PRIVATE FOUNDATIONS

HEARINGS

BEFORE THE

SUBCOMMITTEE ON FOUNDATIONS

OF THE

COMMITTEE ON FINANCE

UNITED STATES SENATE

NINETY-THIRD CONGRESS

SECOND SESSION

ON

THE ROLE OF PRIVATE FOUNDATIONS IN TODAY'S SOCIETY AND A REVIEW OF THE IMPACT OF CHARITABLE PROVISIONS OF THE TAX REFORM ACT OF 1969 ON THE FUNCTION AND OPERATION OF PRIVATE FOUNDATIONS

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PRIVATE FOUNDATIONS

MONDAY, MAY 13, 1974

U. S. SENATE,
SUBCOMMITTEE ON FOUNDATIONS,
COMMITTEE ON FINANCE,
Washington, D.C.

The subcommittee met, pursuant to recess, at 10:10 a.m., in room 2221, Dirksen Senate Office Building, Hon. Vance Hartke presiding.

Present: Senator Hartke.

Senator HARTKE. The committee will please come to order.

Today we begin the first in a series of hearings to be held this year by the Subcommittee on Foundations.

Four years ago, foundations were one of the prime targets of tax reform legislation. Congress closely examined the benefits received by the public from the tax exempt afforded foundations. Almost all of the witnesses appearing before the Senate Finance Committee in 1969 agreed that there were abuses of the tax exemption privilege by foundations.

Some saw the accumulation of wealth in the hands of a few and its use to further the personal interests of those long deceased as inconsistent with our democratic values. Still others objected to foundation activities in politically sensitive areas. And some objected to foundation control of segments of the private sector.

On the other side were posed those in the foundation community who saw private charity as relieving government of responsibilities it would otherwise have to discharge, and those whose programs depended on the support of foundation grants.

There are those who say now that the Tax Reform Act of 1969 cured most of the ills afflicting the foundation community. Quite frankly, I have no idea whether that assertion is true. In fact, I am concerned about our continuing lack of knowledge in this field.

Hard facts were lacking when Congress acted in 1969—they are still in short supply today. On March 22 of this year, I sent a letter to the Commissioner of Internal Revenue, Mr. Donald Alexander, asking him to respond to 17 essential questions. I am placing that letter in the hearing record so that the public may become aware of some of my initial requests for the information which has been lacking so far.[1]

Those 17 questions can be grouped into two categories:

First, how is the IRS organized to administer tax exempt organizations, and just what administrative functions does it now per-

[1] See p. 110.

form? Along this line, I asked for projections of what changes might occur if the special office within IRS for tax exempt organizations proposed in both House and Senate pension bills becomes law.

Second, just what impact has the 1969 Tax Reform Act had on exempt organizations? How many new foundations have been created Since 1969? How many have gone out of existence? How many have changed their exempt status to or from a private foundation? What evidence is there that the 1969 act has resulted in proportionately more foundation wealth going to charitable purposes?

Unfortunately, Commissioner Alexander was unable to be with us today, but he will appear before this subcommittee within the next few weeks. If the IRS is able to respond to my questions, the data will shed some useful light on this important subject.

Let me make it understood at the outset that I come into these hearings with an open mind. I have no predetermined position on private foundations. These hearings are designed to help the members of this subcommittee assess the position and the role of foundations in our society. This is 1974—not 1969, and we will not rehash the arguments of the past. Instead, I want to know just what foundations are doing today and where they may be going in the future.

In making this assessment, it is not enough to say that private charity has been around since the Romans, or that it had an important place in the very early days of this Republic. All of this is true, but it says very little about the role of private charity today.

Nor is it enough to say that, if private foundations ceased to exist, government would have to take up the slack. If foundations are merely on a parallel course with government, they are existing on a very slender reed.

The meaning of private charity has changed from the days of the Romans and colonial America. Perhaps it is not so much that it has changed, but that it has expanded. We may still need private efforts to aid the poor and the handicapped and the infirm, but there is now a much greater need for private charity.

Foundations have a unique opportunity as we begin the third century of our experiment in democracy. They can be true philanthropic by providing for new opportunities to open our society to new ideas and new approaches to the solution of problems which have plagued mankind for centuries. There is injustice all around us, from malnourished babies, to needless deaths which result from insufficient medical knowledge, to inadequate housing and insufficient education, to human lives which are wasted because we have erected barriers in our society or in our economy which have inhibited people from achieving their full potential.

So much remains to be done, and foundations have the resources and the freedom to meet the challenge. From the smallest to the biggest, foundations can help to solve community and national problems.

What was asked in 1969 will also be asked in 1974—just how much does the public benefit from the tax subsidy which it gives to private charity? That is the ultimate question before this subcommittee, and I suggest that private foundations and their grantees can answer

that question best by defining their purposes in terms of essential American needs.

In a speech I made earlier this year, I made the following pertinent points:

1. There is nothing in American society which requires that foundations exist. Public needs can be defined by elected officials who are responsive to the people they serve.

2. Rather than consider foundations "essential" to American society, we should talk of their "desirability". Ours is a pluralistic society, and we should encourage the participation of diverse groups of citizens in the process of defining and meeting the needs of people. Foundations can help fill this need.

3. If foundations are to earn their right to continued existence, they must have a well-defined purpose and clearly delineated policies in pursuit of that purpose.

I do not say that all foundations are without a clear purpose, but I do say that the foundation community as a whole is lacking a clearly defined conception of their role in contemporary American society.

I believe that foundations should be the cutting edge of innovation and experimentation, that they should be probing the resources of America so that we can raise the quality of life for all Americans.

It is true that some foundations came into existence for the purpose of tax avoidance, but if those same foundations use their resources to better our way of life, the motives behind their creation may be inconsequential. What I am suggesting is that we look beyond the superficial issues to determine just how the public is benefiting from the wealth of private foundations.

This subcommittee can shed some light on this question, but foundations themselves must undergo a critical period of self-examination. They must determine just how well they are responding to the needs of our society.

In my February speech, I also suggested that foundations should open themselves to the public. I recognize that vast improvements have been made in terms of annual reports, newsletters and the like—but I have a greater meaning in mind. There is an inherent danger in private foundations where the boards of directors are composed of wealthy people who may be associated with other charitable endeavors. This is an elitist danger, and it can only be resolved by expanding boards to include more members of the public and opening up the grantmaking decision process to the public to a greater extent than is now practiced.

The current strain of elitism means that foundations may be all too prone to support "safe" activities—activities which reflect the values of the members of the board. Diversification of the personnel involved in the grant-making decision process will open up foundations to new insights and new approaches.

I realize that I am painting with a broad brush, but the public views foundation activity in terms of its general impact and its general value. I do not discount the work done by many individual foundations, by the Council on Foundations, and by local and regional associations of foundations to encourage innovation and facilitate cooperation among foundations. By and large, the foundation

community is a responsible one which seeks to avoid the mistakes which led to provisions of the Tax Reform Act of 1969.

At the same time, I note that the excellent program of the recent annual conference of the Council on Foundations was entitled "Blueprints for Survival". There is a certain defensiveness connotated by that title—a defensiveness which recognizes that the foundation community remains under attack. But the best defense is an offense, and I trust that foundations will take to the offense, not in a public relations effort to show us how many grants they make or how much money they spend, but an offense based on the substance of progress and positive contribution to our society.

I open these hearings both with a concern about the role of foundations in our society today and an excitement about the potential of that role. There is much to be done to make the dreams of our founding fathers and the hopes and aspirations of all American men and women a reality. If the wealth of foundations can be harnessed in the effort to realize those dreams, they will have the support of this subcommittee and of the American people.

Our first witness today is the Reverend Monsignor Geno Baroni who is president of the National Center for Urban Ethnic Affairs in Washington, D.C.

Good morning.

STATEMENT OF MSGR. GENO BARONI, PRESIDENT, NATIONAL CENTER FOR URBAN ETHNIC AFFAIRS

Reverend BARONI. Good morning.

Senator HARTKE. Delighted to have you here.

Now, let me say at the beginning that every statement will be included in the hearing record in full, as though it were read in its entirety. And if you care to summarize your statement, you certainly may do so.

Reverend BARONI. Mr. Chairman, my name is Geno Baroni, and I am the president of the center, the National Center for Urban Ethnic Affairs here in Washington, D.C. I welcome this opportunity and invitation to be present.

I appear before this subcommittee in concern and responding to the speech that you had recorded or printed in the Congressional Record of April 11.

My own experience since 1960 has been in urban affairs, primarily here in Washington, D.C. and nationally with urban task forces concerned about racial and ethnic groups in the United States. And I wanted to respond, Mr. Chairman, to your remarks, some of which you immediately quoted here again this morning in terms of private foundations in search of a purpose.

Number one, you spoke of the desirability of foundations in a pluralistic society. I agree that foundations can serve a useful purpose, and that we should encourage the participation of diverse groups of citizens in the process of defining and meeting the needs of people.

In terms of that point, I wish to share with you, Mr. Chairman, in addition to my own written remarks, that I support the need and

desirability of foundations in our society, and the good work they have done. However, I am especially concerned that many foundations do not accept the notion that you have expressed and that I support, that ours is truly a pluralistic society. The notion of a pluralistic society has to be recognized in our public educational system and also by foundations. We have seen foundation grants to cultural institutions, medical institutions, scientific institutions, universities and some efforts by foundations to relate to minorities. My experience, Mr. Chairman, shows that many foundations have ignored a large group of middle Americans, have ignored a large group of working class people who live in the cities, who are not minorities, who are not related to the universities, who are not related to foundations, who are not related to the upper middle class. To ignore lower income, middle American, whites, who live in urban areas is to exacerbate the tensions of our society. This is where the foundations need to do more work if they are going to get more respect from the diverse groups of our society.

Much of my work is to sensitize private and public institutions to the ethnic facts of urban society. In the cities where I have worked since 1968, in particular with the members of my family, whites are often referred to as pigs, or hardhats, or racists just because they live next to blacks in urban areas. I spent my whole life fighting for justice and equality, 10 years in the Washington ghetto, before that in western Pennsylvania in terms of coal mines and steel workers and railroad workers. And I believe that many, many of our public and private institutions have not been sensitive to the alienation, the economic, the social, the cultural, the political alienation of the so-called silent majority. And I believe that the children of workers, and the grandchildren of workers, like myself, sometimes just do not know the right people in many of the foundations, we have just not gone to the same colleges, we have not belonged to the same clubs. Often I am advised in going to a foundation that I really ought to know this member of the board or that member of the board. So, I believe the board of directors of the foundations ought to be more diversified.

This lack of diversity sometimes creates a bias of sometimes an elitism or sometimes a hostility that backfires. We have foundation support for programs in urban areas like Newark, Detroit, Rochester, and many other cities. In our work in about 25 cities, I find that the people who live next to the ghetto are heavily American ethnics. The destiny of cities like Boston depends on neighborhoods and on these ethnic and minority groups' surviving together. I am very interested in the convergent issues between the inner city and people next to them who happen to be very heavily eastern, southern European, middle American ethnics. I am interested in seeing that public policy, in terms of the urban crisis, will only begin to deal with the urban crisis when we understand the ethnic and working class factor as well as the racial factor. I believe some foundations have recognized this, but not enough.

When I go to a foundation and I say I am dealing with the white/black relationship from the white ethnic group perspective, I'm told, "you people are the hard hats or the racists." And I say, "no, if we

are part of the problem as whites who live next to the blacks, then we must be a part of the solution." As one person said in a group in Baltimore, "you know, people in the ghetto may have a broken back, and they need more help, but we also need help for the person with a broken toe who is not the same as the person with the broken back, and it should not be an either/or," and so we are talking about equity. In fact, I think there is more hostility in working class ethnic groups, not toward minorities, but sometimes towards our intellectual society, more often towards the leadership of our society.

Second, you called for greater public participation on governing boards. I would submit that, there are names like Sirica or Rodino or Jaworski which would hardly be found on many foundation boards. I think foundations have made progress in terms of women and minorities on their boards, but they must go beyond that to represent the real pluralism of American society.

I would also say in terms of this, not only am I concerned about support for foundations, and public support will only come when foundations respect and make legitimate the pluralism, the ethnic, the racial, and life style pluralism of our American society. In our brief attempt to study and look at foundations in the last few years, there is much more that needs to be done in terms of the pluralism of grants, members of staff, as well as the board of directors.

Third, I am concerned with the point you made, "that foundations should have a unique ability to be far-sighted, so that they can look into the future, particularly in the area of public education." There is no area that is more critical in our society, and this is ironic because this week we celebrate the Supreme Court Decision of 1954, on May 17, on desegregation.

The challenge of a divided society faces us in Northern urban cities. Take a city like Boston, with more than 60 colleges and universities. It cannot integrate, and the burden seems to be put on the minority community and the working class ethnic community living next door. It is very, very hard to find foundation support for programs that deal with both sides of that agenda, to deal with the real issues in public education that might help us to deal with northern urban problems.

We do not have an intercultural dimension in American education. In fact, American education has been monocultural. The model has been "Dick and Jane" and "Miss Virginia Slim." It has not been legitimate in American education to be either minority or ethnic. Ethnic pluralism has not been legitimate and this creates resentment. This creates resentment not only toward minorities, but also it creates resentment toward the establishment group. It creates resentment to those people that set policy. It creates resentment because people used to believe "whatever the teacher said," was gospel, whatever the university wanted we supported, we supported tax bonds for universities at any level. Now many middle Americans are very "up tight" about the educational establishment. They are very "up tight" and they have been made to feel that they are the problem. In terms of our society, in the area of education very, very little has been done, and few foundations are interes ed in how do we deal with the pluralism of American society in terms of class, in terms of the

ethnic factor, and in terms of race. And here I believe we have a great challenge.

Fourth, you mentioned that foundations must recognize the undercurrents of change which are running through our society and make grants which help influence that change. I agree with that very, very much in terms of present challenges in American life, there is no national social policy. Many programs like OEO, housing, education, and desegregation efforts—and I was very heavily involved—no longer have support because sometimes they ignored people who lived next to the ghetto. What we do not have in this society is programs to help neighborhoods stabilize, to stabilize changing neighborhoods, to help stabilize ethnic and minority neighborhoods in terms of housing, for example, the abandonment of the ghetto, and the de-investment of the working class neighborhoods which is like a cancer ruining our communities. One negative thing I found in terms of the 1969 act is that some foundations are afraid to work with community groups. Whether or not it is legitimate to say they are afraid of the Tax Act of 1969, they say "well, we don't want to work with community groups because we might get in trouble with the IRS" or "the Tax Act of 1969 has some warning signs, or red lights or yellow lights of caution about working with community groups." I am not saying they should use that as an excuse. I am wondering if Congress should not encourage foundations to work with people at the neighborhood level to help stabilize neighborhoods where people live, where blacks and whites and brown people live, and where the hearts and souls of the cities are, and where people are going to have to work together.

And finally, your fifth and sixth points were that you said "foundations in terms of the 200th national birthday ought to be able to help us redefine some objectives of our American society." And you also mentioned that they ought to be able to speak to the frustration and anxiety and create an atmosphere in this country which will encourage new voices, new ideas and new approaches. I would submit, Mr. Chairman, that our country today is going through an identity problem. We do not have a national sense of identity. We do not have a national sense of purpose. We do not have a national sense of commitment. From the young people and their lifestyle, to minority people, to working class people, everybody is saying who am I, who are we as Americans. I believe that the diversity of our society and its pluralism is an important part in recognizing this. I believe that in these terms many people of good will do want to work together. I believe that we can work together if in our American society we recognize that we are not a "melting pot," but we are the most ethnically, racially, and pluralistic country in the world, and if we can recognize and accept our diversity, we will find better ways to work together.

One of the things that I do in neighborhoods is to try to find common issues, what are the common convergent issues between minority people and ethnic working people within our cities. What do we need to do to create a stabilized racial and ethnic community? What do we need to do to create a good school? We do not even know what a good school is. The reason that my family and people

are so angry is they have been abandoned. They say a good school is where the teachers, and the doctors, and the lawyers and professors are. So, if the educated group of Americans would integrate, the working class would follow.

The working class hostility is not as much against the minorities about integration, but it is against the universities and the leadership which fails to bear the burden of social change. So, unless we help working people to bear that burden of social change, I do not think that our cities are going to survive. So, I think there is a great challenge.

I have seen a lot of good work on the part of foundations throughout the country, and I am very supportive of that work. I believe that Congress ought to encourage foundations, as you are indicating, and particularly on the Tax Law of 1969. I think we should encourage them not to be fearful and if there were abuses in the past, not to be fearful of neighborhood programs and to work with ethnic and racial communities which are the life and death of cities, and the life and death of America between racial groups, poor groups, rich and poor.

Senator HARRIS. I would say, Monsignor, you know, not to inject politics into this, but there is a politician in the South by the name of George Wallace who frequently makes a charge about the Democratic Party, of which I am a member, and the Republican Party, that there is not a dime's worth of difference between them, and sometimes he says he wants to deliver a message to Washington. And I frequently have said that you may criticize his own philosophy or his own beliefs, but at least what he is saying in substance is that neither one of the political parties, nor the Government itself, has been able to define that national purpose that you are talking about. I understand that when you come into OEO or into Housing and Urban Development that these are program-oriented operations without understanding what the definite objective was for the totality of society. You see all of these people talking about ghettoes, but you see very few people who are really concerned about eliminating ghettoes as a fact in American society. You hear all this conversation about cities deteriorating at a rapid rate, but you see no one really doing anything about it.

I was here and I looked out and saw Washington burning. I heard everyone talking about how we are going to repair 14th Street and 7th Street. Those scars are still there. I mean, they are visibly there. If anyone wants to take a look you can go see them yet. You see the boarded up walls and you see plastered advertisements on the side of those walls as sort of the billboards of America, something like to billboards of China.

Let me ask you in this, do you really believe that if you changed and modified the boards of directors, expanded the boards of directors, that in and of itself would effect a material change in the foundations?

Reverend BAROZI. I suppose not. I suppose not entirely. But, I would say what is important about that, Senator, is that in recognizing diversity, just as recognizing that women should be present and participate, and that minorities should be more participatory,

I think it does give us a bigger vision of the main characteristic of American life which is cultural diversity. In terms of recognizing that factor, whether it causes us problems or not, and when we recognize that then we find out what are the good things that can bring people together for the common good and good will. And I want to say that I have lived on 14th Street here in Washington for 10 years. I bought 3&1 houses to rehabilitate for low income families. But, I saw that Federal housing programs 235 and 236 and 237 stopped because we do not have political and community support. We did not have support with some of my brothers and sisters who did not want a new house or a rehab, but only needed $2,000, or $3,000 in a changing neighborhood to fix up their home with new shingles. They were told that they are not eligible because they do not live in a Model Cities area, they didn't live in an urban renewal area, they were in a "changing" area and they should move away. And they do not want to move away. So, I am saying it is not an either or. Much more work needs to be done, as I said, with the person with the "broken back" as well as the person with the "broken tax," and that is not an either or.

Senator Harris. What you are saying in substance then is that part of this anxiety, part of the conflicts in this Nation among people is really due to the fact that you are putting them in two categories, one category which is very poor, and the other category in the other group which needs no help whatever or very little help whatsoever. And therefore you are creating more conflict than you eliminate. Is that a fair statement?

Reverend Barnes. Well, I think it is more in terms of the other kinds of pathologies you mentioned earlier in terms of the national or public support, and we have no national public policy that is going to help us in housing or in health care. So how do we develop progressive support? We need the working people down in the middle because they will support minimum wage, they will support housing, they will support health care, they will support educational grants. They helped support the universities, but their resentment is the fact that now they are being ignored, now they are being blamed. It's not that there need is greater than the minorities who have been so much ignored, but they too have a vital need, and there are almost totally set aside.

The question is of being blamed and being ignored because you live next to the ghetto, that you are the people in between the ghetto; and this is the area that I think is being overlooked by neglect, not only by foundations—and some foundations have done some things in this, I must say that very honestly.

Senator Harris. You mentioned something about the Ford Foundation and your experience with them in your written testimony. Would you care to elaborate on that?

Reverend Barnes. The Ford Foundation was most anxious to help us to see if we could work in Newark, Rochester, Detroit, and Baltimore in the neighborhoods next to minorities where there were heavy concentrations of working class people. Many of these people are from a first, second and third generation, heavy eastern and southern Europe in background. The Ford Foundation gave us a

community development grant for the last 3 years to work in some of these communities.

Our experience has been excellent, and our experience is if you get people involved in their own neighborhood concerns, they begin to see that the minority group does not own the bank either, and that blight is also affecting their neighborhoods, and their neighborhoods are being demvested and are decaying, and different community groups begin to see their interdependence. I think ours is a good experience in the communities, and there is a lot of energy that we have not even tapped and used of the people who want to live in cities, and who want to live together, black or white, or whatever. The Ford Foundation has been very good in this area in terms of being one of the only foundations willing to take some risks in terms of doing some community development in this difficult area. These groups were people that were not eligible for OEO, or title I, Urban Renewal, Model Cities, because they are above the poverty line, you know, and yet they live next to poor neighborhoods and their own changing neighborhoods overlap racially, ethnically, and culturally. That is an area that is going to make or break cities.

Senator HARRIS. Now, you said the Ford Foundation. Are there any other foundations that you know of that have taken this step at all or anything similar to it?

Reverend BARNET. Well, some are very interested. I think one of the things that is very interesting, and I don't know if you know about title 9 of the Higher Education Act, the ethnic heritage studies bill, which I have been very involved with. It only received $2.3 million in the set-aside, and it is known as the Schweiker bill, and has led to this date 11,000 requests for information from community groups who are interested in intercultural ethnic, racial, education.

Some foundations like Lilly, Raskob, and Rockefeller, have been somewhat interested, a few others have been interested in this area. Ford is doing a study of ethnicity and race in urban societies.

Senator HARRIS. You mentioned public education. Of course, we are coming up on the floor of the Senate with the education bill, one of the real controversial features of that bill, of course, is the busing provision. Do you have any comment on that?

Reverend BARNET. Not really. Of course, the concept of limiting busing to the adjacent neighborhood does put the burden of school integration on the minorities and the white working class neighborhoods in the cities, leaving the upper classes in suburbia relatively undisturbed. But I do not think busing is the right issue. We have taught "Dick and Jane", and the "melting pot." We must create a "good school" with the children of teachers, doctors, and lawyers as well as the children of poor working people, black and white, and legitimatize that there is an intercultural kind of worth in a pluralistic world, and that an intercultural aspect is imperative in public education. If we respected pluralism in American education I think you would find working class people less opposed and less fearful of busing. What they are afraid of, in your reference to Wallace, is that the educated people have left them behind. The doctors' and lawyers'

kids have gone, and the working class person is left behind with the minorities to share the burden of change. They do not mind doing their share, but they want some help. They do not want to be ignored by the people who moved away in terms of what was or is a "good school". Where is that "good school" that has the doctors' and lawyers' kids, and the working class kids, and blacks, the Spanish, the white kids? That will be a "good school", and that is the kind of school that people will take three buses to get to.

Senator HARTKE. Yes. All right. Thank you.

Reverend BARONI. Could I just mention one final thing?

Senator HARTKE. Yes.

Reverend BARONI. Would you encourage foundations not to be afraid of the tax law of 1969, and to get into community affairs and support more volunteer groups? Volunteerism and volunteer groups, and people at the neighborhood level need help. Cities are so big, society is so big, that it is at the neighborhood level, the neighborhood people, black or white, rich or poor, that we are going to have to make it together. Many foundations say that the Tax Act of 1969 scares them. I think you, Mr. Chairman, in terms of the Congress ought to help eliminate that little fear, and encourage more foundations to get involved.

Senator HARTKE. So far as I am concerned, and I just speak as one member, to the extent I am going to be capable of doing something in that field, I intend to do just that and I talked to Mr. Alexander, and I hope when we have him come before us that we can alleviate part of that fear.

Reverend BARONI. They always say, yes, we feel—afraid, reluctant.

Senator HARTKE. I have often thought this, and I have said this before. I think that the difficulty in permitting the IRS to be the sole agency concerned with foundations creates a sort of a Gestapo type thinking in the minds of a lot of people, and with all due respect, the IRS is responsible for creating that type of feeling about themselves. I think they have a problem. But, I think that is a problem in American society. The people look upon the IRS not as their friend, not as somebody who is looking for justice, but as somebody who is going to intimidate them. And the foundations are only expressing what I suppose is a normal reaction, and that is they feel that if we are going to run the risk of running afoul of the IRS, that they would rather take the safe course rather than be sorry. And I do not think you can really blame the administrators for having that type of an attitude.

Reverend BARONI. Finally, I would say that I picked up some of that paranoia myself when someone says watch out for the IRS, and I have to relate this concern to community groups, "watch out for the IRS" and "who are they," and they have a legitimate role I am sure. But, I just think that some encouragement, some sensitivity in that area would help foundations.

Senator HARTKE. I agree.

Reverend BARONI. To be more generous to community groups.

Senator HARTKE. I quite agree. Thank you, Monsignor.

[The prepared statement of Monsignor Baroni follows:]

PREPARED STATEMENT OF MSGR. GENO BARONI, PRESIDENT, THE NATIONAL CENTER FOR URBAN ETHNIC AFFAIRS

Mr. Chairman, Members of the Subcommittee, my name is (Rev. Msgr.) Geno Baroni, President of the National Center for Urban Ethnic Affairs in Washington, D.C. I welcome this opportunity and invitation to appear before this Committee.

The Center is involved in the economic, social and cultural issues that affect American ethnics. The Center is also concerned with the development of public social policy that responds to the convergent issues facing urban racial and ethnic groups.

The Center's work includes research, community leadership training, and program development surrounding neighborhood stabilization, intercultural education and economic development in nearly twenty cities.

Previously, I have served as director of community relations and urban affairs for the Archdiocese of Washington and as Program Director of the Urban Task Force of the U.S. Catholic Conference. I have been active with the Urban Coalition, and as a consultant to foundations, mayors, Federal agencies as well as other public and private agencies.

Mr. Chairman, in your remarks entitled "Private Foundations: In Search of a Purpose," printed in the Congressional Record of April 11, 1974, you made the following observations to which I would like to respond.

(1) You spoke of the "desirability" of foundations in a pluralistic society and that we should encourage the participation of diverse groups of citizens in the process of defining and meeting the needs of people.

