constituted "adequate" security. Thus,