(2) You called for "greater public participation" on governing boards and greater public awareness of the internal workings of foundations.

(3) You noted that Foundations have a unique ability to be far-sighted, they can look to the future and encourage new ideas and new approaches to public education.

(4) You stated that "foundations must recognize the undercurrents of change which are running through our society and make grants which may help to influence social change."

(5) You pointed out that "the aproach of our 200th National Birthday finds the basic institutions of our society under attack—because they have lost sight of far too many of the objectives of a democratic society."

(6) Finally, "foundations may not be able to speak for those people who are experiencing frustration and anxiety, but they can create an atmosphere which will encourage new voices, new ideas, and new approaches."

In my experience with foundations which has been almost "full-time" since 1968, I have found that most foundation officials still believe that America is a melting pot and they reject your notion that we should encourage the participation of diverse groups of citizens in the process of defining and meeting the needs of the people.

My experience demonstrates that most foundations are made up of people representing a small sector of the American people, and therefore very elite and very biased toward many other different groups of people. I believe that foundations must do more for the neglected minorities and that equality and justice are the major challenges of our democratic system.

In several cases I have noted foundation support for scientific, medical and academic purposes as well as limited support for the performing arts. While there is a sympathy for intellectual and cultural pursuits and some limited attention to minority groups—most foundations ignore or ridicule many lower middle class ethnic groups—particularly those middle Americans who live in our urban areas—and by this practice thus exacerbate racial, ethnic and class polarization.

Before 1968 I was considered "liberal" if I advocated more assistance for housing, health care, and education for minority groups. Since 1968 some of the very same foundations would call me "divisive" because I have tried to sensitize public and private institutions to the legitimate need of heavily ethnic working class communities. I was tired of hearing my family, who lived next to minorities, being referred to as "pigs, hard hats, or racists." Yet none of my family owned or managed the financial institutions that practiced disinvestment or redlining in urban neighborhoods for the blacks, white ethnics or Spanish speaking who dominate many nothern urban areas.

Recently a foundation made a large grant to monitor revenue sharing and the groups represented included an upper middle class women's group and three organizations identified with minority groups. All of these groups are excellent organizations, but they and the foundation ignored any participation by groups or organization who are not upper middle class or in the minority group. They ignored the diversity and pluralism represented by working people. They ignored the ethnic factor in our society.

We wonder then why so many of the so-called silent majority, working class, ethnic Americans feel hurt and ignored and blamed by institutions that are opinion makers such as foundations. We should wonder why so many working people resent the influence and power of the foundations controlled by a very small group of people.

The children and grandchildren of the workers who created the fortunes of the large foundations do not share the same colleges and clubs and, therefore like minority groups do not know the "right people" to participate in the foundation fraternity.

This bias, elitism, and lack of diversity has created hostility toward foundations and minority groups. Working people and the ethnic groups of middle America seek equity—not polarization. "After all," a working housewife exclaimed, "I know the different between a broken back and a broken toe. If 'they' (referring to a minority group) have a broken back, 'they' need more help. But don't tell me, with a broken toe, that I have *no* problems. Don't tell me it's an either-or."

Secondly, Mr. Chairman, you called for greater public participation on governing boards, etc. I should like to say that not only do we need foundation boards to reflect the diversity of our society; foundations should take the lead in the diversification of their boards, staffs, and grants if they seek to better serve the public and expect the public's respect in return.

I have searched long and hard for a useful study in this area and I stand to be corrected if there is a major study showing the diversity of the Boards of Directors, Staffs, and grants of the foundation industry.

For the record, I am submitting a small study ("*Minority Report*") I sponsored of the participation of Blacks, Latins, Poles, and Italians on the Board of Directors and serving as officials of the 106 largest (many of Fortune 500) corporations in Chicago.

FINDINGS AND CONCLUSIONS

Thirty-six, or less than three per cent, of the 1341 directors were Polish, Italian, Latin, or Black. Fifty-two, or less than four per cent, of the 1355 officers were Polish, Italian, Latin, or Black. These four groups make up approximately 31 per cent of the metropolitan area's population. When translated into individual percentages, the findings indicate that 0.3 per cent of all directors were Polish, 1.9 per cent Italian, 0.1 per cent Latin, and 0.4 per cent Black. Out of all officers, 0.7 per cent were Polish, 2.9 per cent Italian, 0.1 per cent Latin, and 0.1 per cent Black.

As a third point, Mr. Chairman, you spoke of foundations' unique ability to be far-sighted: they can encourage new ideas and new approaches to public education.

One of the great tragedies of urban education in the northern cities is our inability to deal with school integration and quality schools. Why can't we integrate? One large northern city has more than 60 colleges and universities in the metropolitan area. No one seems to have an answer; worse yet, no one seems to be working on a "new approach" to the role of public education in a multi-racial and culturally pluralistic society. Minority groups and ethnic groups have long since discovered that it was never legitimate to be ethnic or to belong to a racial minority in our mono-cultural educational system. Foundations have poured large sums of money into educational programs, but Americans of different racial and ethnic groups as well as the isolated educationally affluent are afraid of each other. What makes a good school? Where in American society do we have a pluralistic school system that legitimizes a "good school" as one that reflects the economic, racial, and ethnic diversity of our urban areas? The American educational system has been the chief executor of a mono-cultural, assimilationist model. Indians, Blacks, Spanish speaking

and other ethnic groups have long since realized the heavy price being paid to learn about "Dick and Jane" and "Miss Virginia Slim" as the American models. Cubberly, the philosopher of American education, set the stage for continued Americanization of the immigrants by his writings which are still in circulation.

Most minority and ethnic groups recognize the need for equality of education is not served by a ghetto school. At the same time—"good schools" are defined by class—by the number of doctors, lawyers, professors and professionals children who attend the school, just like a "good" Church seems to be judged by its 'judges,' etc. Lower income ethnics are not afraid of integration—they are largely the only white groups left in the city—but they do resent being left behind to share the burdens of social change in the city school system with minority groups. We would expect that support for multicultural education would be a top priority for foundations interested in education, and one of the most challenging issues facing American society. How do we learn to share a second culture experience, not only for domestic tranquility, but also to live in a culturally pluralistic global village? We have ignored the intercultural imperative of American life and we have failed to create the intercultural dimension in American schools, and foundations will continue to share the blame.

Why is it so difficult, then, to understand the resentment and hostility of so many alienated middle Americans—not toward minority groups, but really to school systems, teachers and universities that they so strongly supported in the past by really believing everything—whatever the "teacher says" is gospel? Now we have trouble getting school bond issues passed. Where is the leadership of those who have fled the city schools—who have lost faith in city schools, leaving the burden on the lower income, less educated, heavily ethnic groups and the minority groups trapped in the city? If the educated white, represented by most foundations, would only lead—lead the way to creating a new American school which says that the "good school," the best school, is the one where rich and poor, bleak, white and brown, educated, "life style" and less educated children are learning to respect their own identity and to share the culture and experience of others in the diversity that binds us together as "valued variants of a common humanity," is the mosaic which is truly American.

Fourthly, Mr. Chairman, you asked that foundations "recognize the undercurrents of change which are running through our society and make grants which may help to influence social change."

Our good experience with the Ford Foundation has enabled us to work in more than 10 to 12 cities where working class—heavily ethnic communities live next to or in changing neighborhoods with black and Spanish speaking groups. While some people with an elitist approach believe we must de-polarize white working class groups—our experience in community organization demonstrates we must be sensitive to the realities facing different groups of Americans. Only when people deal with their own issues and concerns can they begin to relate and understand their interdependence with other groups. We must seek to develop leadership in urban neighborhoods which are truly the heart and soul of cities, no matter how tall and bright the new downtown, empty at night office buildings look.

We have no real neighborhood policy in this country—people should be paid to work in their neighborhoods, to develop bridge issues and convergent issues between groups to stabilize neighborhoods. Housing lasts 300 to 500 years in some European cities, but here a neighborhood falls apart in a generation. Racial and ethnic exploitation, lack of economic and tax base and respect for neighborhoods are the terminal cancers, waiting to be cured, but ravaging on instead to kill our cities, and to increase hostility and isolation between different Americans.

We might mention here that one negative factor of the Tax Reform Act of 1969 has been the increased reluctance of foundations to get involved with volunteer or semi-volunteer community organizations. Can something be done to encourage foundations not to abandon the cities, the neighborhoods—where the daily struggle goes on to live together as Americans who want to know and believe that they have gone beyond the melting pot to cultural pluralism?

Where is the foundation that not only supports major medical and educational institutions and token minority programs, but will also support a workers exchange program to equal the famous Fulbright grants for scholars?

Where is the foundation that now sees the opportunity for minority enterprise and program-related investments for minority business, and also seeks support for new and expanded coops and community development credit unions that are owned by and serve the people of the community? Small foundations, faced with the prospect of having the distribute part of their corpus to meet the distribution requirements of the 1969 law, could be encouraged to make grants of non-interest loans.

Credit is a major issue for working poor and middle Americans. As we know, "not by bread alone does man live."

Finally, Mr. Chairman, neither foundations nor this committee, nor we as witnesses may be able to "speak for those people who are expressing frustration and anxiety; but together with the support and encouragement of Congress, we can create an atmosphere which will encourage new voices, new ideas, and new approaches."

As we reach our 200th Birthday we need to tap our untapped human resources and revive the spirit to face the challenge of redefining America. We must ask why America today has no national sense of identity, no national sense of purpose, no national sense of commitment. Those whose Dream has exploded as a "Raisin in the Sun" and others who seek to pick up the pieces of a new dream find themselves together in saying—"who am *I* and who are *we* as Americans?" Certainly not a tasteless, crustless Wonder Bread—but we are the most ethnically, racially, and religiously pluralistic country in the world—and that diversity may well be the glue that brings us together in good will to provide for the common good.

Minority Report: The Representation of Poles, Italians, Latins and Blacks in the Executive Suites of Chicago's Largest Corporations

Mr. Barta is professor of social science at Mundelein College of Chicago. He had the assistance of Helen A. Smith of the Graduate Program in Urban Studies at Loyola University.

The question "How many are there?" has become one of the most provocative and unsettling questions being raised on all levels of American socity. It reflects the national preoccupation with evaluating the success or failure of various ethnic groups in gaining their share in the American system for distributing income and power. Thus, in just a matter of a few years questions regarding a person's race or ethnic background, once felt to have no public relevance and even considered illegitimate, now not only are being asked but even require answers by law. Companies with government contracts are now required to file reports indicating their utilization rate of Blacks, Latins, American Indians, Eskimos, and women. In January, 1973, the U.S. Department of Labor, Office of Federal Contract Compliance, issued new guidelines to cover discrimination against persons because of religion or ethnic origin. These guidelines said:

"Members of various religious and ethnic groups, primarily but not exclusively of Eastern, Middle, and Southern European ancestry, such as Jews, Catholics, Italians, Greeks, and Slavic groups continue to be excluded from executive middle management, and other job levels because of discrimination based upon their religion and/or national origin. These guidelines are intended to remedy such unfair treatment."[1]

What the guidelines in effect recognize is that, despite the powerful American rhetoric which emphasizes individual achievement, power and affluence in reality still flow along group lines, and that an individual's religious or ethnic affiliation may in fact still be an obstacle to his advancement.

The purpose of this study was to investigate the extent to which members of the Polish, Italian, Latin, and Black communities have penetrated the centers of power and influence in Chicago-based corporations. This was done by determining how many Poles, Italians, Latins, and Blacks either serve on the board of directors or occupy the highest executive positions in Chicago's largest corporations.

In focusing on Poles, Italians, Latins, and Blacks this study selected a combination of minority groups which at this point in time is historically significant. The 1960's saw the rise of group consciousness among Blacks and

[1] 60–50.1 of Chapter 60, Title 41, Code of Federal Regulations.

Latins, and their relentless pursuit of parity with other groups in the U.S. This process released the latent consciousness of other groups, such as Poles and Italians, who are becoming increasingly aware that like Blacks and Latins, they may not be sharing equally in the affluence of American society.

Thus, although this study originated at the request of leaders of the Polish American Congress, Illinois Division, and the Joint Civic Committee of Italian-Americans in Chicago, they were more than willing to see the study expanded to include Blacks and Latins, In the Chicago metropolitan area, where nearly 34 per cent of the seven million population is either Polish, Italian, Latin, or Black, such a perception of mutual concerns could have a positive influence on the future of group relations and thus on the very shape and tone of life in the city and suburbs.

The corporations reviewed in this study were identified by combining the *Chicago Daily News* and *Chicago Tribune* lists of the Chicago area's largest corporations in 1972. Among the thousands of corporations based in the Chicago area, 106 were identified as the largest industrial firms, retailers, utilities, transportation companies, banks, and savings and loan institutions. More than half of them (66 per cent) were included in *Fortune* magazine's 1972 list of the largest 500 industrial corporations or *Fortune*'s lists of the largest non-industrial firms in the U.S. These 106 corporations, therefore, comprise the top layers of the economic and financial power structure of Chicago—and of the nation. It was the top management of these corporate giants and their boards of directors who were scrutinized in order to determine the representation of Poles, Italians, Latins, and Blacks.

Information about direitors and officers was taken directly from the 1972 annual report of each corporation. The number of directors of all 106 corporations totaled 1341; the number of officers, 1355. For the purposes of this study, honorary board members were not included, nor were officers of less than vice-presidential rank such as assistant vice-presidents, assistant secretaries, or assistant treasurers. Where a firm was controlled by a holding company, only the director and officers of the holding company were counted. An officer who also was a member of the board of directors of the same firm was counted twice, once as director, again as officer.

FINDINGS AND CONCLUSIONS

Thirty-six, or less than three per cent, of the 1341 directors were Polish,[2] Italian, Latin, or Black, Fifty-two, or less than four percent, of the 1355 officers were Polish, Italian, Latin, or Black. These four groups make up approximately 34 per cent of the metropolitan area's population. When translated into individual percentages, the findings indicate that 0.3 per cent of all directors were Polish, 1.9 per cent Italian,[3] 0.1 per cent Latin, and 0.4 per cent Black. Out of all officers, 0.7 per cent were Polish, 2.9 per cent Italian, 0.1 per cent Latin, and 0.1 per cent Black. (See Table I.)

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[2] In referring to Poles, Italians, Latins, or Blacks, the author means Americans who are of Polish, Italian, Latin (Spanish-speaking background), or Black ancestry.

[3] One person of Italian background serves on nine different boards. If he were to be counted only once, the percentage of directors who are Italian would be reduced from 1.9 per cent to 1.3 per cent.

TABLE I.—REPRESENTATION OF SELECT ETHNIC GROUPS IN THE CHICAGO METROPOLITAN AREA POPULATION AND ON THE BOARDS OF DIRECTORS AND AMONG THE OFFICERS OF THE 106 LARGEST CHICAGO AREA CORPORATIONS

	Percent area population	Directors		Officers	
		Number	Percent	Number	Percent
Poles	6.9	4	0.3	10	0.7
Italians	4.8	26	1.9	39	2.9
Latins	4.4	1	0.1	2	0.1
Blacks	17.6	5	0.4	1	0.1
All other	66.3	1,305	97.3	1,303	96.2
Total	100.0	1,341	100.0	1,355	100.0

NOTES

The "area population" refers to the Chicago metropolitan area: the six counties of Cook, Kane, Will, DuPage, Lake and McHenry, whose population in 1970 was 6,979,000.

The percentages of area population was prepared by Michael E. Schiltz, Director of Loyola University's Graduate Program in Urban Studies. For Poles, Italians, and Latins, the estimates include first, second, and third generations, based on U.S. Bureau of Census data.

The Black population is based on 1970 data from the U.S. Census Bureau.

How does one make a judgment about such information? How can it be used to evaluate the extent to which Poles, Italians, Latins, and Blacks have entered the executive suites of Chicago's major corporations? Are Poles, Italians, Latins and Blacks equitably represented there?

To answer such questions the executive suite data was compared to the population of each of the four groups in the Chicago metropolitan area. This comparison provides a rough but fair guide for determining whether each group has achieved parity or whether it is underrepresented.[4]

If one compares (Table I) the percentages of officers and directors whose backgrounds are Polish, Italian, Latin, or Black to the percentage distribution of these four groups in the population, it becomes clear that all four groups were grossly underrepresented on the boards of directors and in the executive positions of Chicago's major corporations. Thus, although Poles make up 6.9 per cent of the metropolitan population, only 0.3 per cent of the directors are Polish. Italians make up 4.8 per cent of the population, but only 1.9 per cent of the directors are Italian. Blacks comprise 17.6 per cent of the population yet only 0.4 per cent of the directors are Black. Latins are 4.4 per cent of the population yet only 0.1 per cent of the directors are Latin. The same general pattern holds if one compares the percentages of officers who are Polish, Italian, Latin, or Black to the percentage distribution of these four groups in the population.

As a matter of fact, Poles, Latins, and Blacks were virtually absent from the upper echelons of Chicago's largest corporations. 102 out of the 106 corporations had no directors who were Polish; 97 had no officers who were Polish. Only one corporation had a Black officer and only two had Latin officers. While the Italians were more numerous in the executive suite than the other three groups, 84 corporations out of 106 still had no directors who were Italian and 75 had no officers who were Italian. Finally, 55 out of the 106 corporations had no Poles, Italians, Latins, or Blacks, either as directors or as officers. (See Table II.)

TABLE II.—NUMBER OF CORPORATIONS, OF THE 106 EXAMINED, WHICH HAD NO DIRECTORS OR OFFICERS WHO WERE POLES, ITALIANS, LATINS, OR BLACKS[1]

	Number of corporations without director	Number of corporations without officer
Poles	102	97
Italians	84	75
Latins	105	104
Blacks	101	105

[1] 55 of the 106 corporations had no Poles, Italians, Latins, or Blacks either as directors or as officers.

[4] What should serve as an equitable norm, and how to apply it, is, of course, open to discussion. One can anticipate increasing public discussion of the matter as more groups pursue group gains.

Other significant patterns emerge from the data. Poles and Italians do better in their representation in executive positions than they do as board members. The opposite is true of Blacks, whose major source of representation comes from appointments to boards of directors rather than from holding top executive positions. No Poles were located among the public utilities and banks reviewed in this study, either as directors or as officers. As for Italians, 16 were associated with banks or savings and loan institutions. However, there were no Italians in the executive suites of the utilities.[5] On the other hand, three out of the five corporations with Black directors were public utilities. The number of Latins was not large enough to yield any significant pattern.

Hopefully, this study of four ethnic groups in the corporate structure of metropolitan Chicago will be extended to include their representation in major civic groups such as public boards and commissions, influential private agencies and associations, foundations, and social clubs. Similar studies of other ethnic groups such as Czechs, Greeks, Lithuanians, etc. should be conducted in the Chicago area. Given the lack of adequate research on American ethnic groups, similar surveys should be undertaken in other large cities.

As such studies accumulate, the result may be a national profile for each of America's ethnic groups showing precisely the extent to which each of them share in the power and affluence of the nation. In the process the nation will learn to what extent the American corporation is a "truly public institution bound to the same criteria of selection that today affect government service—freedom from bias, and the requirement at the same time to represent and reflect all parts of the American population."[6]

A NOTE ON METHOD

Trying to determine ethnic origin is a hazardous enterprise. In order to make this study as accurate as possible, knowledgeable leaders from the Polish, Italian, and Latin communities were asked to identify ethnic names by studying the lists of directors and officers in each annual report. In cases of doubtful ethnic origin the individual's office was contacted directly. Each corporation having no apparent representation from any of the four ethnic communities was informally contacted to double check the preliminary findings. In regard to Blacks, all available studies were utilized and persons familiar with the Black community were consulted. Also helpful were several lawyers and business leaders who were generally knowledgeable about many of the corporations studied. If there are any errors in the final tally for each group, the margin of error would not be sufficiently great to invalidate the findings of this study.

A manual describing in full the method used is being prepared by the author and will be distributed through the National Center for Urban Ethnic Affairs in Washington and the Institute of Urban Life in Chicago.

THE 106 CHICAGO-BASED CORPORATIONS

Abbott Laboratories
Admiral
Allied Mills
Allied Van Lines
American Bakeries
American Hospital Supply
American National
Amsted Industries
Baxter Laboratories
Beatrice Foods
Bell Federal
Bell & Howell
Borg-Warner
Brunswick
Bunker Ramo
Carson Pirie Scott
CECO
CENCO
Central National Bank
CFS Continental
Chemetron
Citizens Bank Park Ridge
Chicago Bridge and Iron
Chicago-Milwaukee
Chicago and North Western
Chicago, Rock Island and Pacific
Combined Insurance
Commonwealth Edison
Consolidated Foods
Continental Illinois Corporation
CNA Financial
De Soto

[5] An Italian, however, does serve as an officer of the two subsidiaries of one of the utilities.

[6] Nathan Glaser and Daniel P. Moynihan, *Beyond the Melting Pot* 1963, p. 208.

Donnelley (R. R.) & Sons
Drovers National Bank
Exchange National Bank
First Chicago
First Federal
FMC
General American Transportation
Goldblatt Brothers
Gould
Harris Bankcorp
Hart, Schaffner & Marx
Heller (Walter E.) International
Hilton Hotels
Home Federal
Household Finance
Illinois Bell Telephone
Illinois Central Industries
Illinois Tool Works
Interlake
Inland Steel
International Harvester
International Minerals & Chemicals
Jewel
Kemperco
Kraftco
Lakeview Trust
LaSalle National Bank
Libby, McNeill and Libby
Marcor
Maremont
Marleman
Marshall Field
Masonite
McDonald's
McGraw-Edison
Morton-Norwich Products
Motorola
Nalco Chemical
National Boulevard Bank
National Can
National Tea
Northern Illinois Gas
Northern Indiana Public Service
Nortrust
Northwest Industries
Northwestern National Bank
Outboard Marine
People's Gas
Pioneer Trust
Pullman
Quaker Oats
St. Paul Federal
Santa Fe Industries
Searle (G. D.)
Sears Bank & Trust
Sears, Roebuck
Signode
Spector Industries
Square D
Standard Oil (Indiana)
Sunbeam
Swift
Talman Federal
Trans Union
UAL
U.S. Gypsum
UNICOA
Universal Oil Products
Walgreen
Ward Foods
Washington National
Wieboldt Stores
Wrigley (William) Jr.
Zenith Radio

Senator HARTKE. Our next witness this morning is Dr. Martin Larson, tax policy consultant, for the Liberty Lobby.

STATEMENT OF DR. MARTIN A. LARSON, TAX POLICY CONSULTANT, LIBERTY LOBBY

Mr. LARSON. Mr. Chairman, my name is Martin A. Larson, and I wish to speak concerning the role of the tax-exempt organizations in general and foundations in particular in American society, and their impact upon Federal income taxation. I appear under the auspices of the Liberty Lobby, which is a national organization with 20,000 members in its board of policy, and about 250,000 subscribing members, the purpose of which is to represent the interests of middle Americans, a great majority of our people who work for a living, pay the taxes and who support themselves and who do not look for any favors from the Government, and who insofar as possible like not to be persecuted or interfered with by that Government, especially the Internal Revenue Service.

I have been for a number of years tax policy consultant for the Liberty Lobby; and I have written a number of books on exempt organizations and exempt property. I wrote a book in 1968 called

"The Great Tax Fraud", which was an analysis of the tax inequities of the Internal Revenue Code. And in 1969 I testified before the Ways and Means Committee concerning the Tax Reform Act, which was then under consideration. And may I say that some of the ideas that were presented by the Liberty Lobby at that time were in part incorporated in the Tax Reform Act of 1969.

My latest book is called "Tax Rebellion, U.S.A.," and it describes the tax revolt that is now going on in this country, its basic causes, and what may happen unless something is done to meet the demands for relief from Federal income taxation by the American people.

Now, already I think Liberty Lobby has filed a statement.

Senator HARTKE. We have it and it will be a part of the record.

Dr. LARSON. I am not going to repeat that. I am going to speak in somewhat a parallel manner to what I say in the statement.

But, I want to bring your attention to the fact that people in general, especially those who work for a living, and who are represented by Liberty Lobby, have grown restive and angry because of various reasons that are pressing very heavily upon them. The people in this country are finding it more and more difficult to meet their expenditures, to pay the taxes that are required of them. And they are finding various methods of striking back against this situation.

There are a number of reasons why this is happening. One of them is inflation. The prices have gone up at a rate during the past few months that is simply unparalleled, as far as I can remember, in the history of this country. Many people believe this is due, to a large extent, by the deficit spending of the Federal Government. And they want the Federal Government to spend less money, or at least to balance its budget so that they will not be spending more money than they are taking in.

The middle-income American now pays, in my estimation, approximately 80 percent of the entire personal Federal income tax. And in addition to that, all corporations and business taxes are passed on to them in the form of increased prices for goods and services in the marketplace. And again, because of the enormous cost of the Federal Government, and the fact that those who pay for it get little or no benefit from it, at least as far as they can see, the people are becoming more and more restive and angry at this situation.

The people have learned, also, during the last few years, that the Internal Revenue Code is filled with loopholes, and they now believe rather generally that if these were closed every family in the United States could have an exemption of $15,000, which would relieve approximately 80 percent of the people in this country from the payment of any Federal income tax. And if the tax were equitably assessed and collected from all different individuals in the country, and from all of the organizations in the country, the Treasury could actually obtain more money than it now does, even with this kind of an exemption.

Now, even if every family in the country were to have an exemption of $15,000, this would be no more than it had at the beginning, because when the income tax was first established, the exemption for

a couple was $3,000 and in the twenties it was $3,500 for a family, or a couple, plus $400 for each additional dependent. At the present time, prices and costs have gone up so astronomically that $15,000 is necessary to meet the same living standard as $3,500 or $3,000 did at that time.

I believe that if all of the loopholes in the Internal Revenue Code were to be closed, and if the taxes were to be equitably collected, the Treasury could obtain $70 billion that it is not now collected. And that by remitting that amount of taxes for the middle income American, every family could, as I said a moment ago, have an exemption of approximately $15,000.

I want to point out that a tax rebellion is actually underway in the United States. The facts concerning it are somewhat difficult to obtain. But, the U.S. News and World Report of September 17, 1973, declared that something like 5 million people had not paid their taxes during the previous year, and that that may have involved as much as $30 billion of loss to the Treasury. In any event, Johnnie Walters admitted in an interview that the IRS knew of at least 1,400,000 persons who had not paid their tax during the previous year; yet because they are so many, and because each of these is guilty of a criminal offense, it is impossible to prosecute them all.

Now, supposing this tax rebellion spreads, as it may do, to some 20 or 30 million people in the United States and that that number refused to pay their taxes? What then is going to happen to the Federal income tax and the Internal Revenue Service? I submit that it is absolutely impossible to prosecute 20 or 30 million people or to collect taxes from that number if they refuse to pay.

Now, foundations are only one of the many methods by which Federal taxation is avoided. There are many other ways, but since we are discussing foundations today I will speak to that subject.

According to the 1969 "Cumulative List" published by the Internal Revenue Service, there are about 125,000 exempt entities but this covers about 1½ million different organizations because many of these names cover entire denominations, some of which have several thousand congregations. So, there are something like 1½ million different organizations in the United States that have complete tax exemption. Most of them are free not only from taxation, but also from disclosure, and, therefore, nobody knows how much money they take in or what their financial status is.

Now, in 1968 the Select Committee on Small Business published a book containing 30,262 names of foundations. In addition, the foundation director of New York lists 5,454 as having assets each of more than $500,000 and having total assets of $25 billion plus. They distributed $1,513,000,000 but they spent $1,645,000,000 for administration. In other words, they spent about $120 million more for administration than they distributed to all of those who received any gifts or contributions from them.

I estimate that in 1974 the total assets of these foundations must equal something like $40 billion—that is, of the 5,454 listed in the Accumulative Index. But if we include all of the other foundations, of which there are more than 25,000, I would not be surprised if the

total assets of all foundations totalled something like $60 billion. In other words, here we have organizations into which something like $60 billion of capital has fled, and this is essentially free from taxation and from public control.

To a large extent, the foundation is one of the best methods by which a very wealthy person can escape and avoid taxation legally. Take the case, for example, of Walt Disney. He had a personal fortune of $58 million, one-half of which he gave to the Walt Disney Foundation which owns the two Disneylands. The other half of his fortune was set up in trusts which went to the third and fourth generation, and they also escaped all taxation. In other words, here was $58 million of an estate that escaped all estate and inheritance taxation. Now, this happens in thousands and thousands of cases. The inheritance tax and the estate is assessed for the most part only on middle fortunes, not on the large ones.

In 1969, the Internal Revenue Service listed 1,211 incomes exceeding $1 million apiece, of which 52 paid no tax whatsoever. And when you add up all of the taxes paid by the whole 1,211 of them, which had average incomes of approximately $4 million, their tax amounted to something like 16 or 18 percent, which is less than the average carpenter or plumber pays.

A wealthy person can actually become more wealthy by giving money to his own foundation, because 50 percent of it can be deducted from his adjusted gross income if he has an operating foundation. Remember that wealthy people give money to foundations largely to accomplish their own purposes. And they give money to foundations in order to create monuments to themselves, in order to make themselves famous. They are willing to give, but they are not willing to pay. I think it was Plato who said in "The Republic" that the way to become a saint, in order to become a famous person, is to collect all of the money that you can during your lifetime by any possible method, and then give a part of it to religion or charity, and after a while they will erect monuments for your glory. Well, the same thing is happening at the present time, and foundations are one of the most important methods by which individuals obtain fame and glory and sainthood for themselves.

Well, Liberty Lobby believes that certain fundamental changes should be made in the whole structure under which foundations are erected and under which they operate. We do not deny that many foundations do good. Some of them do a great deal of good, especially those that are engaged in research projects which are for the benefit of the people. However, we believe that a great many of them are organized, the great majority of them are organized, primarily to avoid taxation.

But, even so, Liberty Lobby does not take the position that they should be eliminated or that foundations should have only a limited period of existence. We say that they should be allowed to continue and that they should have sufficient motivation for their establishment and operation. And for that reason, we believe that gifts given to foundations should remain tax exempt, both to the donor and the donee, except that portion which consists of capital gains. In other words, if a man has an asset that cost him $100,000 but is now

worth $1 million and he gives it to a foundation, we think that the $900,000 should be taxable as capital gains.

If that one thing were done, it might bring in $2 billion to the Federal treasury each year.

We do not believe that any State or Federal inheritance or estate tax should be levied upon bequests to foundations. However, we also believe that changes should be made which should be for the benefit of the taxpayer and the people and the treasury.

Now, gifts given to a foundation should not enable the donor to escape taxation upon other income. At the present time, a man can give $500,000 to a foundation, for example, and by so doing he needs to pay no income tax on $1 million of capital gains. We think that should be eliminated. We do not think, furthermore, that the person who gives an asset to a foundation should be permitted to draw the income from it during the rest of his life. At the present time a man can set up a trust for a foundation, a college or university, draw the entire income from it during his lifetime, receive deductions from other sources of income because of this, and when he dies, the gift, the bequest, escapes all inheritance or estate taxes.

We furthermore believe that foundations should be taxed as other foundations are upon their business revenue.

For example, a large foundation may draw business revenues of several hundred million a year, which under the Tax Reform Act of 1969 now is taxed at 4 percent. Well, if a corporation for profit pays 48 percent, we think that a foundation should pay 48 percent on its business income.

Now, if these changes were made, foundations would still have a motivation to exist, but at the same time, the Federal treasury would probably be enhanced by at least $2 or $3 billion a year. And if similar laws were passed in regard to other organizations which are exempt from taxes, and from individuals who escape taxes as a result of the provisions in the Internal Revenue Code, it would be possible so to reconstruct the entire tax system that we could re-establish the concept which existed at the time when the 16th amendment was passed, and that was that no portion of any person's income necessary to maintain a decent contemporary living standard should be subject to Federal taxation.

I thank you very much.

Senator HARTKE. All right. Thank you.

I will point out that some of the things you are talking about we are not really involved with here in this hearing. We are not really involved in a whole reformation of the tax system, which you are talking about.

Dr. LARSON. Yes. I am well aware of that.

Senator HARTKE. Yes.

Dr. LARSON. But we like to mention this.

Senator HARTKE. I understand some of the things you have talked about are in that line.

You allege that there are 180,000 charities that are presently receiving ——

Dr. LARSON. There are approximately 100,000 that are listed either as foundations, trusts, or funds.

Senator HARTKE. And how many of those are foundations?

Dr. LARSON. Well, it is very difficult to say. I know that Wright Patman complained bitterly that he could not find out how many there were, that the IRS does not seem to know the exact number that it has certified as foundations.

Senator HARTKE. I think maybe we will have that information from the IRS. We have information that indicates about 28,000.

Mr. LARSON. 28,000?

Senator HARTKE. Yes.

Dr. LARSON. Well, Wright Patman's committee put out a book in 1968 or 1969 which listed 30,262 which were definitely called foundations.

Senator HARTKE. How much wealth do they have in your estimation?

Dr. LARSON. Well, that is unknown. The Library, Foundation Center of New York lists 5,451 with assets of $25 billion, 181 million as of 1969-70. Now, if this has increased at the same rate, if the increase in this has gone at the same rate since 1968 that it has previously, then the amount now would be very close to $40 billion. Now, that still does not include 25,000 smaller ones.

Senator HARTKE. All right. Thank you, Dr. Larson. We appreciate your testimony.

[Dr. Larson's prepared statement follows:]

PREPARED STATEMENT OF DR. MARTIN A. LARSON, TAX POLICY CONSULTANT, LIBERTY LOBBY

SUMMARY

I. Liberty Lobby is concerned over tax-exempt organizations in general, because it believes in tax equity.

II. Hundreds of thousands of organizations in the U.S. are exempt from taxation and most are also immune to disclosure. Of these, at least 100,000 are funds, trusts, or foundations.

III. How the wealthy avoid federal taxation, which falls most heavily upon the middle income classes.

IV. The private foundation serves not only to glorify its creator, but also enables him to achieve personal objectives otherwise impossible, and also to avoid taxation.

V. Because of existing laws, private foundations have grown so large that they now possess a considerable portion of the Nation's capital.

VI. Private foundations enable their creators to avoid most of their taxes while they are amassing their wealth and enable them also to avoid all estate and inheritance taxes and to dictate what shall be done with their wealth virtually in perpetuity.

VII. The wealthy donor gives to his own foundation to accomplish his personal objectives and for this he receives honor and public acclaim; but the humble taxpayer, who is forced to support the government, receives no award or recognition of any kind.

VIII. If the U.S. Congress wishes to do anything for the benefit of the people, it will rewrite the Internal Revenue Code so that no family will be forced to pay taxes on any portion of income necessary to maintain a decent, contemporary standard of living.

IX. Our I.R. Code seems to have been conceived in discrimination and it operates on the basis of fiscal insanity. It is highly inflationary and costs our people three times as much as the Treasury collects in revenue.

X. It is outrageous that any tax should be levied upon the portion of wages and salaries necessary to maintain a decent, contemporary living standard.

XI. Specific recommendations: 1. Gifts or bequests to foundations should continue tax-exempt to donor and recipient, except for capital gains;

2. No estate or inheritance tax should be levied upon such bequests;

3. Gifts and bequests to foundations should not entitle donor to any reduction in income taxes on revenues derived from sources other than his gifts;

4. Private foundations should pay taxes on investment income at the same rate as other corporations, with no reduction for administrative expenses;

5. Except for operating foundations paying salaries to research scientists or scholars whose work is in no way related to the interests of the donor, no tax deduction should be permitted for such expenditures.

XII. SUMMARY: 1. Even if our reforms were adopted, there would still be ample motivation for the establishment of foundations and other "charities"; but

2. The American people have now grown so restive and angry over our inequitable and burdensome system of taxation that unless drastic changes are made in the tax laws, there will be rebellion and perhaps violence.

STATEMENT

Mr. Chairman and Members of the Committee: I am Dr. Martin A. Larson, Tax Policy Consultant of Liberty Lobby. I appreciate this opportunity to present the views of Liberty Lobby's 20,000-member Board of Policy and also to appear on behalf of the approximately quarter million readers of its monthly legislative report, *Liberty Letter*.

Tax exemption and tax equity

Since Liberty Lobby is primarily interested in tax equity and constitutional government, we are deeply concerned over the growth of tax-exempt, or virtually tax-exempt, organizations in the U.S. We are deeply committed to the propositions that:

1. No tax should be collected by illegal or unconstitutional methods; and

2. Every tax should be as fair as possible to everyone.

Since we know that the rich and super-rich can utilize the loopholes in the *Internal Revenue Code* to avoid all or nearly all taxation, we brand that Code as a fraud; and since private foundations are one of the principal means by which huge taxes are legally avoided, we look upon them as an enemy of the great middle class, whose members do the work of the Nation, pay the great bulk of the taxes, live in obedience to the laws, and support their own families. In return, the only attention they receive from the federal government consists of persecution and extortion by the I.R.S.

The number of foundations and other exempts

The *Cumulative List*, published by the I.R.S. in 1969, gives approximately 125,000 exempt organizations; but, since this includes religious denominations, where a single entry may represent thousands of separate congregations, Sheldon Cohen, then IRS Commissioner, estimated that there were more than 1,500,000 exempt entities, of which the great majority were not only exempt from taxation, but also immune to disclosure. No one, therefore, knows how much money they receive and disburse; but it is certain that the total runs into tens of billions of dollars.

In a publication of the Select Committee on Small Business, dated 1968, we find a list of 30,262 foundations. This, however, is not complete, because it does not include a great variety of funds, trusts, and assorted "charities," which operate very much in the same manner and enjoy the sam immunities. There is no doubt that these private entities now total at the very least 100,000 and constitute a great social, economic, and political force. Rep. Wright Patman complained bitterly that he could never find out from the IRS how many foundations it has certified—which is indeed strange, since it is able to determine to the last penny how much income more than 70 millions of taxpayers have received.

Almost every opulent family seems to have established at least one foundation and many have created entire clusters of these instruments for the obvious purpose of tax-avoidance; and they serve very efficiently as a means by which to shift the tax-burden from the rich onto the backs of the middle income classes and even to the needy.

Tax-avoidance and tax-slavery

According to the 1969 *Statistics of Income*, there were 52 individuals who paid no tax at all on $1 million or more of *adjusted gross income*. There were

1,211 in this category, who average $2,441,846 of adjusted gross, in addition to $1,715,000 of untaxed capital gains—or an average of $4,156,876, on which the tax was $1,015,248, or 24.4%. However, there are 23 categories of unreportable income—such as interest from exempt bonds, revenue from oil, gas, and other investments reduced by depletion allowances, and from tax-sheltered incomes of various kinds. We know, therefore, that the average income of these tycoons was much greater; and also that the tax paid by them—when we compute the Social Security contributions—constituted a much smaller ratio than that paid by an ordinary carpenter or plumber.

The role of the foundation

One of the very important loopholes by which wealthy individuals avoid taxation consists of the funds, trusts, and foundations which they have organized and which they operate. It can be demonstrated that a wealthy man may actually increase the personal estate he can bequeath by giving lavishly to his own foundation, which he may use not only for his own glorification but also to accomplish various personal objectives, not necessarily related at all to the general welfare.

Let us see how this can operat: A man may, for example, own a company which manufactures drugs, medicines, electronics, or whatever; he then organizes a foundation to do research in these fields, and his company can profit by its results. He can also make a $1 million capital gain, which will be tax-exempt if he gives stock to his own foundation with a book value of $100,000 but a current market value of $350,000. Since he is in complete control of his foundation, he can decide what disposition to make of its revenues—and we can be sure that he will never give money unless it is for a purpose he wishes to promote. He can use his own foundation to underwrite the education of his children, grandchildren, nieces, nephews, and other relatives. He may give money to a church—or other similar 501(c)(3) organization—which can then act as a conduit to see that his money reaches any destination he may decree—even a race track or a social club. Remember, no church can be audited even if it is in violation of the law; and no one below the rank of district director may even take notice of such violation when it occurs (Secs. 6033(a) and 7605(c) of the I.R. Code).

The growth of private foundations

No wonder, then, that foundations have grown enormously in number, size, power, and wealth; during recent years, they have become one of the principal havens for huge sums of money intent on escaping taxation. For example, it is conservatively estimated that the Ford Foundation has enabled its creators to avoid approximately $8 billion in federal taxation.

According to Edition 4 of the Foundation Director of 1971, published by the Foundation Center in New York, large foundations increased in number between 1958 and 1969 from 780 to 2,172, and their assets from $10,667 to $23,948 million. There were 5,454, each of which had assets exceeding $500,000, and totalling $25,181 million in 1968–69. Since their administrative expenditures, which were $1,645 million, exceeded their grants by $32 million, we conclude that they must have supplied many lush positions for favorites.

If the assets of these 5,454 foundations have continued to increase since 1968 at the rate of previous years, they must now exceed $32 billion.

However, there are at least 25,000 other foundations. Even if their welath averages only $200,000, we have an additional $5 billion. And these do not include some 75,000 other non-religious funds and trusts; when we add them, we believe that a conservative estimate of the capital which has taken refuge under their wings could probably be not less than $60 billion.

How foundations enrich their creators

What trusts and foundations can do for a private fortune is illustrated in the case of Walt Disney, who disposed by will of his $58 million fortune, which had been amassed largely because of his tax-free Disney Foundation, which owns and operates the two Disneylands, and to which he bequeathed half of

his wealth, while he set up the remainder in trusts, which also escape taxation unto the third or the fourth generation. In other words, Mr. Disney's estate—like that of thousands of other multi-millionaires—paid not one penny in estate or inheritance taxes at his death, and very little of any kind while it was being gathered.

It is true that the Tax Reform Act of 1969 instituted a few reforms in regard to foundations:

1. It imposes a 4% excise tax on their net investment income (IR Code 4140)
2. It prohibits various forms of self-dealing (*ib.* 4941)—some of which may bring fines up to 200%
3. Certain activities are forbidden (*ib.* 508(e)) on pain of lesser penalties; and
4. Involvement in unrelated business is prohibited (*ib.* 4943).

However, a taxpayer may now donate up to 50% of his adjusted gross income to his own *operating foundation*—a provision which we consider highly regressive, since it offers a far too generous escape from taxation to the very rich.

The wealthy donor vs. the average taxpayer

We do not deny that some foundations may do a considerabl amount of good; however, it is indisputable that many of them do none, but, on the contrary, are used for purposes contrary to the general welfare. It is a well-known fact that wealthy individuals are willing to *give* in order to achieve their own purposes or to obtain public acclaim—especially when it costs them little or nothing; but they are not willing to PAY, which is what our ordinary citizens must do, as the IRS levels its loaded gun at their heads. To pay taxes brings neither merit nor award: but those who have spent their lives accumulating a fortune by wicked methods can achieve virtual sainthood and are memorialized in plaques and monuments when they give a fraction of their loot to support religion or so-called charities. Thus, the rich, who pay little or nothing in taxes, are honored as social benefactors; but the producers, who support the government, create our wealth, slave away their lives in ignominy, and then die in obscurity, are treated like the leaves which fall from the trees in autumn.

A law based on injustice and insanity

We would suggest that if you want to do something beneficial for our productive citizens, you will restructure the Internal Revenue Code so that exempt businesses of all kinds will pay a fair share of taxes; this will make it possible for every family in the U.S. to have an exemption of at least $15,000 and still provide the Treasury with the same amount of money it now collects. It is demonstrable that the loopholes in the Code, favoring the rich and exempt organizations, are costing the Treasury at least $70 billion a year.

The Internal Revenue Code is highly inflationary

It seems to us that the I.R. Code, as now written and administered, was conceived by Injustice, born through Discrimination, and is Administered on the basis of fiscal insanity. Those who should pay least or nothing are the ones taxed most heavily; taxes which cause the greatest inflation are those most inexorably imposed. It can be shown that income taxes imposed upon production—individual and corporate—which produce about $125 billion of federal revenue, increase, by escalation and pyramiding, the cost of all goods and services to the ultimate consumer by double the amount received by the government. In short, our productive citizens pay the tax three times: first, as producers, and then again—and doubly—in the market place. The federal government itself pays an additional $60 billion a year for the goods and services it consumes because of its own tax. If it were not for this, the same goods and services that now cost our people $750 billion could be had for $500 billion. And it costs the government $1.5 billion to operate the IRS and the taxpayers another $2.5 billion to make out their reports and to do battle for survival with the gestapo.

Liberty Lobby has long taken the position that taxes which create inflation and close foreign markets to our manufacturers—as our corporation and indi-

vidual income taxes do—should be repealed, or, if necessary, replaced by others which will not inflate the price of goods and services.

Outrageous taxation

Liberty Lobby considers it an outrage that any income tax should be levied upon any portion of personal income necessary to maintain a decent, contemporary living standard. When the 16th Amendment was ratified, it was proclaimed and generally believed that—except during a war-emergency—incomes taxes would be imposed only upon large, unearned incomes. What we have experienced is perhaps the greatest extortion in history and has now resulted in a national tax rebellion, long overdue.

Instead of taxing wages, salaries, and productive business, we should tax only large, unearned incomes; large estates, as they pass from one generation to the next; the capital gains which increase the value of gifts and bequests; the income of non-productive corporations of all kinds, especially foundations and other so-called charities. If this were done, at least $50 billion, now lost, would accrue to the Treasury. If the income tax on all production were abolished, the people would benefit by more than $300 billion; and if this tax were replaced by a universal 5% transactions tax, it would produce, at one-sixth the present cost, all the revenue that would be lost by abolishing the income tax on wages, salaries, and productive enterprise.

Specific recommendations for reform

With respect to the foundations, therefore, Liberty Lobby offers the following recommendations and practical suggestions:

A. In order to retain ample motivation for the continuance of foundations and other private "charities"

1. Gifts or bequests to them should remain tax-exempt both to donors and recipients, except for the portion which constitutes capital gain and which should be taxed, at normal rates, either to the donor or the recipient;

2. No estate or inheritance tax should be levied on bequests to foundations or other qualifying charities.

However,

B. In order that the present inequities may be at least in part remedied

1. Such gifts should not entitle the donor to any reduction in personal income taxes derived from sources other than the gift;

2. No donor should be permitted to receive income from property placed in irrevocable trust for the benefit of an exempt organization;

3. All private foundations should be required to pay federal taxes at the same rate charged to productive corporations, with no allowance for administrative expenditures; and

4. Only in the case of an operating foundation should salaries paid research personnel whose work has no relationship to the interests of any donor be deductible from taxable income.

SUMMARY

Even if these reforms were instituted, we would still have foundations; but they would be performing work beneficial to the general welfare, or they would shoulder at least a partial share of the taxes which should be imposed on them.

This reform would also increase Treasury income by at least $3 and possibly $5 billion.

If the same principles were extended to all tax-exempts, including government-financed cooperatives, power installations, and other enterprises which operate in direct competition with taxpaying business, the Treasury would probably be able to increase exemptions for all wage and salaried workers by 50% without any loss of revenue.

Foundations have assumed the status of American inequality and injustice. The taxpayers are restless, in a state of incipient revolt. I warn you that unless something drastic is done, the tax rebellion which is already in full swing will go completely out of control. For the fact is that taxes now consume fully 50%

of the production of our middle classes and interest takes another 13 or 14%, leaving them only about 36 or 37% of their income for the support of their own families. Unless these conditions are drastically altered, I foresee riots, bloodshed, general violence, and ultimate revolution or dictatorship in our beloved United States.

And this is what Liberty Lobby fervently wishes to avoid.

Thank you again for this opportunity to appear and present our views.

Senator HARTKE. The next witness will be Kyran M. McGrath, Director of the American Association of Museums. Good morning, sir.

STATEMENT OF KYRAN M. McGRATH, DIRECTOR, AMERICAN ASSOCIATION OF MUSEUMS

Mr. MCGRATH. Good morning, Mr. Chairman. Thank you very much for the opportunity to testify here this morning. I wanted to speak about a small point that is of particular interest and concern to museums, and elaborate, if I can, on the prepared statement that I have submitted for the record.

Senator HARTKE. Yes. Fine.

Mr. MCGRATH. It has to do with a small number of museums, by reason of the Tax Reform Act of 1969, which have been classified as private operating foundation museums, private operating foundations rather than as public charities, and this is due solely to the amount of income they receive from their endowments. The endowment providing an income over and above the formulas provided in section 509a, and also now more than allowed under the 10 percent floor under the so-called facts and circumstances test that the IRS has adopted under regulation 1:170(a)9.

What this amounts to is that a small number of museums must pay the 4 percent excise tax on the endowment income, and that excise tax comes directly off the top of their operating income.

Now, studying the record of the Tax Reform Act of 1969 and the discussion by the House Ways and Means Committee, and your Senate Finance Committee, and the Internal Revenue Service, the intention was to improve the charitable efforts of private foundations and not to take away part of the resources that in the case of these museums were devoted entirely to providing charitable and educational activities.

So, the formula test called for in the Tax Reform Act of 1969 and the facts and circumstance test has had an adverse impact on these museums, programs at the application of the 4 percent excise tax.

There is a second adverse effect, and that is the increased filing required now for private foundations distributing income to other private foundations. Because these museums are classified as private operating foundations, these museums must in addition meet these new filing requirements which are in effect.

It is not justified, but a number of private foundations have taken the policy position that because of the increased filing requirements

that they will not distribute income to any organizations other than public charities, which effectively cuts off the private operating foundation museums from foundation grants.

So, try as they will, they are unable to generate outside sources of income that are so necessary to build up to meeting the test either for facts and circumstances, the 10 percent floor, or for the regular one-third test.

Well, I listed a number, six museums in the testimony here, but there are other museums that have been unable.

Senator HARTKE. How long would it take you to get us a complete list on that, or are you able to come up with that?

Mr. MCGRATH. Well, I tried checking with the records from the Internal Revenue Service. They do not have them broken down by museums. That is the sad part.

Senator HARTKE. Don't you have them organized by museums?

Mr. MCGRATH. Yes. On page 2 of the testimony there are six listed, the Winterthur Museum which paid last year $121,000, and the others.

Senator HARTKE. I understand that. I hear you on that. But, what I am saying to you is you have listed here six. Is this approximately all that are involved?

Mr. MCGRATH. No. There are approximately 15 to 20 that are involved.

Senator HARTKE. 15 or 20? That is all involved in the United States?

Mr. MCGRATH. That is correct, yes, to the best of our knowledge. I will try to submit for the record if I can, as thorough a list as we can get.

Senator HARTKE. Let me ask you, are you speaking about those aspects, the 4 percent excise tax and also the question of being eligible?

Mr. MCGRATH. And the filing requirements.

Senator HARTKE. Pardon me?

Mr. MCGRATH. The filing requirements from other private foundations to make grants to these museums.

Senator HARTKE. But they fall into the same category?

Mr. MCGRATH. Correct. That is correct.

Senator HARTKE. In other words, there would be an identical list for both elements?

Mr. MCGRATH. That is correct.

Senator HARTKE. Can you supply those for the record for us?

Mr. MCGRATH. I will try by the end of next week. We tried to get it up last week.

Senator HARTKE. That is fine if you can get it in by that time because we will not have concluded these hearings by that time anyway.

Mr. MCGRATH. Certainly. Yes, we will.

Senator HARTKE. I would also like to have the amount of taxes they paid.

Mr. McGRATH. Yes.

Senator HARTKE. And if possible, an estimate of what they have lost as a result of the filing requirements. Do you have any idea?

Mr. McGRATH. That is the hard one because they get turned down, they just get rejected.

Senator HARTKE. Well, I understand that. But, you certainly ought to have a past history of contributions.

Mr. McGRATH. Yes. Prior to 1969.

Senator HARTKE. As to what they had received prior to that time, and what they have lost as a result of that decision.

Mr. McGRATH. Yes, indeed. I will do that.

[The following was subsequently received for the record:]

AMERICAN ASSOCIATION OF MUSEUMS,
Washington, D.C., June 17, 1974.

Hon. VANCE HARTKE,
Chairman, Subcommittee on Foundations,
U.S. Senate,
Committee on Commerce,
Washington, D.C.

DEAR SENATOR HARTKE: In accordance with Kyran McGrath's letter of May 29, 1974, which stated that we would send you more information about the museums which are classified as private foundations, enclosed please find statistics on the amount of tax these museums paid in 1971, 1972, and 1973 and statistics on the amount of grant support the museums received in 1968 and 1973. In addition to the figures, we have attached some comments taken from letters to the AAM as a result of our survey; the comments reaffirm the burden placed on museums classified as private foundations. We will be glad to provide any other information you may need. Thank you.

Sincerely yours,

MARILYN HICKS FITZGERALD,
Executive Assistant to the Director.

MHF/
Enclosure.

MUSEUMS CLASSIFIED BY IRS AS PRIVATE FOUNDATIONS

Name of museum	4 percent excise tax paid			Income from private foundations	
	1971	1972	1973	1968	1973
Pajaro Valley Historical Association, P.O. Box 960, Watsonville, Calif. 95076	(1)	$30	(1)	(1)	(1)
San Francisco Aquarium Society, Golden Gate Park, San Francisco, Calif. 94118	(1)	149	(1)	(1)	(1)
Butte County Pioneer Memorial, c/o Irene Parker, P.O. Box 309, Oroville, Calif. 95965	(1)	80	(1)	(1)	(1)
Briggs-Cunningham Automotive Museum, 747 East Green St., Pasadena, Calif. 91101	$0	19	$82	$0	$0
American Air Museum Society, 616 Canal St., San Rafael, Calif. 94901	(1)	(1)	(1)	(1)	(1)
The J. Paul Getty Museum, 17985 Pacific Coast Highway, Malibu, Calif. 90265	669,025	97,270	54,273	0	0
Norton Simon, Inc., Museum of Art, 3440 Wilshire Blvd, suite 1216, Los Angeles, Calif. 90010	12,251	10,164	52,494	0	0
Western Museum of Mining and Industry, P.O. Box 387, Colorado Springs, Colo. 80901	(2)	15	1,534	(2)	20,000
Automotive Museum, P.O. Box 13, Berlin, Conn. 06037	(1)	(1)	(1)	(1)	(1)
Litchfield Nature Center and Museum, Litchfield, Conn. 06759	(1)	(1)	(1)	(1)	(1)
Torrington Historical Society, c/o Colonial Bank & Trust Co., P.O. Box 148, Torrington, Conn. 06790	(1)	96	81	(1)	(1)
Hagley Museum, Eleutherian Mills-Hagley Foundation, Wilmington, Del. 19735	43,419	126,411	68,697	0	0

See footnotes at end of table.

MUSEUMS CLASSIFIED BY IRS AS PRIVATE FOUNDATIONS—Continued

Name of museum	4 percent excise tax paid			Income from private foundations	
	1971	1972	1973	1968	1973
Delaware Museum of Natural History, P.O. Box 3937, Greenville, Del. 19807	(1)	1,496	(1)	(1)	(1)
The Henry Francis DuPont Winterthur Museum, Inc., Winterthur, Del. 19735	(1)	$113,174	$121,318	(1)	(1)
The Phillips Collection, 1600 21st St., NW, Washington, D.C. 20007	$4,411	18,690	6,400	$0	$0
The De Ette Holden Cummer Museum Foundation, 829 Riverside Dr., Jacksonville, Fla. 32204	(1)	6,752	(1)	(1)	(1)
Marie-Selby Botanical Gardens, c/o Palmer First National Bank & Trust, P.O. Box 2018, Sarasota, Fla. 33578	(1)	4,159	(1)	(1)	(1)
Ships of the Sea, Inc., 501 East River St., Savannah, Ga. 31401	(1)	3,475	(1)	(1)	(1)
Kauai Library and Museum Association, Lihue, Kauai, Hawaii 96766	(1)	22	(1)	(1)	(1)
Morton Arboretum, 110 North Wacker Dr., Chicago, Ill. 60606	41,166	51,402	51,799	0	0
Harry and Delta Burpee Art Gallery, 737 North Main St., Rockford, Ill.	(1)	37	(1)	(1)	(1)
Historical Bldg., 19 Grove St., Petersborough, N.H. 03458	(1)	176	(1)	(1)	(1)
George F. Harding Museum, 86 East Randolph St., Chicago, Ill. 60601	(1)	(1)	(1)	(1)	(1)
Treaty-Line Museum, Inc., Rural Route 4, Liberty, Ind. 47353	(1)	260	(1)	(1)	(1)
Rush County Historical Society, c/o Priscilla Winkler, Rural Route 5, Rushville, Ind. 46173	(1)	1,528	(1)	(1)	(1)
Historic New Orleans Collection, 533 Royal St., New Orleans, La. 70130	(1)	17,170	(1)	(1)	(1)
Zigler Museum Foundation, P.O. Box 986, Jennings, La. 70546	(1)	789	(1)	(1)	(1)
Old Gaol Museum, c/o York County Historical Society, York, Maine 03909	826	779	946	(1)	(1)
Blandford Historical Society, Main Street, Blandford, Mass. 01008	49	47	54	0	0
Fruitlands Museums Inc., Prospect Hill, Boston, Mass. 01451	(1)	167	(1)	(1)	(1)
Isabella Stewart Gardner Museum, 225 Franklin St., suite 800, Boston, Mass. 02180	(1)	27,653	(1)	(1)	(1)
Kendall Whaling Museum Trust, c/o Hale & Dorr, 28 State St., Boston, Mass. 02110	57	80	96	(1)	(1)
Leonard Boyd Chapman Wildbird Sanctuary, suite 4500 Prudential, Boston, Mass. 02199	[illegible]	363	246	0	0
Cambridge Historical Society, 159 Brattle St., Cambridge, Mass. 07138	374	316	286	0	0
Cape Cod Museum of History and Art, South Main St., Centerville, Mass. 02632	(1)	99	(1)	(1)	(1)
Fall River Historical Society, 451 Rock St., Fall River, Mass. 02720	(1)	627	1,843	0	0
Haverhill Historical Society, 240 Water St., Haverhill, Mass. 01830	(1)	303	(1)	(1)	(1)
Thayer Museum Inc., 314 Main St., Lancaster, Mass. 01623	(1)	11	(1)	(1)	(1)
Lynn Historical Society, 125 Green St., Lynn, Mass. 01902	919	1,033	1,224	0	0
Manchester Historical Society, 41 Union St., Manchester, Mass. 01944	173	177	605	0	0
Merrimack Valley Textile Museum, Massachusetts Ave., North Andover, Mass. 01845	2,842	2,979	5,994	167,000	83,757
North Andover Historical Society, 153 Academy Rd., North Andover, Mass. 01845	(1)	325	(1)	(1)	(1)
Heritage Plantation of Sandwich, Grove St., Sandwich, Mass. 02503	261	251	37	0	0
Somerville Historical Society, Westward Blvd. and Central St., Somerville, Mass. 02143	(1)	39	(1)	(1)	(1)
Stockman Historical Society, c/o Clark A. Richardson, 3 Barrett Ave., Stoneham, Mass. 02180	(1)	36	(1)	(1)	(1)
Western Hampden Historical Society, Westfield, Mass. 01085	(1)	38	(1)	(1)	(1)
Sterling and Francine Clark Art Institute, Willimstown, Mass. 01267	(1)	58,832	(1)	(1)	(1)
Manchester Historic Association, 129 Amherst St., Manchester, N.H. 03104	467	140	907	[illegible]	(1)
Alpena Museum Association, c/o Jesse Besser Museum, 491 Johnston St., Alpena, Mich. 49707	(1)	4,993	(1)	(1)	(1)
Campbell Museum, Campbell Pl., Camden, N.J. 08101	(1)	(1)	(1)	(1)	(1)
Adirondack Museum, Blue Mountain Lake, New York	0	0	0	10,000	0
Long Island Historical Society, 128 Pierrepont St., Brooklyn, N.Y. 11101	796	1,033	(1)	0	0
Alice T. Miner Colonial Collection, Chazy, N.Y. 12921	853	811	822	0	0
Corning Museum of Glass, Corning, N.Y. 14830	0	1,011	(1)	(1)	(1)
Trotting Horse Museum, 240 Main St., Goshen, N.Y. 10924	(1)	40	(1)	(1)	(1)
Henry L. Ferguson Museum, Fishers Island, N.Y. 14453	14	86	71	0	0
Johnstown Historical Society, 17 North William St., Johnston, N.Y. 12095	29	54	59	0	0

Footnote at end of table.

MUSEUMS CLASSIFIED BY IRS AS PRIVATE FOUNDATIONS—Continued

Name of museum	4 percent excise tax paid			Income from private foundations	
	1971	1972	1973	1968	1973
Storm King Art Center, Mountainville, N.Y. 10953	(1)	2,634	(1)	(1)	(1)
Frick Collection, 1 East 70th St., New York, N.Y. 10021	$52,935	$77,513	[4] $70,000	$0	$4,050
American Museum of Immigration, Liberty Island, New York, N.Y. 10004	(1)	221	(1)	(1)	(1)
Millicent A. Rogers Memorial Museum, c/o Jerome W. Sinsheimer, 660 Madison Ave., New York, N.Y. 10021	(1)	17	(1)	(1)	(1)
Hill-Stead Museum, c/o Manufacturers Hanover Trust Co., 350 Park Ave., New York, N.Y. 10022	(1)	172	(1)	(1)	(1)
Dutchess County Historical Society, P.O. Box 88, Poughkeepsie, N.Y. 12601	377	381	(1)	0	0
Genesee County Museum, 445 St. Paul St., Rochester, N.Y. 14605	(1)	138	(1)	(1)	(1)
Rochester Historical Society, c/o Security Trust Co., 1 East Ave., Rochester, N.Y. 14638	(1)	534	(1)	(1)	(1)
Sleepy Hollow Restoration, P.O. Box 245, Tarrytown, N.Y. 10591	38,448	43,519	48,115	0	0
Woodstock Museum, 747 Chillicothe Rd., Amora, Ohio 43202	(1)	133	(1)	(1)	(1)
Dawes Arboretum, Rural Route 5, Newark, Ohio 43055	10,726	14,242	14,094	0	0
Barnes Foundation, Merion, Pa. 19066	(1)	(1)	(1)	(1)	(1)
Merrick Free Art Gallery and Museum, c/o Union National Bank, New Brighton, Pa. 15066	()	673	(1)	(1)	(1)
Colonial Flying Corps Museum, 1200 Packard Bldg., Philadelphia, Pa. 19102	(1)	3	(1)	(1)	(1)
John J. Tyler Arboretum, c/o Providence National Bank, 1632 Chestnut St., Philadelphia, Pa. 19103	(1)	157	(1)	(1)	(1)
Taylor Memorial Arboretum, Girard Trust Bank, Philadelphia, Pa. 19101	(1)	306	(1)	(1)	(1)
Widner Memorial Museum, 1518 Republic Bank Bldg., Dallas, Tex. 75201	(1)	(1)	(1)	(1)	(1)
Kimbell Art Museum, Fort Worth, Tex. 76107	(1)	12,859	(1)	(1)	(1)
Heard Natural Science Museum and Wildlife Sanctuary, Route 2 McKinney, Tex. 75069	0	0	1,828	0	1,000
Lynchburg Museum, c/o Fidelity National Bank, P.O. Box 700, Lynchburg, Va. 24505	200	747	(1)	(1)	(1)
Sheldon Art Museum, Archaeological and Historical Society, East Middlebury, Vt. 05740	(1)	239	(1)	(1)	(1)

[1] Information not available or not yet computed.
[2] Not open.
[3] Advance ruling for public charity status under regulation section 1.507-2(e) "60-month procedure".
[4] Estimated.

Excerpts From Letters to American Association of Museums in Response to AAM Survey to Museums Classified by IRS as Private Foundations

"The excise tax on our P.O.F. status constitutes approximately ten percent (10%) of our annual operating deficit." James P. Hurley, Executive Director, Long Island Historical Society, Brooklyn, New York

"Additional burden is (the) necessary expense of (a) professional accountant preparing (the) tax forms." Peter Van Kleeck, Treasurer, Dutchess County Historical Society, Poughkeepsie, New York

"Along with the tax and restriction on contributions, the costs of detailed accounting to the IRS should be also considered." "The public test should be whether the general public uses the foundation's operating assets." Edward J. Durkin, The Dawes Arboretum, Newark Ohio

"Our educational offerings to students and adults are reduced by the amount paid as excise tax." John W. Harbour, Jr., Sleepy Hollow Restorations, Inc., Tarrytown, N.Y.

"Maintenance, security, utilities, and related expenditures are rather well fixed. One cannot reduce them without closing down parts of the Museum. Excise taxes are, therefore, not paid by reducing basic operating expenses, but rather are taken from funds that normally would be available for educational programs." Charles van Ravenswaay, Director, Winterthur Museum, Winterthur, Delaware

"Our work with school groups has been curtailed . . . it has meant dropping

many programs." Mrs. Mary B. Gifford, Curator, Fall River Historical Society, Fall River, Massachusetts

"We are a new museum not yet open to the public. This tax is already a burden on our limited resources and we expect this burden toincrease substantially in years to come." Edward A. Pacey, Treasurer, Western Museum of Mining & Industry, Colorado Springs, Colo.

Mr. McGRATH. Yes, both of these adverse effects were not foreseen in 1969. And I want to emphasize the distinction between the privafe foundations which accumulate money for distribution and museums which use all of their income for their charitable programs. The only fault of these museums has consisted of having a high percentage of income from their endowments. And at the time that their endowments were created prior to 1969, this was the tax policy, to encourage that kind of assurance for the future, for the perpetuation of these museums, and in many cases, to assure free admission to the public.

The application of the excise tax to pay the cost of IRS auditing of 1969 was not extended to cover other public charitable institutions such as hospitals, universities and churches, and those that could meet the formula test, but because of this quirk in the formula it has been applied to this limited number of museums. I hope your committee will appreciate the problem and afford treatment to these private operating foundation museums equal to that of public charities.

Senator HARTKE. Let me ask you, would you apply this same type of modification of the law to a private museum?

Mr. McGRATH. To private foundation museums?

No. There is a program, Senator, of museum accreditation that the AAM implemented in 1970. And one of the elements in the definition of a museum for purposes of accreditation is that it has to be open to the public on some regular schedule. Prior to 1969, actually prior for our purposes to the museum accreditation, there were about three or four museums around the country that were not open to the public on a regular schedule. In fact, one of them, when I testified before the House Ways and Means Committee in 1969, Chairman Mills asked the J. Paul Getty Museum and he named it for the record as requiring a written invitation to attend, and I said for purposes of a museum accreditation, that would not be considered a museum.

Since that time, that institution has opened its doors. The limited number, and there were only three or four that we could identify around the country, had opened themselves to the public and they use their full resources for the preservation of the collection, for research on it, and for use by the public.

Senator HARTKE. Would you apply the same modification to nursing homes?

Mr. McGRATH. I am not as familiar with nursing homes.

Senator HARTKE. They have the same problem. How about high school scholarship funds? They have these problems. These are the areas in which this same definite problem exists.

Mr. McGRATH. Yes, high schools. I understand from 509(a) there is a specific exemption and it makes exemption for education,

for universities and educational institutions that provide a degree. But, museums don't grant degrees, so the U.S. Office of Education, for that purpose, does not consider them to be educational.

Senator HARTKE. I am talking about a privately established high school scholarship fund, not for the educational institution itself.

Mr. MCGRATH. For the scholarship itself?

Senator HARTKE. Yes.

Mr. MCGRATH. Well, that would have a pretty private connotation to it as a private determination. In the case of museums, for example, the institution is open to anybody who comes in, not just the student who gets the scholarship.

Senator HARTKE. All right.

I just want to explore with you these possibilities.

Mr. MCGRATH. I appreciate the argument that IRS has made that other types of institutions would then want to be afforded the same treatment.

Senator HARTKE. All right. Let me put it also on this aspect as to what assurances would we have that these museums would not then become the source of a tax dodge?

Mr. MCGRATH. As a private accumulation of wealth? Well, there are two assurances, the first of which would be the enforcement and investigative procedures available within the IRS, and the filing requirements, the form 990, which should be able to determine at least on paper if they are for real, if they are devoting most or all of their resources to serving the public. You also have, admittedly in the private sector, a program now within the national museum organization of a self-policing effort that was not in existence in 1969.

The AAM accreditation program is a pretty strict effort. The batting average to date of museum applicants vis-a-vis those accredited has been to table or reject approximately one out of four applicants. They can be rejected for up to 1 year to correct a known deficiency, or they can be rejected outright. Certainly the IRS has the public enforcement and the AAM has within the profession respect to command that kind of professional service to the public.

As I said, the intent in 1969, from all the material and all of the conversation that I have been able to obtain, centered on improving the charitable output of 501(c)3 institutions. And in the case of museums, they had already been putting out in many cases a deficit type of operation in their efforts to serve the public. A resolution of this problem might be afforded by regulation within the U.S. Treasury Department, but the IRS has said they cannot go below the 10-percent floor regarding endowment income to overall budget under present Congressional instructions.

At least they are unwilling to go below it unless there is some congressional mandate in that direction. Or, a solution could be obtained legislatively and perhaps by amending into section 509(a) a fifth provision for museums, according to the definition set forth in my prepared statement.

Senator HARTKE. Do you object to the 4-percent tax as a matter of policy or just as a matter of rate?

Mr. McGRATH. As a matter of policy, because it is based upon a distinction between museums that is invalid in terms of their function and service to the public and in terms of their programs, education and cultural, in the United States. And it distinguishes solely on the grounds of endowments, which were built up prior to the enactment of the legislation.

I think all museums, as I think universities and churches and hospitals, those that are validly serving the public, should be treated alike if they can be reasonably and effectively identified.

You can now identify these institutions, whereas they could not be that easily and professionally identified prior to 1969.

If I could draw one particular example, the Winterthur Museum in Winterthur, Del. and the Hagley Museum, and the Longwood Botanical Gardens which is not on my list, are all three classified as private operating foundation museums. All three are open to the public the year round. They, in fact, maintain a program of graduate education and museum studies with the University of Delaware. They are as public an institution as you could dream of, other than the source of their funding. They are located in a semirural section of Delaware and Pennsylvania and they just do not have the kind of local public access charitable contributions. If they started charging admission fees right now, they would still be able to count the admission fees as part of that 10-percent floor of public gifts or grants under the 107(b), so they are caught in this bind.

Senator HARTKE. All right. Thank you. I thank you for your testimony.

And if you will submit the rest of that list, that would be fine.

Mr. McGRATH. Be happy to.

[Mr. McGrath's prepared statement follows:]

TESTIMONY OF KYRAN M. McGRATH, DIRECTOR, AMERICAN ASSOCIATION OF MUSEUMS

Mr. Chairman, and members of the Committee, I am grateful for the opportunity to appear before you today and respond to your notice of hearings on problems which may exist in connection with the administration by the Internal Revenue Service of tax laws pertaining to private foundations.

SOME MUSEUMS CLASSIFIED AS PRIVATE FOUNDATIONS, REGARDLESS OF THEIR PUBLIC PROGRAMS

The matter that I wish to point out involves those provisions in the Tax Reform Act of 1969 identifying private foundations, particularly the provisions under Section 509(a). These provisions identify in a generic sense private foundations as those tax exempt organizations which are not expressly classified as public charities under sub-paragraphs within Section 509(a). The formula tests called for in the Tax Reform Act of 1969 in relation to income from public sources, plus the "Facts and Circumstances" test adopted by the Internal Revenue Service, have enabled most museums to obtain a classification as "public charity"; however, a small number of museums that were founded through an initial endowment and funded through the years from endowment income have been unable to meet the formula test in the 1969 legislation, or even the Facts and Circumstances test. Most of these museums are in existence to serve the public through regularly and professionally accepted museum practices and have been examined and found to be operated according to the standards adopted by the museum profession, i.e., museum accreditation (implemented by the AAM in June 1970).

TRA 1969 HINDERS CHARITABLE EFFORTS OF MUSEUMS CLASSIFIED AS PRIVATE OPERATING FOUNDATIONS

The impact of the Tax Reform Act of 1969 on those museums which have been unable to meet the public charity test regarding income sources and which have subsequently been classified as private operating foundations has been significant and in every case adverse to th programs of the museums. The first impact was the direct loss of income in the amount equal to 4% excise tax on endowment income. This has resulted in the following taxes paid by museums listed below:

Name of private operating foundation museum	Amount of excise tax
1. Winterthur Museum, Winterthur, Del.	$121,000
2. Hagley Museum, Wilmington, Del.	68,000
3. Sterling and Francine Clark Art Institute, Williamstown, Mass.	58,800
4. Isabella Stewart Gardner Museum, Boston, Mass.	30,000
Frick Collection, New York, N.Y.	177,500
6. Old Gaol Museum, York, Maine.	946

(1970)

There are other museums in addition to these that are also treated as private operating foundations and must pay the excise tax also, but I was unable to develop a complete list in time for this hearing.

The second adverse impact that affects each of these institutions concerns the requirement for additional reporting in the distribution of income from a private foundation to another private foundation (including a private operating foundation). For fund raising purposes, a number of private foundations have adopted the policy of not distributing monies to other private foundations because of the additional report writing and filings now required by IRS. Granted that this practice is not justified from the theoretical point of view, but because of the additional filing requirements, many foundations refuse to consider grant applications from institutions that are not classified as public charities. As a result, the museums not classified as public charities have been unable and will continue to be unable to obtain funding for museum projects from private foundations.

ADVERSE EFFECT NOT FORESEEN

This double hardship was not contemplated during 1969. I appreciate the intention of Congress to maintain a close scrutiny and legislative oversight on the administration of tax provisions effecting private foundations. I also appreciate the Congressional efforts to prevent undue accumulation of private capital and any violation of the tax-exempt purposes of private foundations. But I want to emphasize the distinction between the privte foundations which accumulate money for distribution and museums which operate in full accord with professionally accepted standards, exist to provide programs for the educational and cultural development of the public, and whose only fault consists of having a high level of income from endowment sources.

The assurance of future funding through the vehicle of endowment was a procedure in full accord with public policy and federal tax provisions prior to TRA 1969. At the time the museums now classified as private operating foundations were created, through substantial endowments from private contributors, the intention of the donors, in accordance with federal tax provisions then in effect, was that the use of the endowment income would sustain the programs of the museum and make them available to the public in perpetuity, usually free from any admission cost. The application of an excise tax to pay the cost of IRS auditing in 1969 was not extended to cover public charitable institutions such s hospitals, universities, churches, and those other tax-exempt organizations which were able to demonstrate a sufficiently broad base of public support. The formula for public support was too high for these museums which had been too successful in the past in building their endowment to provide for the future existence of the institution and its programs for the benefit of the

public. I hope your committee will appreciate this problem and afford treatment to these private operating foundation museums equal to that afforded public charities as defined in Section 509(a).

INTENT OF TRA 1969 TO SUPPORT PUBLIC CHARITIES AND ENCOURAGE THEIR USE OF RESOURCES

The intent of TRA 1969 regarding private foundations was to encourage the distribution of their income and resources to eligible public charities. Accredited private operating foundation museums are public charities in all of their programs and activities, indeed in everything but classification by the Internal Revenue Service. Those museums which are so classified have had to reduce their public programs by amounts equal to the 4% excise taxes they have had to pay on endowment income. The toll taken on their future programs will include losses from future taxes as well as the inability to obtain program monies from regular private foundations. In 1969, the intent of Congress appeared to focus primarily on the public value of the services provided by museums and similar organizations rather than the nature of their income. I believe the test should emphasize the use of their resources, including endowment, collections and programs instead of the category of income.

MUSEUM ACCREDITATION AS ONE TEST

In 1969, the program for museum accreditation had not been developed. The AAM completed its two years of study and implemented the program in June 1970. Since that time, a total of 606 museums have applied for accreditation, 296 are now fully accredited (as meeting the standards established by the profession), and the remainder are either awaiting the final on-site visit or have been tabled or rejected. The average rate for tabling or rejecting is running on out of four applicants. For purposes of accreditation, a museum is defined as: "an organized and permanent non-profit institution, essentially educational or aesthetic in purpose, with professional staff, which owns and utilizes tangible objects, cares for them, and exhibits them to the public on some regular schedule."

The investigative procedure involves the filing of a detailed 25-page questionnaire, interim consideration by a seven-man commission of museum professionals, an on-site visit, and final determination by the commission. Of the examples listed above, all are accredited. (See attached Appendix A for full list of accredited institutions.)

SOLUTION PROPOSED: TREAT ALL MUSEUMS AS PUBLIC CHARITIES

A resolution of this problem might be afforded by regulation within the U.S. Department of Treasury upon an expression of intent on the part of Congress, or upon amendment to existing language in Section 509(a) perhaps by adding "(5)" expressly identifying museums as one of the excepted categories to the private foundation classification. The museum could then be identified according to the definition above, which contains the elements expected for minimal standards within the U.S. museum community.

I hope you will give full consideration to the museums which face this problem, small in terms of other matters facing your Committee and the private foundation question, but large in terms of the institutions involved and the public they serve.

ACCREDITED BY THE AMERICAN ASSOCIATION OF MUSEUMS

NEW ENGLAND REGION

American Clock & Watch Museum, Bristol, Connecticut (5–73)
Stowe-Day Memorial Library & Historical Foundation, Hartford, Conn. (11–73)
Wadsworth Atheneum, Hartford, Connecticut (2–73)
The Marine Historical Association, Mystic, Connecticut (8–72)
New Britain Museum of American Art(New Britain, Connecticut (11–72)
Yale University Art Gallery, New Haven, Connecticut (8–72)
The Mattatuck Historical Society, Waterbury, Connecticut (11–72)

Mid-Firfield County Youth Museum, Westport, Connecticut (2–73)
The Webb Deane Stevens Museum, Wethersfield, Connecticut (2–73)
Bath Marine Museum, Bath, Maine (11–73)
William A. Farnsworth Library & Art Museum, Rockland, Maine (11–72)
Old Gaol Museum, York Maine (11–73)
Mead Art Building, Amherst, Massachusetts (8–72)
Isabella Stewart Gardner Musem, Boston, Massachusetts (2–72)
Museum of Fine Arts, Boston, Massachusetts (2–72)
Museum of Science, Boston, Massachusetts (8–71)
Busch-Reisinger Museum, Cambridge, Massachusetts (5–73)
William Hayes Gogg Art Museum, Cambridge, Massachusetts (5–73)
Concord Antiquarian Museum, Concord, Massachusetts (11–73)
Historic Deerfield, Inc., Deerfield, Massachusetts (8–73)
The Whaling Museum, New Bedford, Massachusetts (2–74)[1]
Merrimack Valley Textile Museum, North Andover, Massachusetts (5–71)
Berkshire County Historical Society Museum, Pittsfield, Mass. (2–74)[1]
Essex Institute, Salem, Massachusetts (8–72)
Peabody Museum of Salem, Massachusetts (8–71)
Connecticut Valley Historical Museum, Springfield, Massachusetts (2–73)
Old Sturbridge Village, Sturbridge, Massachusetts (11–71)
Wenham Historical Association and Museum, Wenham, Massachusetts (8–72)
Cardinal Spellman Philatelic Museum, Massachusetts (8–71)
Sterling and Francine Clark Art Institute, Williamstown, Massachusetts (8–72)
John Woodman Higgins Armory, Worcester, Massachusetts (11–72)
The Currier Gallery of Art, Manchester, New Hampshire (8–73)
Newport Historical Society Museum, Newport, Rhode Island (2–72)
Old Slater Mill Museum, Pawtucket, Rhode Island (11–73)
Bennington Museum and Topping Tavern Museum, Old Bennington, Vermont (8–72)
Fairbanks Museum of Natural Science, St. Johnsbury, Vermont (8–72)

NORTHEASTERN REGION

The Saskatoon Gallery and Conservation Corporation, Saskatoon, Saskatchewan, Canada (11–73)
Delaware Art Museum, Wilmington, Delaware (2–72)
Hagley Museum, Wilmington, Delaware (2–72)
The Henry Francis du Pont Winterthur Museum, Winterthur, Delaware (5–71)
Daughters of the American Revolution Museum, Washington, D.C. (2–73)
National Museum of History and Technology, Washington, D.C. (8–72)
The Octagen, Washington, D.C. (2–73)
The Textile Museum, Washington, D.C. (11–73)
The Baltimore Museum of Art, Baltimore, Maryland (2–72)
The Peale Museum, Baltimore, Maryland (11–72)
Walters Art Gallery, Baltimore, Maryland (2–72)
Morris Museum of Arts and Science, Convent, New Jersey (11–72)
Montclair Art Museum, Montclair, New Jersey (11–72)
The Newark Museum, Newark, New Jersey (11–72)
Roberson Center for the Arts & Sciences, Binghamton, New York (5–73)
Adirondack Museum, Blue Montain Lake, New York (8–73)
The New York Botanical Garden, Bronx, New York (5–71)
The New York Zoological Park and New York Aquarium of the New York Zoological Society, Bronx, New York (11–72)
The Brooklyn Museum, Brooklyn, New York (8–72)
Buffalo Museum of Science, Buffalo, New York (8–72)
Vanderbilt Museum of the Suffolk County Museum Commission, Centerport, New York (2–72)
The Fenimore House, The Farmers' Museum, and The Carriage & Harness Museum of The New York State Historical Association, Cooperstown, New York (8–72)
The Corning Museum of Glass, Corning, New York (11–73)

[1] As of February 28, 1974.

Guild Hall, Inc.—Museum Section, East Hampton, New York (2–73)
Heckscher Museum, Huntington, New York (8–72)
Sleepy Hollow Restorations, Inc., Irvington, New York (2–73)
Herbert F. Johnson Museum of Art, Ithaca, New York (5–71)
American Museum of Natural History, New York, New York (11–72)
The Frick Collection, New York, New York (8–73)
Museum of Contemporary Crafts of the American Crafts Council, New York, New York (2–73)
Museum of the American Indian, New York, New York (8–72)
Museum of the City of New York, New York, New York (8–72)
The Methropolitan Museum of Art, New York, New York (8–72)
The New-York Historical Society, New York, New York (8–72)
The Solomon R. Guggenheim Museum, New York, New York (5–71)
Whitney Museum of American Art, New York, New York (8–72)
Remington Art Museum, Ogdensburg, New York (5–73)
Shaker Museum Foundation, Inc., Old Chatham, New York (2–72)
Yager Museum of Hartwick College, Oneonta, New York (2–72)
Potsdam Public Museum, Potsdam, New York (11–72)
Campbell-Whittlesey House, Rochester, New York (2–73)
Memorial Art Gallery of the University of Rochester, Rochester, New York (5–73)
Rochester Museum & Science Center, Rochester, New York (5–73)
The Schenectady Museum, New York (2–74)[1]
The Parrish Art Museum, Southampton, New York (2–73)
Suffolk Museum and Carriage House, Stony Brook, New York (5–73)
Nassau County Museum, Syosset, New York (2–73)
Fort Ticonderoga, Ticonderoga, New York (2–72)
Rensselaer County Historical Society, Troy, New York (8–72)
Jefferson County Historical Society, Watertown, New York (8–72)
Hudson River Museum, Yonkers, New York (2–74)[1]
Westmoreland County Museum of Art, Greensburg, Pennsylvania (2–72)
North Museum of Franklin and Marshall College, Lancaster, Pa. (5–72)
Academy of Natural Sciences, Philadelphia, Pennsylvania (8–72)
Franklin Institute Science Museum, Philadelphia, Pennsylvania (2–74)
Pennsylvania Academy of Fine Arts, Philadelphia, Pennsylvania (5–73)
Philadelphia Museum of Art and the Rodin Museum, Philadelphia, Pennsylvania (5–73)
Buhl Planetarium & Institute of Popular Science, Pittsburgh, Pennsylvania (5–72)
Carnegie Museum of Natural History, Pittsburgh, Pennsylvania (11–72)
Musuem of Art, Carnegie Institute, Pittsburgh, Pennsylvania (11–72)
Lycoming County Historical Museum, Williamsport, Pennsylvania (2–73)
The General Gates House and Golden Plough Tavern, The Log House, The Bonham House, and The Museum of the Historical Society of York County, York, Pennsylvania (5–72)

MIDWESTERN REGION

Art Institute of Chicago, Chicago, Illinois (8–72)
Field Museum of Natural History, Chicago, Illinois (5–72)
The Adler Planetarium, Chicago, Illinois (8–71)
Early American Museum, Mahomet, Illinois (2–73)
Lakeview Center for the Arts and Sciences, Peoria, Illinois (2–73)
Illinois State Museum & Dickson Mounds Museum, Springfield, Illinois (2–72)
Indian University Museum, Bloomington, Indiana (11–71)
Indianapolis Museum of Art, Indianapolis, Indiana (8–72)
The Children's Museum of Indianapolis, Inc., Indianapolis, Indiana (11–71)
Ball State University Art Gallery, Muncie, Indiana (5–72)
Art Gallery, University of Notre Dame, Notre Dame, Indiana (11–73)
Sheldon Swope Art Gallery, Terre Haute, Indiana (8–72)
Sanford Museum and Plantarium, Cherokee, Iowa (5–72)

[1] As of February 28, 1974.

Davenport Municipal Art Gallery, Davenport, Iowa (2–73)
Davenport Museum, Davenport, Iowa (2–74)[1]
Norwegian-American Museum, Decorah, Iowa (11–72)
Charles H. MacNider Museum, Mason City, Iowa (2–73)
University of Michigan Museum of Art, Ann Arbor, Michigan (2–73)
Cranbrook Institute of Science, Bloomfield Hills, Michigan (8–72)
Detroit Institute of Arts, Detroit, Michigan (5–73)
Kresge Art Center Gallery, East Lansing, Michigan (5–73)
Flint Institute of Arts, Flint, Michigan (5–72)
Grand Rapids Public Museum, Grand Rapids, Michigan (5–71)
Kalamazoo Institute of Arts, Gilmore Art Center, Kalamazoo, Michigan (8–72)
Historic Projects Division, Mackinac Island, Michigan (11–73)
Minneapolis Institute of Arts, Minneapolis, Minnesota (8–72)
Walker Art Center, Minneapolis, Minnesota (5–73)
Minnesota Museum of Art, St. Paul, Minnesota (8–72)
The Science Museum of Minnesota, St. Paul, Minnesota (5–71)
Museum of Art and Archaeology, Columbia, Missouri (5–73)
Nelson Gallery of Art, Atkins Museum of Fine Arts, Kansas City, Missouri (8–72)
Albrecht Gallery of Art, St. Joseph, Missouri (8–73)
St. Joseph Museum & Pony Expres Stables Museum, St. Joseph, Missouri (2–72)
McDonnell Planetarium, St. Louis, Missouri (11–71)
St. Louis Art Museum, St. Louis, Missouri (2–73)
St. Louis Medical Museum, St. Louis, Missouri (11–71)
Akron Art Institute, Akron, Ohio (11–72)
Stark County Historical Society Museum, Canton, Ohio (2–73)
Cincinnati Art Museum, Cincinnati, Ohio (2–72)
The Taft Museum, Cincinnati, Ohio (2–72)
Cleveland Museum of Art, Cleveland, Ohio (5–73)
Howard Dittrick Museum of Historical Medicine, Cleveland, Ohio (2–72)
The Columbus Gallery of Fine Arts, Columbus, Ohio (5–72)
Ohio Historical Center of the Ohio Historical Society, Columbus, Ohio (2–73)
Johnson-Humrickshouse Memorial Museum, Coshocton, Ohio (11–73)
Dayton Art Institute, Dayton, Ohio (5–72)
Dayton Museum of Natural History, Dayton, Ohio (5–72)
The Massillon Museum, Massillon, Ohio (5–73)
Allen Memorial Art Museum, Oberlin, Ohio (5–73)
The Toledo Museum of Art, Toledo, Ohio (2–73)
Circus World Museum, Baraboo, Wisconsin (8–71)
Logan Museum of Anthropology, Beloit College, Beloit, Wisconsin (8–72)
Neville Public Museum, Green Bay, Wisconsin (2–74)[1]
Tallman Restorations of the Rock County Historical Society, Janesville, Wisconsin (8–72)
Kenosha Public Museum, Kenosha, Wisconsin (8–73)
G.A.R. Memorial Hall Museum, Madison, Wisconsin (2–74)[1]
Museum of the State Historical Society of Wisconsin, Madison, Wisc. (2–74)[1]
Milwaukee Public Museum, Milwaukee, Wisconsin (11–72)
The John Nelson Bergstrom Art Center and Museum, Neenah, Wisconsin (2–73)
Paine Art Center and Arboretuh, Oshkosh, Wisconsin (2–73)
Marathon County Historical Society, Wausau, Wisconsin (8–72)

MOUNTAIN-PLAINS REGION

Colorado Springs Fine Arts Center, Colorado Springs, Colorado (5–71)
Colorado State Museum, Denver, Colorado, and six subsidiaries (11–72):
1. El Pueblo Museum, Pueblo, Colorado
2. Fort Garland, Alamosa, Colorado
3. Fort Vasquez, Platteville, Colorado
4. Ute Indian Museum, Montrose, Colorado
5. Healy House and Dexter Cabin, Leadville, Colorado
6. Baca House and Bloom House, Trinidad, Colorado

[1] As of February 28, 1974.

Denver Museum of Art, Denver, Colorado (8–72)
Denver Museum of Natural History, Denver, Colorado (11–72)
Historical Museum and Institute of Western Colorado, Grand Junction, Colorado (11–71)
Greeley Municipal Museum, Greeley, Colorado (2–72)
Kansas Health Museum, Halstead, Kansas (11–73)
Wichita Art Museum, Wichita, Kansas (2–72)
Wichita Historical Museum, Wichita, Kansas (2–72)
Montana Historical Society Museum, Helena, Montana (11–73)
Hastongs Museum House of Yesterday, Hastings, Nebraska (8–73)
Nebraska State Historical Society Museum, Lincoln, Nebraska (2–73)
Sheldon Memorial Art Gallery, Lincoln, Nebraska (5–72)
University of Nebraska State Museum, Lincoln, Nebraska (5–73)
Joslyn Art Museum, Omaha, Nebraska (2–73)
Maxwell Museum of Anthropology, Albuquerque, New Mexico (5–73)
Ernest Thompson Seton Memorial Library and Museum, Cimarron, New Mexico (2–73)
Woolaroc Museum, Bartlesville, Oklahoma (5–72)
Museum of the Great Plains, Lawton, Oklahoma (2–72)
Stovall Museum of Science and History, Norman, Oklahoma (5–72)
Oklahoma Art Center, Oklahoma City, Oklahoma (11–73)
Art Museum of South Texas, Corpus Christi, Texas (2–73)
Corpus Christi Museum, Corpus Christi, Texas (2–73)
Dallas Health and Science Museum, Dallas, Texas (11–72)
Dallas Museum of Natural History, Dallas, Texas (11–72)
El Paso Museum of Art, El Paso, Texas (8–72)
Amon Carter Museum of Western Art, Forth Worth, Texas (5–71)
Fort Worth Art Center, Fort Worth, Texas (8–72)
Fort Worth Museum of Science and History, Fort Worth, Texas (5–71)
Harris County Heritage & Conservation Society, Houston, Texas (8–72)
McAllen International Museum, McAllen, Texas (11–72)
Carson County Square House Museum, Panhandle, Texas (2–72)
Marion Koogler McNay Art Institute, San Antonio, Texas (11–71)
John K. Strecker Museum, Waco, Texas (5–73)
Star of the Republic Museum, Washington, Texas (8–72)
Wichita Falls Museum and Art Center, Wichita Falls, Texas (5–73)
State Museum of the Wyoming State Archives & Historical Department, Cheyenne, Wyoming (2–73)

WESTERN REGION

Anchorage Historical and Fine Arts Museum, Anchorage, Alaska (2–73)
University of Alaska Museum, College, Alaska (2–73)
Museum of Northern Arizona, Flagstaff, Arizona (11–73)
Heard Museum of Anthropology and Primitive Art, Phoenix, Arizona (11–73)
Phoenix Art Museum, Phoenix, Arizona (11–73)
Arizona-Sonora Desert Museum, Tuscon, Arizona (8–72)
Arizona State Museum, University of Arizona, Tucson, Arizona (2–72)
San Bernardino County Museums, Bloomington, California (2–73)
Rancho Santa Ana Botanic Garden, Claremont, California (8–72)
Fresno Arts Center, California (2–73)
San Joaquin County Historical Museum, Lodi, California (2–73)
Long Beach Museum of Art, Long Beach, California (8–72)
Los Angeles County Museum of Art, Los Angeles, California (8–72)
Los Angeles County Museum of Natural History, Los Angeles, California (5–71)
The Oakland Museum, Oakland, California (2–73)
Pacific Grove Museum of Natural History, Pacific Grove, California (11–72)
Diablo Valley College Museum, Pleasant Hill, California (11–72)
Riverside Municipal Museum, Riverside, California (8–72)
Fine Arts Gallery of San Diego, San Diego, California (2–73)
San Diego Museum of Man, San Diego, California (2–73)

San Diego Natural History Museum, San Diego, California (2–74)[1]
Serra Museum, Library and Tower Gallery, San Diego, California (2–73)
California Academy of Sciences, San Francisco, California (5–71)
The Fine Arts Museum of San Francisco (formerly, Legion of Honor/de Young Memorial, San Francisco, California (11–72)
Center of Asian Art and Culture, San Francisco, California (11–72)
San Francisco Museum of Art, San Francisco, California (2–73)
San Mateo County Historical Association, San Mateo, California (11–72)
Coyote Point Museum, San Mateo, California (11–72)
Santa Barbara Museum of Art, Santa Barbara, California (5–73)
Santa Barbara Museum of Natural History, Santa Barbara, California (5–73)
The Art Galleries, Santa Barbara, California (5–73)
Santa Cruz Museum, Santa Cruz, California (11–72)
Lyman House Memorial Museum, Hilo, Hawaii (5–73)
Honolulu Academy of Arts, Honolulu, Hawaii (11–72)
Mission Houses Museum, Honolulu, Hawaii (11–72)
Idaho State Historical Museum, Boise, Idaho (11–72)
Nevada State Museum, Carson City, Nevada (2–72)
Northeastern Nevada Museum, Elko, Nevada (11–73)
Nevada Historical Society Museum, Reno, Nevada (2–72)
Columbia River Maritime Museum, Astoria, Oregon (11–72)
Oregon Historical Society Museum, Portland, Oregon (2–74)[1]
Oregon Museum of Science & Industry, Portland, Oregon (8–72)
Portland Art Museum, Portland, Oregon (5–71)
B. F. Larsen Gallery, Brigham Young University, Provo, Utah (11–73)
Utah Museum of Fine Arts, Salt Lake City, Utah (8–72)
Utah Museum of Natural History, Salt Lake City, Utah (8–72)
Museum of History and Industry, Seattle, Washington (8–73)
Seattle Art Museum, Seattle, Washington (8–72)
Thomas Burke Memorial, Washington State Museum, Seattle, Washington (5–71)
Cheney Cowles Memorial Museum, Spokane, Washington (8–72)
Tacoma Art Museum, Tacoma, Washington (5–73)

SOUTHEASTERN REGION

The Arkansas Arts Center, Little Rock, Arkansas (8–72)
Arkansas State University Museum, State University, Arkansas (5–73)
Lowe Art Museum, Coral Gables, Florida (8–72)
Florida State Museum, Gainesville, Florida (2–73)
University Gallery, Gainesville, Florida (2–73)
Loch Haven Art Center, Inc. Orlando, Florida (5–71)
The Henry Morrison Flagler Museum, Palm Beach, Florida (11–73)
Society of the Four Arts, Palm Beach, Florida (11–72)
John & Mable Ringling Museum of Art, Sarasota, Florida (5–72)
Historic St. Augustine Preservation Board, St. Augustine, Florida (8–73)
Museum of Fine Arts, St. Petersburg, Florida (5–72)
Norton Gallery and School of Art, West Palm Beach, Florida (8–72)
The High Museum of Art, Atlanta, Georgia (8–72)
Augusta Richmond County Museum, Augusta, Georgia (2–72)
Columbus Museum of Arts and Crafts, Inc., Columbus, Georgia (11–72)
Louisiana Arts and Science Center, Baton Rouge, Louisiana (2–72)
New Orleans Museums of Art, New Orleans, Louisiana (2–72)
Mississippi State Historical Museum, Jackson, Mississippi (2–72)
Lauren Rogers Memorial Museum, Laurel, Mississippi (2–73)
The Country Doctor Museum, Bailey, North Carolina (5–72)
Charlotte Nature Museum, Inc., Charlotte, North Carolina (5–72)
Mint Museum of Art, Charlotte, North Carolina (5–72)
Duke University Art Museum, Durham, North Carolina (2–73)

[1] As of February 28, 1974.

North Carolina Museum of Art, Raleigh, North Carolina (2–73)
North Carolina Museum of History, Raleigh, North Carolina, and eight of its subsidiary musegums (5–72):
1. Alamance Battleground, Burlington, North Carolina
2. Charles B. Aycock Birthplace, Fremont, North Carolina
3. Historic Bath, Bath, North Carolina
4. Brunswick Town, Southport, North Carolina
5. Fort Fisher, Kure Beach, North Carolina
6. James K. Polk Birthplace, Pineville, North Carolina
7. Town Creek Indian Mound, Mount Gilead, North Carolina
8. Zebulon B. Vance Birthplace, Weaverville, North Carolina

St. John's Art Gallery, Inc., Wilmington, North Carolina (5–72)
Old Salem and the Museum of Early Southern Decorative Arts, Winston-Salem, North Carolina (8–72)
Reynolda House, Winston-Salem, North Carolina (8–72)
Historic Camden, Camden, South Carolina (8–72)
The Charleston Museum, Charleston, South Carolina (8–73)
Gibbes Art Gallery, Charleston, South Carolina (5–72)
Columbia Museums of Art and Science, Columbia, South Carolina (5–71)
Florence Museum, Florence, South Carolina (8–73)
Greenville County Museum of Art, Greenville, South Carolina (2–73)
Brookgreen Gardens, Murrells Inlet, South Carolina (11–72)
B. Carroll Reece Museum & Memorial Archives, Johnson City, Tenn. (11–73)
Frank H. McClung Museum, Knoxville, Tennessee (8–72)
Student's Museum, Inc., Knoxville, Tennessee (2–72)
Brooks Memorial Art Gallery, Memphis, Tennessee (5–73)
Memphis Pink Palace Museum, Memphis, Tennessee (5–73)
The VMI Museum, Virginia Military Institute, Lexington, Virginia (8–72)
Hall of Valor, New Market Battlefield Park, New Market, Virginia (11–73)
The Mariner's Museum, Newport News, Virginia (2–72)
The Valentine Museum, Richmond, Virginia (5–72)
The Virginia Museum of Fine Arts, Richmond, Virginia (8–73)
Colonia Williamsburg, Williamsburg, Virginia (2–72)
Williamsburg, Virginia (2–74)[1]
Abby Aldrich Rochefeller Folk Art Collection of Colonial Williamsburg, Ogelbay Mansion Museum, Wheeling, West Virginia (11–72)

[1] As of February 28, 1974.

ACCREDITATION STATISTICS: FEB. 28, 1974

GEOGRAPHIC DISTRIBUTION

	Applications	Accredited museums
Total	580	296
New England	81	37
Connecticut	24	9
Maine	5	3
Massachusetts	40	20
New Hampshire	5	1
Rhode Island	3	2
Vermont	4	2

ACCREDITATION STATISTICS: FEB. 28, 1974

GEOGRAPHIC DISTRIBUTION

	Applications	Accredited museums
Northeast	124	61
Delaware	3	3
District of Columbia	14	4
Maryland	5	3
New Jersey	8	3
New York	74	37
Pennsylvania	20	11
Midwest	114	61
Illinois	16	6
Indiana	14	6
Iowa	7	5
Michigan	18	8
Minnesota	9	4
Missouri	11	7
Ohio	22	14
Wisconsin	17	11
Mountain-Plains	67	37
Colorado	8	6
Kansas	5	3
Montana	2	1
Nebraska	5	5
New Mexico	6	2
North Dakota		
Oklahoma	11	4
South Dakota	1	
Texas	26	15
Wyoming	3	1
Western	89	51
Alaska	3	2
Arizona	11	5
California	50	25
Hawaii	4	3
Idaho	2	1
Nevada	3	3
Oregon	6	4
Utah	3	3
Washington	7	5
Southeast	100	48
Alabama	3	----
Arkansas	4	2
Florida	21	10
Georgia	9	3
Kentucky	2	----
Louisiana	7	2
Mississippi	3	2
North Carolina	16	9
South Carolina	8	7
Tennessee	11	5
Virginia	12	7
West Virginia	4	1
Canada	3	1
Puerto Rico	1	----
American Samoa	1	----

TYPE OF MUSEUM

	Applicant museums	Accredited museums
Art	196	106
History	104	50
General	88	36
Natural History	47	23
Historical Society Museum	28	17
Historic House	21	12
Children's	12	6
Science	17	9
Professional	5	1
Arts Center	10	9
Planetarium	4	3
Military	4	1
Botanical Garden	3	2
Zoo	2	1
Other	39	20
Anthropology	7	6
Indian	5	1
Marine	6	4
Ethnic	2	----
Outdoor	2	2
Regional	3	1
Transportation	2	----
Doll & Toy	2	----
Armor & Arms	1	1
Glass	1	----
Horological	1	1
Literary	1	----
Musical	1	----
Philatelic	1	1
Religion	1	1
Restoration	1	2
Boy Scouts	1	----
Archeology	1	----
University (in addition to being particular type)	52	39

PRIMARY SUPPORT

Private	229	130
Combination	137	64
Municipal	77	41
State or Regional	75	37
Other	62	24
Contributions	17	3
College	15	6
County	12	5
Federal	2	1
Trust	9	6
Boy Scouts	1	1
Church	1	
Indian Tribe	1	
Society	1	1
Public Membership	1	1
Service League	1	
Corporate	1	

BUDGET CATEGORY

Below $50,000	180	64
$50,000 to below $100,000	114	46
$100,000 to below $250,000	108	77
$250,000 to below $500,000	68	40
$500,000 to below $750,000	20	19
$750,000 to below $1,000,000	18	13
$1,000,000	46	37
Incomplete	26	----

Accreditation Stages

Applications	580
Questionnaires Returned	424
Questionnaires Still Out	156
Accredited	296
Tabled One Year	30
Rejected	29
Visiting Committee Evaluation Taking Place	50
Interim Approval—Awaiting Visiting Committee	34
Questionnaire Being Reviewed	10

Senator HARTKE. All right now, the next witness will be Mrs. Nancy M. Glasgow, president of the National Association of Foundations, Inc.

Good morning.

STATEMENT OF NANCY M. GLASGOW, PRESIDENT, NATIONAL ASSOCIATION OF FOUNDATIONS

Mrs. GLASGOW. It is a pleasure to be here, Mr. Chairman. And I prepared a summary of the principle points included in the statement of the National Association of Foundations, Inc.

One. The Internal Revenue Service has made a sincere effort to assist and instruct private donor foundations before, during, and after the Tax Reform Act of 1969.

Two. The private donor foundations have also made a sincere effort to comply with the new rules and regulations imposed by the Tax Reform Act of 1969.

Three. The National Association of Foundations, Inc., has kept private donor foundation members informed of all the latest development affecting their status as private donor foundations by bulletins, membership letters, and material from the Federal Government particularly the Internal Revenue Service. We cover all hearings affecting private donor foundations and take notes and gather all information which could be of help to our member foundations.

Four. Need for investigation of the Government Printing Office to find out why private donor foundations cannot receive their orders for the Federal Register and other documents without undue delay.

Five. Need for some form of special security to protect private individuals running private donor foundations from undue harrassment by the public, usually radical groups.

Mr. Chairman, distinguished members of the Senate Committee on Finance and the Subcommittee on Foundations, it is a pleasure for me to have the opportunity to express my views before you on such an important area for private donor foundations. I shall confine my remarks to the "way the Internal Revenue Service administers the tax laws pertaining to private foundations." We, in Washington, have the responsibility to cover the Federal Government and keep those out in the States informed of matters that affect their general welfare. "Ignorance is no excuse of the law." By mailing out all information received from the Internal Revenue

Service concerning private donor foundations, we can be sure our member foundations have a good background knowledge of the rules and regulations they must live under.

"Eternal vigilance is the price of freedom," and we feel confident that the members of N.A.F. are paying close attention to what is happening in the Nation's capitol. The National Association of Foundations, Inc., has been serving the needs of private donor foundations long before the Tax Reform Act of 1969. Our founder, Dr. Charles L. McClaskey, presented his statement on the 1969 Tax Reform Act during the Senate Finance Committee Hearings of 1969. Since that time, I have assumed the running of the association on the death of my father and have continued his work with the loyal support of our N.A.F. members.

Most of the requests we receive are for information. I try to answer them and if it is something we cannot handle we refer the foundation to the Internal Revenue Service. I cannot comment on any complaints from private donor foundations regarding the implementation of this law as I have never received a complaint of any kind from our N.A.F. members or from any other foundation contacting us.

I think the Internal Revenue Service has made a real effort to instruct the private donor foundations by sending out many instruction sheets on the new rulings and holding hearings at the Internal Revenue Service Headquarters and asking for comments from interested foundations. The bulk of the material I receive from the Internal Revenue Service is reproduced and sent out to our members. Occasionally, the Internal Revenue Service prepares special material for foundations which is printed in the Federal Register. Since 1971, I have been unable to get a correct order from the Government Printing Office. I have taken the matter up with Hon. J. Glenn Beall, Republican of Maryland, and he has written to the Public Printer on behalf of the private donor foundations. I have written to the Commissioner of Internal Revenue and also to the Superintendent of Documents concerning this problem. It is not unusual to have to make four or five trips to the Government Printing Office Bookstore over a period of months to get one order correct.

The private donor foundation must assume a passive role in national life because of their tax exempt status. Please understand, Gentlemen, because you don't receive a large volume of mail doesn't mean the private donor foundations are not interested in the committee. I have found a considerable interest shown in their own subcommittee and in the activities of the Congress by the private donor foundations. We live in troubled times, the chairman of the Subcommittee on Foundations, Honorable Vance Hartke, Democrat of Indiana, spoke at the first hearings last October about the changes which would take place in the seventies and how private donor foundations would come in for their share of trouble along with everyone else in the establishment of this country. Thought should be given to some form of security to protect the private donor foundation movement from the radical groups who are even now seeking ways of assailing foundations. "The danger to this Nation

is not from without but from within." The protection of private wealth is a necessity for the freedom of all!

Thank you.

[An attachment to Mrs. Glasgow's statement follows:]

THE NATIONAL ASSOCIATION OF FOUNDATIONS, INC., CODE OF ETHICS

PREAMBLE

The National Association of Foundations, Inc., in order to inspire public confidence, affirm the fairness of the self-assessment tax process and to indorse the basic principle of promoting private philanthropy through tax-exemption, does proclaim ethical standards of conduct for foundations as follows.

(1) Be ever mindful that they are organized for philanthrophy and not for private gain.

(2) Recognize that they hold a public trust.

(3) Realize that tax-exemption imposes special obligations to operate solely in the public interest.

(4) Never permit a foundation to be used for the self-service or private interests of its donors, trustees, directors, officers or employees.

(5) The foundations recognize the need to make distributions annually commensurate with their incomes and consistent with their respective charters.

(6) To make investments as a prudent man would in a fiduciary capacity.

(7) Willingly furnish required information when requested by duly constituted local, State and Federal authorities.

Senator HARTKE. The last witness this morning will be Patricia S. Senger, Public Citizen Tax Reform Research Group.

Good morning.

STATEMENT OF MS. PATRICIA S. SENGER, PUBLIC CITIZEN TAX REFORM RESEARCH GROUP; ACCOMPANIED BY ROBERT BRANDON, DIRECTOR, PUBLIC CITIZEN TAX REFORM RESEARCH GROUP

Ms. SENGER. Good morning.

Mr. Chairman, I would like to thank you for the opportunity to testify here this morning.

I am with the Tax Reform Research Group, and with me is our director, Bob Brandon. We are supported by the Public Citizen, which was founded by Ralph Nader. Public Citizen is a non-profit, non-exempt organization which is supported and paid for by $15 contributions.

Foundations in America have become a multi-million dollar enterprise, supported largely by tax subsidies from Federal, State and local Government. Our purpose here is to encourage this committee to study a most important and basic question: Are we getting our money's worth for the immense tax subsidies we give to foundations?

The crucial question is too frequently answered with broad generalities and specifically selected examples rather than analysis based on substantial facts and statistics. The spokesmen for the foundations who have appeared before this committee speak with pride of the accomplishments of private philanthropy, and they do indeed have much to be proud of. However, there are critics who have

studied this question and would conclude otherwise. Nielsen, in his study "The Big Foundations" argues that foundations are far from the dynamic, creative, reformist institutions that some of their defenders claim. He states that probably not one-twentieth of their grants have any measurable impact upon the major social problems of our country.

The point for this committee to consider is that the Federal Government, which supports these foundations so heavily by not taxing their investments or contributing income, has little control and even less information on their practices. Neither the Congress that writes the subsidy nor the IRS that administers it collects enough systematic information on the foundation business to judge its effectiveness—to even guess whether we are in fact getting our money's worth.

A conservative estimate is that foundations held assets valued at between $28–$30 billion in 1972. Even with inflation that is still an impressive amount today. In a year when the administration is proposing a restrictive budget, it is worth noting the magnitude of those assets. That $28 billion would finance all the programs of the Department of Housing and Urban Development at the projected 1975 levels for 5 years. It would support the State Department for almost 36 years. It would fund the entire Federal judicial system and the Federal legislature for more than 28 years.

Clearly, foundations could, and often do, fulfill an important social function. Unfortunately, however, they are all too often created and operated to help the wealthy family that set them up. Social considerations then become secondary to the interests and the power of the families involved. In these situations, the foundation is little more than a tax shelter for the family which enables them to donate a large block of stock to the foundation, and then continue to control that stock by sitting on the board of the foundation.

According to a study done by economist Richard Bourdon of the Tax Reform Research Group in 1972, an example of just such an arrangement is the Lilly Endowment which has one of the lowest payout rates of the large foundations.

The reason for the low payout rate is that the Lilly Corp. board of directors prefers to let the company's profits increase the value of the stock rather than pay it out annually to stockholders as dividends. This way, stockholders—mainly the Lilly's—receive the gain when the stock is sold and are taxed at lower capital gains rates, rather than taxed at ordinary income rates on annual dividends. What this means for the endowment is that it receives very little current income from its huge investment in the family firm. While the Lilly Corp. continues to make an average of 23.8 percent return on equity, the Lilly Endowment grants in 1972 amounted to only 1.1 percent of its assets—1972 figures.

If the endowment directors were primarily concerned with contributions to charity, they would have reinvested some of the money years ago in stocks that pay higher dividends. The median return on equity for all U.S. companies for the last 5 years has been 11 percent. Even savings and loan associations now pay better than 7.7

percent on savings accounts. The only reason the directors would continue an investment policy which gives them only 1.1 percent to pay out to charity is that they are more interested in the family corporation than in supporting charity.

WHO CONTROLS FOUNDATION MONEY?

So the real question, it seems, is now whether or not these foundations do good, but whether they do the best they can with the funds. Since so much of the money they use is a Federal subsidy, it is therefore money out of the pockets of the average taxpayer. But the average taxpayer has no voice in the use or the amount of that money, no voice in choosing the projects it supports, and no voice in deciding whether or not charity should be so heavily supported in the first place.

An interesting point was made in a recent Nader study about the duPont's of Delaware on the subject of economic control through foundations. The study states:

> Instead of paying taxes to the government, the duPont family has created an alternative government through personal gifts and foundation grants * * * In 1968, for example, the 36 duPont foundations distributed between $12 million and $13 million in grants * * * In the same year, the officials of both Wilmington and New Castle County each spent about the same amount—$16 million and $9 million—to carry out their local government functions.
>
> The difference * * * is that the government may be run by democratic process while foundations are operated on the personal preferences of the donor * * * elected officials make budget proposals which are subject to public debate; officials know they not not be re-elected if they antagonize their constituents. But the directors of a foundation are appointed by the donor. Foundations make no budget proposals to the public and do not ask for public debate.

With so much power held in the hands of a few, it is the responsibility of Congress to protect the interests of the average taxpayer.

While it is impossible to accurately judge whether the direct benefits of private foundations are equitably distributed, the tax subsidy benefits are clearly not distributed fairly.

The Internal Revenue Code allows taxpayers to deduct, within generous limits, charitable donations from their income otherwise subject to tax. As do most tax subsidies, this provision confers substantially more benefit on the wealthy than on the average taxpayer. Take the wealthy taxpayer—in the 70-percent bracket—contributing, say, $100 to charity. His tax savings on the transaction are $70. On the other hand, the average taxpayer is possibly in the 25-percent bracket. His $100 contribution will give him a tax savings of $25. Of course, for the majority of taxpayers who take the standard deduction, contributions to charity yield no extra tax benefits.

Not only does the wealthy taxpayer get a larger tax benefit, dollar for dollar, but he also gets much larger absolute benefits. Statistics from the 1972 tax expenditure indicate the median-income taxpayer benefited an average of about $15 from the charitable deduction provision, the wealthiest taxpayer benefited an average of over $8,000 each.

Contributions to foundations are a special case of charitable donation. They provide potentially even greater benefit to the wealthy

donor, compared to the small taxpayer who cannot afford to establish his own foundation. But they are not necessarily the most efficient ways to support charity.

A simple example illustrates the point:

(A) Assume I'm an average taxpayer. I give my money to a local charity—a $100 donation. Almost immediately, my donation is expended for a charitable purpose. Once spent, it rejoins the general circulation of taxable money.

(B) But if I do it differently—I'm rich and decide to have a lawyer set up the Senger Foundation. Then I contribute my $100. I put my foundation money in a bank account, say at 5½ percent interest. Each year I collect the $5.50 and donate it to some charity. If I'm in the 70-percent tax bracket, the Government has forgone $70 in taxes collectable immediately. Instead, charity must wait over 12 years, just to get $70 in benefits. And that doesn't count the interest the Government could have collected just by investing the $70 in taxes in the first year.

This simple example shows why foundations can be inefficient. The tax deduction comes immediately, but the benefits to charity may be long afterward.

And, of course, I could designate that the money be used for any legal purpose whether or not it is socially relevant or acceptable. For example, I could require the funds to be used to study methods of legalizing slavery.

The question of payout rates also deserves examination.

In determining the percentage of foundation assets paid out to charity, we again face uncertain figures. Forbes gives figures indicating a charitable payout in 1971 of about 6 percent for all foundations. The American Association of Fund-Raising Counsel lists the 50 largest private foundations, with an average charitable payout of slightly over 5 percent in 1971.

Within this group, some foundations—such as Ford—made substantially larger contributions, while others—such as Pew and Lilly—contributed substantially less. In fact, only 2 of the top 10 met or exceeded the 4½ percent payout requirement for 1972. That was Ford and Mellon.

By contract, the Peterson Commission has recommended that:

> * * * foundations be required to make annual distributions to charity in the range of 6 to 8 percent of their asset market values. The annual total return of a wide variety of balanced investment funds over the previous ten years was about 9 to 10 percent. Allowing for an annual rate of inflation of 2 to 3 percent, we felt that a payout of 6 to 8 percent would permit a reasonably manged foundation to maintain its size in real dollars.

Foundation spokesmen reply to discussions of payout by observing that charitable activity is not to be measured in quantity alone.

They argue: Foundations are more effective philantropic instruments than individuals just because of the advantages of organization. Those advantages include continuity, certainty of finding professional staffing, and the bringing to bear upon selected problems of larger sums of money—and therefore a broader and stronger array of talents—than individual efforts had theretofore been able to supply.

Unfortunately, many foundations do not live up to this potential. Waldemar Nielsen, in his study of the major foundations, points out that the caliber of the foundation staff generally correlates with the caliber of the program. Most of the big foundations, he reports, have little or no such staff.

> About one-quarter employ no full-time professionals, operating with only an accountant or secretary. Another quarter operate with only one or two professionals, in some cases on less than a full-time basis. A few employ what could be called a professional nucleus. Only ten have reasonably well-developed and capable staffs.

Furthermore, according to a study done in 1972, there are about 1,062 full-time foundation administrators in the country. Fully 25 percent of them work for the Ford Foundation and 15 percent for the Rockefeller Foundation. Seven foundations with assets of more than $100 million and 126 with assets between $10 million and $100 million have no staffs at all.

The study stated:

> With no one to tend store many foundations have been unable to discharge even the most elementary administrative responsibilities.

The Peterson Commission makes a number of recommendations to aid smaller foundations in obtaining expert staff support, even though they may not be able to afford as much in-house help as the larger foundations. Without adequate staff, foundations inevitably must find it difficult to live up to the potential wisdom which should accompany the power to dispense $28 billion in assets and the income from those assets.

Finally, the quality of foundation programs must to some significant degree reflect the quality of foundation trustees.

RECOMMENDATIONS

The 4-percent excise tax on foundations has yielded significant revenues beyond that needed by IRS for administration of the tax laws applying to foundations. In fact, many of the spokesmen for foundations argue that the excise tax should be reduced. However, it would seem that a wiser use of the money is that proposed by Representative Patman. He suggested that the money collected be shared with the States Attorneys General who are in a far better position to monitor some of the functions of foundations than the IRS. We agree with that proposal. For example, Julius Greenfield, assistant attorney general for the State of New York which has 18,000 foundations, explained to the committee:

> It is under State law and in the State courts that most corrective action can be taken. * * * Actions against foundation managers for improper administration, removal of officers and directors and the election of new officers and directors, dissolution of foundations and the disposition of their assets to qualifying charities and also a full judicial accounting by foundation administrators.

All of this is available through the State courts.

A small amount of the excise tax should also be used by the Federal Government to fund a study of the economics of founda-

tions. Several important questions need to be answered, and alternatives to the present system should be examined.

1. How might the costs of the tax subsidy for foundations be reduced and made more equitable? In 1972, the charitable income tax deduction for individuals cost the Federal Government about $3.5 billion. That is an expensive program annually, considering that we know little about its effects. Even less is known about the charitable deduction provisions of the estate and gift tax laws. The property tax exemption for foundation property must be included. And finally, any cost analysis must also take into account the cost of administration which is incurred by the governments overseeing these laws.

2. How might foundation programing be made more effective? This issue is often obscurred when foundation spokesmen raise objections to Government specification of "good" and "bad" programs. This is not the issue here. Rather, the question is whether the Government might not greatly improve foundation programs by specifying staff requirements and other elements of decision quality.

3. How might the law be amended to protect against the possible abuses that still exist? A look at the 1972 payout rates indicates that many of the large foundations are still not complying with the requirements of the 1969 act. Other problems might still exist in areas relating to self-dealing. For example, there is little assurance that property donated to a foundation is not overvalued to give the donor—who is also often in control of the foundation—a larger charitable deduction. Another question is how much money goes to support company purposes such as research which specially benefits the donating company. An example of similar uses can be seen in some of the functions supported by the duPont foundations which include a company museum and schools for company officials' children.

Another area which needs monitoring is that of excessive administrative expenses.

4. What are the costs and benefits of terminating foundation lives after a specified number of years? When private universities are forced—largely by Government budget cuts—to consume the capital resources, as Yale, Princeton and Stanford have recently done, it may be time to analyze this question carefully with regard to foundations.

5. How might foundation trustees be made more charitable or representative of the Nation as a whole? It is time to make a public assessment of the composition of the boards of directors and the degree to which their decisions over $28 billion in assets reflect national values. On the other hand, more than rhetoric is needed to determine whether donations would seriously decline as a result of reform in this area.

6. Finally and most important, how are foundations complying.

The total penalties assessed on foundations for failure to meet the different requirements of the 1969 act nearly trebled after the first year of operation from $36 thousand in fiscal year 1971 to $103 thousand in fiscal 1972. That figure again more than doubled in fiscal

1973 to $236 thousand. It seems that as a general observation, they are having increasing difficulty complying with the terms of the act. An inquiry is needed into the causes of the problems.

The reporting requirements of the 1969 act and the extensive discretion given to the Treasury Department to require additional information from foundations are available to aid in collecting all this information.

In summary, we're urging that Congress carefully study costs and benefits of foundations. Congress cannot afford to relax just because the 1969 act was successfully passed. Foundations cannot be expected to reform themselves alone. They need your help.

Thank you.

Senator HARTKE. You have raised some very good points. There is not any question about that. Some of the material you related to demonstrates the lack of knowledge by referring to the Peterson report and the Nielsen book, both of which were basically done before the effects of the 1969 act could be assessed.

Ms. SENGER. That is correct.

Senator HARTKE. Let me ask you what about using part of the 4 percent for the study of the facts?

Ms. SENGER. A study of the facts? Well——

Senator HARTKE. Well, I mean if there is one thing that is obvious, I think that has been obvious to us from the beginning, it is the dearth of information that is really available.

Ms. SENGER. Right. I think the witnesses here this morning have pointed that out, that we do not even know how many foundations there are. The estimates on their assets range from $20 billion to $60 billion but we just do not know the exact figures.

Senator HARTKE. My own judgment is we are going to touch on some of these things. But, one of the real purposes of these hearings is to sort of open up that door and find out if we can get more information.

You mentioned one thing. For example, you said that the Government should specify the types of administrators or staffing requirements. Would that not be having the Government interfere?

Ms. SENGER. What we have suggested is that a study be done of the feasibility of setting minimum standards.

Mr. BRANDON. We already have many Government programs which, in fact, do have Federal guidelines and guidance attached to them, and I think when we are talking about a program costing the taxpayers as much as $3.5 billion we should have some Federal guidelines.

Senator HARTKE. All right. I have no further questions for you and I want to thank you for your very valuable statement.

Mr. BRANDON. Thank you.

[Ms. Senger's prepared statement follows:]

STATEMENT OF PATRICIA S. SENGER, ATTORNEY, PUBLIC CITIZEN TAX REFORM RESEARCH GROUP

Mr. Chairman and Distinguished Members of the Committee: Thank you for the opportunity to testify here this morning. Foundations in America have

become a multi-million dollar enterprise, supported largely by tax subsidies by federal, state and local government. The most important point in considering the the laws on foundations is the fact that the federal government, which supports these foundations heavily by not taxing their investment or contribution income, has little control and even less information on their practices. Neither the Congress that writes the subsidy nor the IRS that administers it collects enough systematic information on the foundation business. Without that information it is impossible to gauge what the foundations do and whether they use their money efficiently. The question is: are we getting our money's worth for the immense tax subsidies we grant to foundation.

That crucial question is too frequently answered with broad generalities and specially selected examples rather than analysis based on substantial facts and statistics. The spokesmen for the foundations who have appered before this committee speak with pride of the accomplishments of private philanthropy, and they do indeed have much of which to be proud. However, there are critics, such as Waldemar Nielsen who in his study "The Big Foundations" concludes that the big foundations are far from the dynamic, creative, reformist institutions that some of their most eloquent defenders have claimed. According to his analysis, not one-tenth (probably not one-twentieth) of their grants have any measurable impact upon the major social problems confronting the nation at the present time.

A conservative estimate is that foundations held assets valued at between $28-$30 billion in 1972. Even with inflation that is still an impressive amount today. In a year when the administration is proposing a restrictive budget, it is worth noting the magnitude of those assets. That $28 billion would finance all the programs of the Department of Housing and Urban Development at the projected 1975 levels for five years. It would support the State Department for almost 36 years. It would fund the entire federal judicial system and the federal legislature for more than 28 years.

In short, foundations hold a lot of money. An indeterminate amount—but doubtless quite large—consists of tax money forgone by federal, state and local governments. It is high time that we weigh the costs of forgone government services against the value of the tax subsidy program for foundations.

Clearly, foundations could, and often do, fulfill an important social function. Unfortunately, however, they are all too often created and operated to help the wealthy family that set them up. Social considerations then become secondary to the interests and the power of the families involved. In these situations, the foundation is little more than a tax shelter for the family which enables them to donate a large block of stock to the foundation, and then continue to control that stock by sitting on the board of the foundation. The main concern is not the amount of money given to charities annually, but the control of the stock and, through it, the corporation. The stock is held by the foundation, rather than owned by the family outright for tax purposes.

According to a study done by economist Richard Bourdon of the Tax Reform Research Group in 1972, an example of just such an arrangement is the Lilly Endowment which has one of the lowest payout rates of the large foundations. The study pointed out that five of the seven directors of the Endowment were also directors of the Eli Lilly Corporation, including Mr. Eli Lilly himself. Ruth A Lilly sat on the Endowment board alone. The Lilly family owned about $1 billion of Lilly Corporation stock which amounted to about 25% of the corporation, and the Endowment held another 20%. Today, the Endowment board has 11 members, only one of them a member of the family. The record of charitable contributions has not changed, however, with the new board.

The reason for the low payout rate is that the Lilly Corporation board of directors prefers to let the company's profits increase the value of the stock rather than pay it out annually to stockholders as dividends. This way, stockholders (mainly the Lillys) receive the gain when the stock is sold and are taxed at lower capital gains rates, rather than taxed at ordinary income rates on annual dividends. What this means for the Endowment is that it receives very little current income from its huge investment in the family firm. While the Lilly Corporation continues to make an average of 23.8% return on equity, the Lilly Endowment grants in 1972 amounted to only 1.1% of its assets (1972 figures).

If the Endowment directors were primarily concerned with contributions to charity, they would have reinvested some of the money years ago in stocks that pay higher dividends. The median return on equity for all U.S. companies for the last five years has been 11%. Even Savings and Loan Associations now pay better than 7% on savings accounts. The only reason the directors would continue an investment policy which gives them only 1.1% to pay out to charity is that they are more interested in the family corporation than in supporting charity.

WHO CONTROLS FOUNDATION MONEY?

So the real question, it seems, is not whether or not these foundations do good, but whether they do the best they can with the funds. Since so much of the money they use is a federal subsidy, it is therefore money out of the pockets of the average taxpayer. But the average taxpayer has no voice in the use or the amount of that money, no voice in choosing the projects it supports, and no voice in deciding whether or not charity should be so heavily supported in the first place.

An interesting point was made in a recent Nader study about the duPont's of Delaware on the subject of economic control through foundations. The study states:

"Instead of paying taxes to the government, the duPont family has created an alternative government through personal gifts and foundation grants . . . In 1968, for example, the 36 duPont foundations distributed between $12 million and $13 million in grants . . . In the same year, the officials of both Wilmington and New Castle County each spent about the same amount—$16 million and $9 million—to carry out their local government functions.

"The difference . . . is that the government may be run by democratic process while foundations are operated on the personal preferences of the donor . . . elected officials make budget proposals which are subject to public debate; officials know they may not be re-elected if they antagonize their constituents. But the directors of a foundation are appointed by the donor. Foundations make no budget proposals to the public and do not ask for public debate. With so much power held in the hands of a few, it is the responsibility of Congress to protect the interests of the average taxpayer."

It is the difficult task of Congress to weigh the costs and benefits of tax exempt foundations and decide on national policy. Congress must be attentive to the interests of average taxpayers—who must bear a heavier tax load or reduced government services, in proportion to the size of the tax subsidy program for foundations—as well as the interests of potential beneficiaries of foundation largesse. Needed for this decision are sufficient facts. This statement appears self-evident until we consider the following: Although foundations today hold about $30 billion in assets, there is no accurate record of the complete assets held by foundations today, or even the number of foundations which exist! Of course, there is little accurate information yet available on the proportion of total foundation wealth which would have gone to support government services but for tax subsidy in the form of a deduction or exemption.[1] Without such information, it is difficult to weigh costs and benefits except in general terms.

THE TAX SUBSIDY BENEFITS ARE INEQUITABLY DISTRIBUTED AMONG TAXPAYERS

While it is impossible to accurately judge whether the direct benefits of private foundations are equitably distributed, the tax subsidy benefits are clearly not distributed fairly.

The Internal Revenue Code allows taxpayers to deduct, within generous limits, charitable donations from their income otherwise subject to tax. As do most tax subsidies, this provision confers substantially more benefit on the wealthy than on the average taxpayer. Take the wealthy taxpayer—in the 70% bracket—contributing, say, $100 to charity. His tax savings on the transac-

[1] The assumption here is that the money would have been collected in tax. Although it might have been sheltered by use of other tax devices, those would have entailed a different set of costs and benefits deserving analogous evaluation.

tion are $70. On the other hand, the average taxpayer is possibly in the 25% bracket. His $100 contribution will give him a tax savings of $25. Of course, for the majority of taxpayers who take the standard deduction, contributions to charity yield no extra tax benefits.[2]

Not only does the wealthy taxpayer get a larger tax benefit dollar for dollar, but he also gets much large absolute benefits. Statistics from the 1972 tax expenditure indicate the median income taxpayer benefited an average of about $15 from the charitable deduction provision, the wealthiest taxpayers benefited an average of over $8,000 each.

Adjusted gross income class	Number of returns per income class	Percent of returns in each income class	Deductibility of charitable contributions (other than education)	Deductibility of contributions to educational institutions
$0 to $3,000	17,180,193	23.1	0.29	
$3,000 to $5,000	9,981,704	13.4	2.00	0.30
$5,000 to $7,000	8,839,820	11.9	9.05	0.79
$7,000 to $10,000	12,606,192	16.9	15.57	1.59
$10,000 to $15,000	14,613,620	19.6	28.06	3.97
$15,000 to $20,000	6,445,678	8.7	58.86	10.84
$20,000 to $50,000	4,427,371	5.9	185.21	20.33
$50,000 to $100,000,000	405,463	0.5	1,109.84	49.33
$100,000 and over	91,286	0.15	8,106.39	76.68

Contributions to foundations are a special case of charitable donation. They provide potentially even greater benefit to the wealthy donor, compared to the small taxpayer who cannot afford to establish his own foundation. But they are not necessarily the most efficient way to support charity.

A simple example illustrates the point:

(A) Assume I'm an average taxpayer. I give my money to a local charity—a $100 donation. Almost immediately, my donation is expended for a charitable purpose. Once spent, it rejoins the general circulation of taxable money.

(B) But if I do it differently—I'm rich and decide to have a lawyer set up the Senger Foundation. Then I contribute my $100. I put my foundation money in a bank account, say at 5½% interest. Each year, I collect the $5.50 and, donate it to some charity. If I'm in the 70% tax bracket, the government has forgone $70 in taxes collectible immediately. Instead, charity must wait over twelve years, just to get $70 in benefits. And that doesn't count the interest the government could have collected just by investing the$70 in taxes in the first year.

This simple example shows why foundations can be inefficient. The tax deduction comes immediately, but the benefits to charity may be long afterwards.

Establishing a foundation is an opportunity which increases with affluence of the taxpayer. (In this simplified example we have set aside other advantages to the foundation donor. I could always appoint my brother, for a fee of, say, $50 to run the $100 foundation for the next ten years. The assets would amount to only $50 then, and annual payout would only be $2.75.

And, of course, I could designate that the money be used for any legal purpose whether or not it is socially relevant or acceptable. For example, I could require the funds to be used to study methods of legalizing slavery.

The question of payout rates also deserves examination. In determining the percentage of foundation assets paid out to charity, we again face uncertain figures. *Forbes* gives figures indicating a charitable payout in 1971 of about 6% for all foundations. The American Association of Fund-Raising Counsel

[2] Various proposals have been advanced to cure this inequitable result. See, for example, Paul R. McDaniel, "Federal Matching Grants for Charitable Contributions: A Substitute for the Income Tax Deduction," Tax Law Review, Spring 1972, pp. 377–413.

lists the 50 largest private foundations, with an average charitable payout of slightly over 5% in 1971.

Within this group, some foundations—such as Ford—made substantially larger contributions, while others—such as Pew and Lilly—contributed substantially less. In fact, only 2 of the top 10 met or exceeded the 4½% payout requirement for 1972. That was Ford and Mellon.

[Amounts in millions]

Top 10 foundations	1971 assets	1971 grants	Percent	1972 assets	1972 grants	Percent
Ford	$3,260	$225	7	$3,146	$195.7	6.2
Johnson	1,100	3	.....	1,510	35.7	2.3
Lilly	927	10	1	1,248	14.2	1.1
Rockefeller	832	42	5	969	33.3	3.4
Kresge	781	8	1	887	28.9	3.2
Mellon	672	35	5	703	32.0	4.5
Kellogg	488	19	4	491	18.6	3.7
Pew	481	4	1	400	8.7	2.1
Duke	425	20	5	432	18.6	4.3
Mott	288	14	5	409	15.2	3.7

By contrast, the Peterson Commission has recommended that: ". . . foundations be required to make anual distributions to charity in the range of 6 to 8 percent of their asset market values. The anual total return of a wide variety of balanced investment funds over the previous ten years was about 9 to 10 percent. Allowing for an annual rate of inflation of 2 to 3 percent, we felt that a payout of 6 to 8 percent would permit a reasonably managed foundation to maintain its size in real dollars."[8]

The Peterson Commission saw a high payout rate as significant in promoting the valuable effects of foundations. "As long as a high payout requirement assures that foundations will continue to be productive, a mandatory death sentence is not justified," said the Commission in its argument against limitation on the lifetime of a foundation.

Foundation spokesmen reply to discussions of payout by observing that charitable activity is not to be measured in quantity alone.

They argue: Foundations are more effective philanthropic instruments than individuals just because of the advantages of organization. Those advantages include continuity, certainty of finding professional staffing, and the bringing to bear upon selected problems of larger sums of money—and therefore a broader and stronger array of talents—than individual efforts had therefore been able to supply.

Unfortunately, many foundations do not live up to this potential. Waldemar Nielsen, in his study of the major foundations, points out that the caliber of the foundation staff generally correlates with the caliber of the program. Most of the big foundations, he reports, have little or no such staff. "About one-quarter employ no full-time professionals, operating with only an accountant or secretary. Another quarter operate with only one or two professionals, in some cases on less than a full-time basis. A few employ what could be called a professional nucleus. Only ten have reasonably well-developed and capable staffs.

"Within this last group, the range in staff size is considerable: the Ford Foundation has 611 professionals, Rockefeller 160, Carnegie 41, Duke 38, Sloan 30, Danforth 32, Kellogg 27, Rockefeller Brothers 17, and Commonwealth 12. Even

[8] "Foundations, Private Giving, and Public Policy: Report and Recommendations of the Commission on Foundations and Private Philanthropy" 1970. The Commission, headed by Peter G. Peterson, president of the Bell and Howell Co., has come to be known as the Peterson Commission.

the largest foundation staffs, however, are small compared to those of universities and are almost microscopic compared to large corporations and government agencies."

Furthermore, according to a study done in 1972,[4] there are about 1,062 full-time foundation administrators in the country. Fully, 25% of them work for the Ford Foundation and 15% for the Rockefeller Foundation. Seven foundations with assets of more than $100 million and 126 with assets between $10 million and $100 million have no staffs at all.

The study stated:

"With no one to tend store many foundations have been unable to discharge even the most elementary administrative responsibilities.

"In far too many cases there has been no one to establish an operating standard that would pass muster with the most indulgent student of administration; no one to compile, write and distribute a public report; no one to provide the hard data about the foundation for appropriate reference volumes or for those making legitimate inquiry."

The Peterson Commission makes a number of recommendations to aid smaller foundations in obtaining expert staff support, even though they may not be able to afford as much in-house help as the larger foundations. Without adequate staff, foundations inevitably must find it difficult to live up to the potential wisdom which should accompany the power to dispense $28 billion in assets and the income from those assets.

Finally, the quality of foundation programs must to some significant degree reflect the quality of foundation trustees.

RECOMMENDATIONS

The 4% excise tax on foundations has yielded significant revenue beyond that needed by IRS for administration of the tax laws applying to foundations. In fact, many of the spokesmen for foundations argue that the excise tax should be reduced. However, it would seem that a wiser use of the money is that proposed by Rep. Patman. He suggested that the money collected be shared with the States' Attorneys General who are in a far better position to monitor some of the functions of foundations than the IRS. We agree with that proposal. For example, Julius Greenfield, Assistant Attorney General for the State of New York which has 18,000 foundations, explained to the committee:

"It is under State law and in the State courts that most corrective action can be taken. Actions against foundation, managers for improper administration, removal of officers and directors and the election of new officers and directors, dissolution of foundations and the disposition of their assets to qualifying charities and also a full judicial accounting by foundation administrators."

All of this is available through the state courts.

A small amount of the excise tax should also be used by the federal government to fund a study of the economics of foundations. Several important questions need to be answered, and alternatives to the present system should be examined.

1. How might the costs of the tax subsidy for foundations be reduced and made more equitable? In 1972, the charitable income tax deduction for individuals cost the federal government about $3.5 billion. That is an expensive program annually, considering that we know little about its effects. Even less is known about the charitable deduction provisions of the estate and gift tax laws. The property tax exemption for foundation property must be included. And finally, any cost analysis must also take into account the cost of administration which is incurred by the governments overseeing these laws.

2. How might foundation programming be made more effective? This issue is often obscured when foundation spokesmen raise objections to government specification of "good" and "bad" programs. This is not the issue here. Rather, the question is whether the government might not greatly improve foundation

[4] "The Management of Foundations", 1972, New York University Press.

programs by specifying staff requirements and other elements of decision quality.

3. How might the law be amended to protect against the possible abuses that still exist? A look at the 1972 payout rates indicates that many of the large foundations are still not complying with the requirements of the 1969 act. Other problems might still exist in areas relating to self-dealing. For example, there is little assurance that property donated to a foundation is not overvalued to give the donor (who is also often in control of the foundation) a larger charitable deduction. Another question is how much money goes to support company purposes such as research which specially benefits the donating company. An example of similar uses can be seen in some of the functions supported by the duPont foundations which include a company museum and schools for company officials' children. Another area which needs monitoring is that of excessive administrative expenses.

4. What are the costs and benefits of terminating foundation lives after a specified number of years? When private universities are forced—largely by government budget cuts—to consume the capital resources, as Yale, Princeton and Stanford have recently done, it may be time to analyze this question carefully with regard to foundations.

5. How might foundation trustees be made more charitable or representative of the nation as a whole? It is time to make a public assessment of the composition of the boards of directors and the degree to which their decisions over $28 billion in assets reflect national values. On the other hand, more than rhetoric is needed to determine whether donations would seriously decline as a result of reforms in this area.

6. Finally and most importantly, how are foundations complying.

The total penalties assessed on foundations for failure to meet the different requirements of the 1969 Act nearly trebled after the first year of operation from $36 thousand in Fiscal Year 1971 to $103 thousand in Fiscal '72. That figure again more than doubled in Fiscal 1973 to $236 thousand. It seems that, as a general observation, they are having increasing difficulty complying with the terms of the act. An inquiry is needed into the causes of the problems.

The reporting requirements of the 1969 Act and the extensive discretion given to the Treasury Department to require additional information from foundations are available to aid in collecting all this information.

In summary, we are urging that Congress carefully study costs and benefits of foundations. Congress cannot afford to relax just because the 1969 Act was successfully passed. Foundations cannot be expected to reform themselves alone. They need your help.

Thank you.

Senator HARTKE. All right, that concludes the hearing this morning until tomorrow morning at 9:30 a.m.

[Whereupon, at 11:45 o'clock a.m., the hearing was recessed to reconvene on Tuesday, May 14, 1974 at 10 a.m.]

PRIVATE FOUNDATIONS

TUESDAY, MAY 14, 1974

U.S. SENATE,
SUBCOMMITTEE ON FOUNDATIONS,
COMMITTEE OF FINANCE,
Washington, D.C.

The subcommittee met, pursuant to recess, at 9:45 a.m., in room 2221, Dirksen Senate Office Building, Hon. Vance Hartke presiding.

Present: Senator Hartke.

Senator HARTKE. The committee will come to order.

This is the second day of hearings designed to open a public discussion of current issues which affect foundations and other tax exempt organizations. Yesterday, we heard from several witnesses who expressed a variety of concerns about foundation activity.

As I said in my opening statement yesterday, the ultimate question is just how much the public benefits from the tax exemption accorded to foundations. Of course, that is a difficult question to answer, but it must be answered to the satisfaction of Congress and the American people.

So our witnesses today will continue this dialog. In future hearings, the subcommittee will examine the activity of foundations in such areas as education, the performing arts, minority problems, health and mental health, and public television. The subcommittee also plans to take testimony in the future on specific aspects of the Internal Revenue Code which affect tax exempt organizations.

The first witness is Hon. Dewey Bartlett, U.S. Senator from Oklahoma.

Senator, delighted to have you here and honored by your presence.

STATEMENT OF HON. DEWEY F. BARTLETT, U.S. SENATOR FROM OKLAHOMA

Senator BARTLETT. I thank you. Thank you also very much for the hearing today.

Mr. Chairman, I appreciate very much the opportunity to appear before the Subcommittee on Private Foundations to present my views concerning the 4 percent excise tax on the income of private foundations. I appear before the committee because I have introduced S. 1135, a bill to reduce that tax from 4 to 1 percent of net investment income.

You, Mr. Chairman, and the other members of the subcommittee, are of course familiar with the history of section 4940 of the Internal

Revenue Code which imposes the tax that my bill would lower. However, for purposes of the record, let me review that history briefly. Prior to passage of the Tax Reform Act of 1969, the investment income of private foundations qualifying as exempt organizations was not subject to tax. Many exempt organizations were taxed on their unrelated business income, but this tax did not apply to ordinary investment income.

During consideration of the Tax Reform Act by the Committee on Ways and Means, some members voiced the suggestion that private foundations ought to bear some of the burden of the general cost of Government, including providing the funds necessary for more vigorous enforcement of the tax laws relating to exempt organizations. The Committee on Ways and Means responded to these views and imposed a general income tax equal to 7½ percent of the investment income of private foundations.

However, the Senate Committee on Finance concluded that it was inappropriate to levy a general revenue tax on private foundations even though it was appropriate to assess private foundations an audit fee to provide the funds needed by the Internal Revenue Service for the administration of the Internal Revenue Code provisions relating to private foundations and other exempt organizations. The measure recommended by the committee as ultimately passed by the Senate would have imposed on private foundations an audit fee measured by a percentage of the fair market value of the investment assets held by a foundation.

The conference committee on the Tax Reform Act took the middle ground between these two conflicting philosophical views and section 4940, as enacted into law, provided that an excise tax measured by net income would be imposed on private foundations. The current rate of tax, Mr. Chairman, is 4 percent. Experience has shown that this figure produces revenue which is far in excess of what the Treasury needs to audit the activities of all exempt organizations, let alone what it needs to audit just private foundations.

It is because this tax on foundation income has become a general revenue producing measure that I introduced S. 1139 to lower the tax to 1 percent of net investment income, thereby bringing the amount collected into line with the amount that is needed by the Treasury to fund its audit activities. It is my understanding that a tax imposed at the rate of 1 percent of net investment income would produce funds sufficient for this purpose. If this figure is not correct, I would suggest that Treasury be requested to inform the subcommittee as to what precise level of tax would produce the amount that legitimately is needed for compliance activities by the Internal Revenue Service.

Mr. Chairman, I think it is appropriate to provide for the record a statement of the reasons why I believe passage of S. 1135 is not merely desirable but necessary, and is necessary immediately. Initially, I cannot agree in principle with the philosophy that private foundations ought to provide part of the general revenue of our Government. But even putting that point aside, the tax as it currently operates is not justified. It is essential to recognize that even

the 4 percent tax currently imposed is not a tax on private foundations. The tax is a tax on those operating charitable and educational organizations which depend upon private foundations for support.

That this is so may be demonstrated easily by reference to other provisions of the laws governing foundations. Section 4942 of the Internal Revenue Code requires a private foundation to distribute annually a minimum amount for the active conduct of charitable activities. This figure to be distributed each year is derived through the application of rather complicated provisions and it is not necessary to review them in detail at this point. What is critical is a recognition of the fact that the tax on investment income is subtracted from the amount that a private foundation must otherwise distribute each year under section 4942. Thus, the incidence of the tax on investment income is borne dollar for dollar by the charitable and educational organizations that otherwise would have received the moneys that are now being applied to pay the tax.

I find this to be a terribly unfortunate situation. Let me cite but one of the many examples from my own State of Oklahoma to illustrate the reason for my concern. St. Francis Hospital in Tulsa is one of the leading hospitals and medical research institutions in the United States and it has been generously supported from its very inception by a private foundation located in Tulsa. The fact that St. Francis has such a substantial level of private support has enabled it to provide the citizens of Tulsa with some of the most sophisticated and advanced medical facilities in the world. In addition, the medical community resident at St. Francis is of the highest academic and professional level, and has contributed in great measure over the years to the better health of all Americans through research and other activities. Since 1970, when the 4 percent tax became effective, hundreds of thousands of dollars have been diverted from the work of this hospital into the general revenues of the United States. I feel strongly that this diversion is not justified and is not in the best interests of citizens of Oklahoma and the United States.

Viewed as a general revenue measure, the tax on investment income of private foundations raises an insignificant sum of money for the Government, but it takes from active charitable pursuits money that in many cases is critical to the continued existence of many charities, and might have enabled other charities to make even greater contributions to society. Who can tell what might have been done with several additional hundreds of thousands of dollars at St. Francis Hospital in the way of providing new and better medical facilities, or perhaps even in contributing through research to the elimination of significant diseases.

One need not look only at hospitals to understand why I introduced my bill. All around the country many small private colleges that have contributed greatly to our society are being forced to close through lack of support. These examples are specific but they are by no means unique.

Mr. Chairman, I might digress for a moment to point out how important I thought, particularly when I was Governor of the State

of Oklahoma, the contribution made by private educational institutions was. Oklahoma doesn't have a high incidence of private colleges, and therefore, we appreciate very much the ones that we do have and certainly their contribution and innovative methods of education is significant. I think in the extra dollars that would be forthcoming because of this bill to the private colleges and universities over the country would be very significant to education and to the value of education in that State supported colleges and universities because of the innovative aspects of this private education.

I am also concerned, Mr. Chairman, with the fact that the imposition of a tax on the investment income of private foundations for the purpose of increasing the general revenues is a marked departure from the centuries old tradition in this country of encouraging private support of charitable activity. Although the Government has properly undertaken many worthwhile activities in the social and educational fields, I must say that it is my firm conviction that private philanthropy is essential to our country, and that absent private philanthropy many worthwhile institutions will not be able to function and many worthwhile projects will have to be abandoned.

I believe, Mr. Chairman, that the time for action has arrived. Prior to your scheduling these hearings there have been three congressional hearings since 1969 concerning private foundations. You, Mr. Chairman, held hearings on October 1 and October 2, 1973. The Committee on Ways and Means and the Subcommittee on Domestic Finance of the House Committee on Banking and Currency each held hearings in April of 1973. At each hearing a number of witnesses urged that the tax imposed by section 4942 should at least be reduced to a level consonant with Internal Revenue Service audit costs. Thus, Mr. Chairman, it is my opinion that a record of opposition to the collection of more than is necessary to audit exempt organizations has been made in every available forum and legislation is justified. Indeed, I believe that I am correct in saying that, from 1969 on, the Treasury has never favored a tax which would produce revenues greater than that necessary to fund a vigorous enforcement program.

I view S. 1135 as a necessary first step to achieve equity. I should point out, Mr. Chairman, that all this bill does is to bring the level of the tax down to the amounts needed by the Internal Revenue Service to fund its audit activities of exempt organizations. In a sense this bill may be viewed as but a necessary and desirable interim measure. It leaves many questions unanswered that are properly subject to continuing discussion and debate. For example: I question whether a tax on foundation income is the best way of collecting an audit fee. Similarly, many have asked whether private foundations ought to be taxed even to provide for their own audit activities, and if they should, whether the amounts collected ought not be earmarked for this specific purpose.

These questions and others, Mr. Chairman, while a fit subject of debate for the future, are not raised by my bill and do not have to be resolved now. The only purpose of my bill is to return to the original philosophy that prompted the Senate of the United States to provide what it described as an audit fee or a supervisory fee.

Mr. Chairman, the Congress in 1969 acted properly and decisively to eliminate the abuses alleged to exist in the foundation field. Comprehensive statutes now regulate the relationship between a private foundation and those who donate to it, prevent unreasonable accumulations of income or imprudent investments, assure that funds are distributed for active charitable purposes, and prevent the granting of money to individuals for improper purposes. Having done this, Mr. Chairman, there is no reason further to deplete the funds available for charities that are in such dire need of support. The audit fee collected from private foundations should, at most, be no more than is sufficient to provide for the supervision of exempt organizations by the Internal Revenue Service.

The work of a charitable organization is the expression of the love of man for his fellow man—an endeavor of the highest order. The Federal Government should encourage or even provide incentives for charitable activities, but not prevent some of these activities by a revenue tax.

Mr. Chairman, I appreciate the opportunity of appearing before your subcommittee, and I hope that the subcommittee will see fit to act favorably on S. 1135.

Senator HARTKE. Thank you, Senator Bartlett. We have had conversations about the question of whether or not this tax has been more than necessary to conduct the audit and the Internal Revenue Service will be before us to give us detailed information on that and I am certain that will provide us additional information to make an intelligent judgment along this line.

I also requested the IRS to provide us with information as to just what they are doing in regard to tax exempt organizations generally and what type of fee if any would be required, and just what the cost would be to administer such a program.

So thank you, Senator.

Senator BARTLETT. Thank you very much, Mr. Chairman.

Senator HARTKE. Next we have the distinguished president of Concordia College, St. Paul, Minn., Mr. Harvey Stegemoeller, formerly associated with me and my staff. We were sorry to see him leave, but delighted to see him in this position in the very fine private institution of Concordia College.

STATEMENT OF HARVEY STEGEMOELLER, PRESIDENT, CONCORDIA COLLEGE, ST. PAUL, MINN.

Mr. STEGEMOELLER. Mr. Chairman, I assume that I am not to read my statement this morning?

Senator HARTKE. You can proceed in any way you want to. I give you carte blanche authority.

Mr. STEGEMOELLER. Well, I would summarize the three principal points of my statement. The first is the importance of foundations to private education in Minnesota including Concordia College.

The second is to speak of the benefits of the Tax Reform Act of 1969 as they relate to foundations and private education. Certainly, I want to have some comments about how things might even be better if private education at Concordia College got greater benefits.

I start out with a couple of assumptions. I would like to think that we mutually share these assumptions, Senator. The first being that we are a pluralistic society and that the great variety and diversity of institutions and the great variety and diversity of value systems, and the great variety and diversity of approaches to meeting our value system needs are good for what we call the quality of American life.

The alternative is something monolithic, whether it is monolithic government system or monolithic education system or whatever, but a monolithic system. I believe it is not good for the quality of American life.

Now, the importance of foundations to private institutions in Minnesota is quite significant. Thirteen percent of all of the gifts to Minnesota private colleges come from foundations. Now that is of our operating budget. That is, you know, the thing that keeps us going one day at a time and one semester at a time. But of our overall total gifts to private education for all purposes, the foundations provide 28 percent of the total dollar to private education in Minnesota.

Now, I don't know how to say that any other way, Senator. It is just that simple—more than one-fourth of the dollars that come to private education in Minnesota come from foundations, and I would guess that possibly one-fourth of the private colleges in Minnesota wouldn't stay in business without that 28 percent.

Now the Tax Reform Act of 1969 I think has been very helpful. I could give you a list of about 10 or 11 items that I think have been positive contributions from the Tax Act of 1969. The most immediate one is that it has brought about a greater payout. That payout has increased from $14.9 million to $18.4 million and that has gone into the various philanthropic endeavors of Minnesota.

Some people would question whether or not it is a good and healthy thing that this greater payout was $2.5 million above foundation earnings. I think we won't have a major debate about whether or not foundations should have a terminus: should all foundations automatically pass out of human existence, go out of business in a few years? I think I could argue both sides of that if I prepared myself philosophically for it, but I won't.

I think the improvements of the 1969 Tax Act come most clearly in just finding out who they are. In other words, nobody knew who the foundations were. You don't know whether you had 200 or 2,000 in the State of Minnesota or in the Nation. Nobody knew who they were, what they were doing, how to get in touch with them. And at least this flushed them all out. They had to file reports as to who they were, where they were, and what they were doing.

Now they also have to have some kind of staff, individually or through pooled efforts. In the past you might have some uninformed-type dowager who was in control of the family foundation. She didn't have any procedures and she didn't know how to go about it. And if you didn't have some semi-spiritual communication with her, I will call it, there was no way to work with her. I know that from my own personal experience.

Now just having to come up with some staff that knows what their foundation is and what they are supposed to be doing and what the procedures are for making the foundation function, that has been a tremendous contribution to the Tax Act of 1969.

Now the open and full disclosure of foundation practices and policies, that is also an advantage that has come about. Improvement is still necessary there for the less experienced.

I think I will just move on to the third thing, and that is, they could be better. I think we just have a beginning in the tax act in terms of requiring clarification of objectives. I think the foundation, to have the tax advantages which it has, should have very, very clear objectives of how it proposes to meet the public interest. I noticed in your statement yesterday, and it is also in my statement at the last page of my statement, we both use the term "elitism." Elitism I think has been a mark of many foundations in the past. One group of insiders being very friendly and cozy with another group of insiders without having any obligation to spell out objectives, purposes, and results in terms of public interest. So the healthy getting fat and the lean getting weaker and the rich getting richer and the poor getting poorer resulted.

I think we could document all kinds of perversions like that over the past years, but these are much less since 1969.

Finally, I would like to simply encourage any review or reform to be somewhat cautious because I think this is a fairly productive goose, and I would hate to see the goose defeathered and made unhealthy and finally strangled and the golden eggs for philanthropic activities and private education cease to be laid. So I would encourage some caution about moving very rapidly from the Tax Act of 1969 until we have a little better evidence of what the outcome will be.

Senator HARTKE. Thank you, Dr. Stegemoeller. Let me ask you this. Do you have any idea how much—first, you have approximately 500 foundations estimated, right? Is much of that money leaving Minnesota?

Dr. STEGEMOELLER. Yes, I can give you that specifically. We have a good balance of payments in Minnesota. We send out $6.5 million and we bring in $7.3 million. So I would say Minnesota foundation activity has a good balance of payments.

We bring in from non-Minnesota foundations more than we send out by that much.

Senator HARTKE. How much cooperation has there been between the various foundations to coordinate their activities to prevent overlapping and also to provide for some type of cooperation in their projects?

Dr. STEGEMOELLER. Well, I would say that is another advantage of the 1969 act. That is something that has just been coming to the surface where the foundations have started to talk to one another about what they are trying to do. I would refer you to the National Council and the Minnesota Council. And this is from my experience in Minnesota, but it came about the time we were taking the Tax Act of 1969 seriously. At first I sensed some kind of defensiveness.

I think in yesterday's statements you were concerned about foundations thinking only in terms of their own survival rather than what they could accomplish. And I think I detected some defensiveness at first, but we now have a number of cooperative efforts going.

I met with some foundation directors not too long ago to really discuss our mutual concerns. So I think the cooperation level has been greatly improved through the Tax Act of 1969.

Senator HARTKE. How much conversation do you receive from the people who are administering these funds and complaining about law as being inhibiting rather than contributing factor? Do you receive much of that?

Dr. STEGEMOELLER. Well, the major foundations, the largest ones, and I think of the 10 largest in Minnesota, from those I have heard almost no negative comments. I think the negative comments I have heard were some of the smaller kinds of private family foundations that can't quite know how to cope with it. There was only a small amount of money in the foundation, for instance, to meet the criteria of the 1969 act, and so the 1969 act would to all intents and purposes put them out of business. So some of them did go out of business. I have to say that Concordia benefited from a couple of those. They decided to just quit so they dispensed their moneys and quit.

Senator HARTKE. Would it be better if you had some type of State administration of the foundations rather than having the Internal Revenue Service do it on a national basis in order to accommodate the peculiar regional concepts and ideas and problems?

Dr. STEGEMOELLER. Well, I guess I would think so if you had some way of providing a public interest board of monitors or board of auditors or whatever. I guess I would think that could happen better, and at much less cost.

May I ask this question—and I don't know whether they would appreciate my trying to answer it here—but I would like to hear Mr. Alexander's testimony because I ask the question: What has this auditing-monitoring amounted to that is constructive and helpful? $786,000 in fees takes a lot away from programs and projects in Minnesota.

Senator HARTKE. And we will ask him that when he comes.

Dr. STEGEMOELLER. I asked that and the answers I got were, well, we are not too sure, or, as far as we know, nothing, but maybe IRS thinks so.

And you know, some have been audited two, three, four times and some haven't ever heard of the IRS.

Senator HARTKE. Well, we will find out about that. One of the difficulties we have had is we intended to have Mr. Alexander first but due to a conflict in scheduling here, we had to rearrange his schedule and we had to bring some of the other witnesses in first.

Has there been any increase in the amount given? You have indicated here in the last few years the dollars have gone up. Do you believe the increase in contributions is due to the auditing of the foundations, or maybe has it been due to the fact that stock markets have been in the doldrums, and the investment in that field is less desirable?

Dr. STEGEMOELLER. You see, in 1971–72—we speak of academic fiscal years—there was a decrease in it because of the market. Now I am a little bit afraid of 1974–75 as to what actual dollars might be because of the portfolio situation.

I think the increased payout has not been because of auditing. It has been because of the mandatory 6 percent payout. The $750,000 for audit cut the payout.

Senator HARTKE. You think it has been because they had to pay out mandatorially, otherwise they would not have done so?

Well, you said some of the Minnesota foundations have ceased to operate. Now, do you have any idea what the number is of that?

Dr. STEGEMOELLER. I don't. That is one of the mysteries. We don't have any idea. I know of some instances.

Senator HARTKE. You have indicated that the amount of contributions which are received by the foundations in Minnesota provide for a favorable balance in favor of Minnesota. Do you find in this type of concept subsidies for certain activities, and without any comment upon whether they are meritorious or not, do you find in this type of situation it is a fact that the geographical location of many of these foundations is centered in certain areas, and is that a factor which could make formal distribution of tax funds difficult?

Dr. STEGEMOELLER. Well, if I understand your questions, I think Minnesota would have to say it looks pretty healthy——

Senator HARTKE. In other words, I wonder what it is, for example, in Montana?

Dr. STEGEMOELLER. Well, I am not sure, but I know that Montana gets a good bit of the Minnesota foundation money because they are included in the specific geographical concern of some of our largest foundations.

Senator HARTKE. I'm not really spelling out Montana as a State which I am particularly concerned about. I only pointed it out as an example and since our majority leader lives there.

Dr. STEGEMOELLER. I would assume that they would have a very favorable balance because I don't know of a great amount of foundation activity in Montana, but I do know of some generous awards that have gone there. And I should add that Concordia College received a $65,000 grant from a Montana foundation.

Senator HARTKE. In the field of contributions now though, how do you really see anybody determining the basic objectives in the light of what goes on as long as you have the success of the program determined simply on the question of whether or not you give the money away?

In other words, you see, the only failure I can see of a foundation is not the failure of the foundation generally speaking as far as malfeasance—well, not malfeasance, but I mean in the field of malfeasance—the only failure is the simple fact that they run out of money and don't give any money, which is not a very serious failure. It is not like a business failure.

Now how do you judge whether or not they are making their social contribution; whether or not they are meeting their social contribu-

tion? Do you determine it simply on the basis of the fact that they gave Concordia College 28 percent of their budget, for instance?

Dr. STEGEMOELLER. Whatever they give to Concordia, I feel confident that is a good investment.

But to your question, I just feel about the Minnesota foundations, I just feel very comfortable and very positive. And Concordia does not get a lot of foundation money. My predecessor didn't know that world or didn't care about it or something; but I do, and I hope to change that record some. Minnesota colleges are basically excellent and the foundations have helped to bring about or to sustain the excellence.

But apart from private education, there are some really outstanding projects going on. I can think of one dealing with the whole question of alcoholism and that is probably one of the finest programs in the United States; and that is in Minnesota and run through a family foundation. Now whether the family had a problem generations ago, I don't know, but they dedicated the family's resources to this problem. It is just a tremendous program.

Senator HARTKE. Well, in the field of academic donations though, how do you break down this apparent conflict that exists at the present time where you have what amounts to practically feuding between some of the adacemic communities as to how they are really going to use funds and what the overall program is when you just have no definition of academic studies in the United States?

I mean, isn't it true that most curriculums in schools are judged simply on the accreditation, you know, whether they have the required number of professors, and from there on it is a matter of happenstance? Now I don't want you to be too critical of the institutions, but would you care to answer?

Dr. STEGEMOELLER. Well, there are two sides of that coin. We'll take the bad side first.

One of the problems with both Government projects and foundation projects, with granting agencies, is that they look to things to be innovative and distinctive and unusual and they launch these things and they get you committed. So you get this grant for 2 years or 3 years and you have created this thing, whether it be a program, project, or what, and then you are stuck with it without funds to sustain it. How do you dismantle it? And this is something that schools have had a lot of trouble with. I have an excellent program for minority teacher education at Concordia, but now it is difficult to sustain.

On the other side of the coin, the good side, is that innovation, experimentation, is necessary, but I think that also should be related to the objectives of the institution. And here is where Minnesota foundations I think are really taking a look: How can we get long-term values for the institutions rather than immediate or 2-year values?

So to say that here is some money and we hope it turns out okay this year, and so you just spend it the same old way, and if you were

doing a bad job, it stays bad, that, Senator, is not what we had in mind.

One of the foundations has been working purely in terms of what they call "long-term." They think 5 to 10 years is the shortest of that long-term; 10 years or more of value to that institution in order to help make the institution a stronger institution.

Senator HARTKE. In your statement you make the statement that it is important to note that 61 percent of the foundation dollars were for current operations.

Now do you mean that the foundation moneys went for current operations of the educational institutions?

Dr. STEGEMOELLER. Yes.

Senator HARTKE. Is that a legitimate expenditure of foundation funds?

Dr. STEGEMOELLER. Well, when I say "current"——

Senator HARTKE. What I am talking about really is the general operating expenses.

Dr. STEGEMOELLER. Well, as opposed to capital?

Senator HARTKE. That is right.

Dr. STEGEMOELLER. As opposed to buildings, and, for instance, building a wing on the art center?

Senator HARTKE. Well, I am not specifically speaking about this. I was talking about the general kind of operating expenses as distinguished from programmatic expenses.

Dr. STEGEMOELLER. When I say "current operating" I would include any new program or——

Senator HARTKE. Well, let me give you an example of what I have in mind. There is a small institution down in southern Indiana where I come from which presents a social problem similar to much of the United States, whether they know it or not. Very simply the population of southern Indiana is decreasing. Now, as far as the State population is concerned, it is anticipated that it will actually decrease. It is anticipated that the total population will decrease in the decimal census of 1980 for the first time in history.

Now that is not unique for some States. Many States have had a decrease in population. I think North Dakota and South Dakota and Iowa, all three, have had a decrease in population. Many of the western States also have had actually numerical decreases in population.

Now there is a small school called Oakland City College, which has had a very difficult time in keeping accredited amongst everything else. Yet, in that part of southern Indiana it provides practically, and has for a long time, practically the only avenue for some of those people to obtain a higher education. Now they really don't need money to go ahead and have a cancer research laboratory or have a study of whether or not the gull wasp is going to take over the United States or not. And incidentally, that is an old Kinsey project in case you didn't know. I would state here parenthetically Dr. Kinsey of sex fame originally had the theory that the gull wasp

would have an increase in population and would become the dominant factor in all of society and conquer the world, and they had the mentality to do so. Well, thank goodness we got over that kick.

But anyway, Oakland College just needs money to pay professors, and secretaries, and to go ahead and get new desks and pay for the repairs for the locker room door and so on.

Now is this a legitimate expense of foundation money?

Dr. STEGEMOELLER. I think so.

Senator HARTKE. And I do too. I didn't want to leave the impression that I didn't think so. I think if we could see that they continue, it might be better than giving Harvard and Yale all of this expertise so that they can't even find time for their graduate students to teach any more.

Dr. STEGEMOELLER. I guess so. I can see a way of distinguishing between corporate support of education and foundation support. I think a lot of private research projects, whether it is dealing with petrochemical, or medical, or cancer, or pharmaceutical, or what-have-you type of thing, I think that maybe the corporate support could go for these short duration special projects. And foundation support as I see it should give long-term strength to the institutions in the country.

Senator HARTKE. Yes. Well, all right. Thank you, Dr. Stegemoeller. We have been delighted to see you again. We appreciate your coming here

I also appreciate the seminar you gave us last night on the practical aspects of political life and college activities.

Dr. STEGEMOELLER. Thank you

[The prepared statement of Harvey Stegemoeller follows:]

STATEMENT OF HARVEY STEGEMOELLER, PRESIDENT OF CONCORDIA COLLEGE, ST. PAUL, MINN.

I have had the opportunity to review the hearings before this Committee last October and have noted your definition of your task as the examination of the extent to which such private philanthropy as is represented by the foundations of this country "can and should be encouraged so that important human needs can continue to be met." You also indicated your desire to assess the effect of the Tax Reform Act of 1969, specifically with respect to the remedying of abuses that may have existed and the maximizing of public benefits derived from the tax benefits which foundations enjoy.

My own response to the questions implicit in your Committee's assignment is that the kind of private philanthropy represented by foundations is indeed important and ought to be encouraged, and that the human needs to be met are so many and so vast that everything possible should be done to maximize the public benefits which can be derived from them.

The vantage point from which I view the operation of foundations is as the President of a small mid-western college, private and church-related.

According to figures submitted to your Committee by Dr. Goheen on the geographical distribution of grants, one of the under-privileged areas was the West North-Central region, which has 8% of the population and received 4% of the grants. Minnesota is part of that region and we would obviously be happy to have that situation improved. Nonetheless, Minnesota is fortunate in having something over 500 foundations, 10 of which have combined assets of nearly $500 million. Minnesota also has twenty or more private colleges. The comments which I will make will reflect the experience of these colleges with foundations in general, and Minnesota foundations in particular.

I will address myself to the following questions:

1. To what extent are the private colleges dependent on foundation grants?

2. What effect has the Tax Reform Act of 1969 had on the availability of such foundation grants?

3. In what ways could foundations be more helpful in meeting the needs of such institutions as I represent?

I. THE DEPENDENCE OF PRIVATE COLLEGES ON PHILANTHROPY IN GENERAL AND FOUNDATIONS IN PARTICULAR.

For the last fiscal year (1972–73) 13% of the operating budgets of the 17 colleges which are members of the Minnesota Private College Council came from gifts ($13 million out of $100 million). This was a slightly larger percentage than was the case in 1971–72 when 12.3% of the budgets were covered by gifts and slightly less than in 1969–70 when the figures was 14%. The dollar figure in the most recent year, however, was nearly two million more than in either of the earlier years.

A more detailed report covering 15 of the 17 colleges shows that foundations are the largest single source of gifts, providing $4,768,404 out of a total of $17,023,161, received from all sources for all purposes. This represents 28% of the total gifts received. Of that total $2,923,073 (61%) was for current operations and $1,845,331 (39%) was for capital purposes. Sources of support in the order of dollar amounts received and the respective percentages were as follows:

	Amount	Percent
Foundations	$4,768,404	28
Nonalumni individuals	3,861,133	23
Alumni	2,974,575	17
Religious denominations	2,799,377	16
Business corporations	1,820,384	11
Other	799,288	5

National reports (CFAE) indicate that just under 26% of the total giving to higher education comes from foundations. It would appear therefore that Minnesota's private colleges with 28% of their gift income coming from foundations have special reason to be grateful for the measure of support they have received. It is, of course, also possible that the total gifts received from all sources has been smaller than in many other parts of the country and hence foundation givink constitutes a larger percentage though it may not constitute a larger amount.

Statistics do not tell the whole story, or even the most important part of it. I would like to indicate by a few illustrations some concrete ways in which they have helped private colleges address specific needs.

(a) Minnesota has a rather large Indian population with very few Indian students entering college. A foundation grant enabled the colleges to set up an office, engage an Indian Education coordinator to supervise a program of recruitment of Indian students and the development of supportive programs at the colleges at which the Indians enrolled. The number of Indian students has grown from less than fifty to nearly one hundred and fifty in three years and the number of Indian staff members at these colleges has increased from three to fourteen. Indians predominate in the committee which make the grants to institutions as well as in the committee which gives general supervision to the program. About one third of a million dollars has been invested in this program.

(b) Minnesota has an extensive public two-year college system which now enrolls a large number of high school graduates. Because of certain limitations in the state scholarship and grant program, very few of these students were transferring to the private four-year colleges when they completed their two-year program. A foundation developed a program of grants for such students who might want to transfer to private colleges and funded it with one and a quarter million dollars to be used over a four-year period. The first year of operation found a 31% increase in junior college transfers and the second year which is just now coming to a close saw a further increase of 12%. It is expected tht more adequate funding of state and federal student aid programs may make it unnecessary to continue the program beyond that initial period, or may allow it to continue at a lower level of funding.

(c) A sizeable grant to five metropolitan colleges has enabled them to develop cooperative programs in a number of areas, to provide full student exchange options between these institutions including bus transportation, and has enabled the institutions to effect economies by joint use of staff and

facilities. While this might have been economically desirable, apart from any foundation grant, it is highly improbable that it would have happened without the catalytic influence of such a grant.

The above are illustrative only and could be extended greatly.

II. THE EFFECT OF THE TAX REFORM ACT OF 1969 ON THE AVAILABILITY OF FOUNDATION SUPPORT FOR MINNESOTA'S PRIVATE COLLEGES.

Foundation support of these colleges has increased significantly since the 1969 Act was put into effect. The total volume of such grants for all purposes in the past thre years has been as follows: 1970–71, $4,070,399; 1971–72, $3,-409,049; 1972–73, $4,768,404.

While there have been some increases in the assets of local foundations due to estate settlement, there appears to be general agreement among foundation representatives as well as among the beneficiaries of foundation grants that the 1969 Act has encouraged the volume of such grants. It has also formalized the operation of some foundations enabling more orderly and effective processing of grants. Larger foundations have increased their staff and some of the smaller foundations have made arrangements for management which allowed them to get the benefit of others experienced in foundation programs. Fewer foundations operate "out of their back pocket." They have an address and staff who can be reached and who can provide guidance and counsel. A foundation which has a long-time record of generous support for a wide range of health nd educational projects acknowledges that it was encouraged to develop a specific "Independent Collegé Program" because it was put into the position of needing to dispense additional funds as a result of the 1969 Act. Under that program it has now dispensed $2,243,274 to sixty-nine colleges in a half dozen states.

Ten Minnesota foundations having a total of $457.8 million in assets had earnings in 1972 of $14,920,000 and paid out in grant $18,438,000, which is $3,518,000 above their earnings. I presume that the excess pay-out over earnings was influenced to some degree at least by 1969 Act requirements. They also paid a federal tax of $786,000. We could call to your attention, as others have done, that this amount was not available for distribution in grants, but your rejoinder could well be that this is offset several times over by the $3.5 million additional pay-out over earnings. Whether this additional pay-out is a threat to the long term stability of the foundations is a question to which I could not respond and which undoubtedly depends on a variety of factors, including the general economic picture.

We do not have data on the number of foundations in Minnesota which may have closed out their operations because they found it burdensome to comply with the 1969 requirements. We believe that this has been the case in some specific instances. Neither do we have a way of measuring the deterrent to the establishment of new foundations. If evidence develops that individuals are reluctant to establish general welfare foundations at a modest level we believe that institutions such as ours will suffer in the future.

III. HOW FOUNDATIONS COULD BE MORE HELPFUL

Foundations could be more helpful if there were more of them, if they could give away more money, and if they included institutions like mine more often.

From what I know about private colleges and from what I see around me I can find no reason to believe that the problems of the private sector are likely to diminish in the future. Given the rate of inflation our costs are not going to decrease even when enrollments drop. The unmet need in financial aid for students may diminish but it will not dsappear. The demands on public funds make t even more difficult for private colleges to get more than the most modest supplementary aid from federal and state governments. Although in Minnesota the private sector has maintained a modest level of growth in recent years and for the most part has been able to live wthin its available income, it has a very fragile stability. The sharp increase in fuel oil costs may very well have shifted a number of our institutions from the

black to the red; a modest drop in enrollment can do the same. It is extremely important that none of the sources of support be weakened or discouraged.

Foundatons have many different interests and this helps to safeguard the variety and diversity which characterizes American higher education, as well as other aspects of our culture. It would be most unfortunate if only a few large and powerful foundations were to dominate the philanthropic field. They tend inevitably to specialize in designated areas, since they cannot be all things to all men, and thus eliminate other valid and worthwhile concerns. Many foundations of diverse character, representing the interests of many different types of founders and donors and administered by persons of various interets, is the best safeguard against uniformity and standardization. It may also be the best assurance that relatively modest institutions with worthwhile goals will receive foundation support.

To the extent that provisions of the 1969 Act discouraged the creation of foundations we believe it should be looked at carefully to ee whether this cannot be corrected.

We would find it helpful if foundation interests were more easily identified. This need is being met to some extent by the information made available through The Foundation Center.

We believe that foundations will need to focus more of their resources on general support of the basic educational programs. There was a tendency nn the past to fund only the innovative and the distinctive, which sometimes turned out to be peripheral to the central purpose of the institution. There has been a wholesome shift in the last few years toward assisting colleges to improve their central and essential programs, such as teaching, admissions, matching alumni giving, and providing student aid. Foundations are showing a wholesome concern for the institution which sponsors the project, making sure that at the end of the grant period the institution will not have jeopardized its general program.

May I say, finally, that our concern for the welfare of foundations is only a part of a larger concern for the role of the private sector in American life. We share the opinion expressed by Mr. Alan Pifer, President of the Carnegie Foundation, before this subcommittee last October when he said, "The day has come when Government must encourage charity in every way it can, if the American system is to continue to embrace the traditional and well-proven concept of private initiative for the public good." Nothing is more characteristically American than the public-private sponsorship of programs and institutions designed to meet our common needs. Every individual contributes to that partnership and draws something from it. While we ought not deprive public agencies and institutions of the support which they need and which is largely provided from public tax funds, we ought not either deprive private agencies and institutions of the capacity or the will to provide for some part of the needs of our society. Therefore, I would urge the Subcommittee to exercise caution in its recommendations so that any changes made in the laws governing charitable gifts, including gifts that come from foundations, may result in the maximum benefit for all.

SUMMARY

Private colleges in Minnesota are very much dependent on foundation dollars, such dollars accounting for 28% of total gifts received. It is important to note that 61% of the foundation dollars were for current operations.

The Tax Reform Act of 1969 has been helpful to private colleges. The pay-out has been greater. But beyond pay-out, there are other benefits. We know who they are since they must file annual reports and these reports ar available. Their record of interests and awards clarify possibilities and probabilities. Staffing and procedures are now necesary and make for rational contacts, proposals and follow-through.

Additional benefits for private colleges (and other beneficiaries) could be achieved through even more extensive reporting of objectives, criteria, awards and results. Elitism, the healthy getting fat and the lean getting weaker, the rich getting richer and the poor getting poorer, and other possible perversions of public interest, are less a threat now than before the 1969 Act. Firm en-

courragement to long-term values in the public interest should be continued in the guidance of these vehicles called foundations.

Senator HARTKE. Our next witness is Karl R. Ross, president, the Myron Stratton Home.

Senator Dominick, delighted to have you. Are you going to testify or introduce somebody?

STATEMENT OF HON. PETER H. DOMINICK, A U.S. SENATOR FROM THE STATE OF COLORADO

Senator DOMINICK. Good morning, and I appreciate your courtesy in letting me appear. I want to introduce today a very good friend, Mr. Karl Ross, who is president of the Myron Stratton Home in Colorado Springs, Colo.

Karl for the past several years has been spearheading an effort to correct what appears to be a burdensome effect of the Tax Reform Act of 1969, namly, the treatment of the Stratton Home and other type homes across the country as private foundations, thereby including them under certain provisions of the act, which really threatens the very existence of those homes.

Now I have been working with Karl in an effort to come up with legislation which would mitigate this problem and be acceptable to the Senate Finance Committee and the Treasury Department. I introduced S. 3312 on April 4 of this year with the bipartisan support of eight co-sponsors, including Senator Bentsen of the Finance Committee, and I am sorry he isn't here today, to alleviate the situation, but the Treasury Department raised objections to certain provisions of that bill.

Through Karl's efforts these objections have been eliminated and the amended version of S. 3312, which I introduced as S. 3460, on May 9, does meet with the approval of the Treasury people, and I am hopeful it will be proved acceptable to the members of this subcommittee.

I know that Karl intends to explain the effects of the Tax Reform Act of 1969 on the Stratton Home and similar homes across the country, and I hope you will give favorable consideration to S. 3460 or similar legislation to remedy this problem.

Mr. Ross is here and I am sure he will go into this at detail, and I appreciate very much your courtesy in letting me appear and introduce him.

Senator HARTKE. Thank you. You have an excellent Senator here, Mr. Ross, who always goes out and does the best he can for his constituency. But his voice on the floor of the Senate is one of the more prominent ones, and we always appreciate his coming forward.

STATEMENT OF KARL R. ROSS, PRESIDENT, THE MYRON STRATTON HOME; ACCOMPANIED BY GEORGE HELM, COUNSEL

Mr. Ross. Mr. Chairman, as Senator Dominick has advised you, I am president and a trustee of the Myron Stratton Home in Colorado Springs, Colo. I would like to introduce also George Kelm of the firm of Hopkins, Sutter, Owen, Mulroy & Davis, in Chicago.

Senator HARTKE. Will you pull that microphone closer to you? It won't bite you and it will make it possible to hear you. I mean, it hasn't bitten anyone yet.

Mr. ROSS. As the Senator has advised you, I am here today to discuss with you a problem that has occurred under the Tax Reform Act and is what we feel an unintended application of that act to homes similar to the Myron Stratton Home. I would like, if I may, to give you a little bit of the history of the Home and I find that this history is not unique. Many of the other homes that are affected by the Tax Reform Act, which are listed on the statement, which has been filed with the subcommittee, have similar histories.

The Home is a foundation under the direction of the will of Winfield Scott Stratton, who was an early day gold miner in Colorado. He was a bachelor and wished to benefit needy people in the immediate area and throughout the State of Colorado.

Under the terms of his will, he left his residuary estate to three trustees and directed them to construct a home. He first instructed them to organize a charitable corporation and then to construct a home costing not less than $1 million for the purpose of taking care of people who because of age, youth, sickness, or other infirmity, were unable to earn a livelihood and were without other means of support.

The original trustees did build a home. It is located on a 110-acre campus. There are 26 cottages for the housing of the elderly and four large dormitories for the children.

We operate at a capacity of 168 people; 100 elderly people and 68 children.

The balance of the endowment coming out of the residuary estate was invested and the income therefrom has been used to operate and manage the home since its inception in 1909. During that period of time no solicitation has ever been made for funds from any party. No Government assistance of any nature, either Federal or otherwise has ever been asked for or received by the home. In other words, we are running this home solely through the income that has been generated by the endowment.

Now under the Tax Reform Act of 1969 we found ourselves in the same category as a private grant making foundation. We are subject to the 4-percent excise tax and also subject to the mandatory payout requirements under section 4942.

In our investigation of the problem we found that most homes in this field are completely exempt from the provisions of the act mainly because of church sponsorship, or in many instances, through public support. And interestingly enough, that public support oftentimes, particularly in the case of homes for the elderly, is generated by virtue of medicare-medicaid payments and other welfare payments from the various States.

Those homes are therefore completely exempt from provisions of the act under the 170 sections. Now, of course, we do not like the payment of the 4-percent excise tax. In the last 4 years this has amounted to over $100,000. But the section 4942 requirements are probably the most serious as applied to us and as applied to other homes like us. It requires a mandatory payout of a certain percentage

of the endowment each year. It bears no relation whatsoever to the amount of care we give or the amount of care that is required in the operation of the home. Basically the standard by which the amount of the endowment is paid out in each year is the caring for these 168 people and the constant battle to meet the inflationary spiral; the increased cost of that care, in other words.

A further problem is that the mandatory payout requirement fluctuates. As you well know, it is determined by the Secretary of the Treasury depending upon various factors in the economy. In any one year if the payout requirement is increased, it is almost impossible to expand your services in that one particular year to use up the required payout and the next year if the economy changes, I can assure you Senator, you cannot retract services that had once been expanded.

The third problem is the payout provision in essence requires an investment in high yielding, low growth securities. The only way homes of our nature can survive and continue to live off their endowment is if a portion of that endowment is invested in low-income producing growth securities to combat the continuing inflationary spiral.

So for those three reasons, Senator, section 4942 is a very difficult and burdensome problem to the homes, and actually threatens their very existence in the future.

We originally discussed this matter with Senator Allott several years ago and he made a very thorough investigation of other homes that might be affected by this same problem. Attached to my statement you will find a list of those homes. There are 25 in number. A very interesting part of it is that the bulk of these homes are over 50 years old and some of them even older than 100 years. They have been in business all these years and lived on their endowment and they have done a good job caring for people similar to those that we care for. They also are faced with the burdensome payment of the tax and the mandatory payout provisions.

At the last session of Congress, Senator Allott introduced a bill which amended section 170 of the statute. It would add a new provision under section 170 which would provide that an organization operating long-term care facilities of a residential nature for the care, comfort or maintenance of residents consisting of totally disabled, elderly persons, needy widows, or children, would be exempt from the provisions of the act.

Now this in and of itself—and this was felt in discussions with many of the staff members in Washington—left a rather large loophole in the act because it is conveivable that someone could buy an old house and install two elderly ladies and live under the guise of a long-term care facility, while in essence really being a grant making foundation.

As a result, a 3-percent test was put into the definition to make certain that a substantial commitment of the assets of the foundation would be committed to this program. So the further definition is that you not only have to provide long-term residential care for these different categories of people, but you must spend at least 3 percent

of your net investment or your endowment each year in the operation of the facility.

The bill was reintroduced in this session on the House side, and is House bill 2259. Senator Dominick sponsored the introduction of Senate bill 3312 with the various cosponsors.

The Treasury Department objected to the bill as written because of the fact that it left these organizations outside of the sanctions provided under section 4941 and section 4943, section 4944, and section 4945.

As a result, the new bill, 3460 and its companion bill in the House, which is 14467, has amended section 4942 to exempt organizations of this nature from its application, and has also provided under section 4940 that such organizations so exempted under 4942 are also exempted from the 4-percent excise tax. It leaves these organizations subject to the other section 4940 area sanctions that I have mentioned previously.

Concurrently through all of these proceedings over the last 2 or 3 years, the American Association of Homes for the Aging has taken an interest in the problem. They filed a statement in the hearings in the Ways and Means Committee on the bill a year ago and I understand they have supplied this subcommittee with a written statement for the hearings here today. AAHA, as they commonly call themselves, is an organization consisting solely of section 501 (c) (3) organizations. They are all devoted to the care of the elderly. There are about 1,300 members in it. The bulk of the members of AAHA are church supported and are therefore exempt, however, AAHA was very helpful in determining amongst their members, the ones that might be affected by this act and therefore are urging you to support it in its passage.

In conclusion, I would like to simply state that hopefully the subcommittee will consider seriously and favorably this legislation so that the services of these various homes, which these homes have carried out for many, many years, can continue uninterruptedly in the future.

Senator HARTKE. Senator Bartlett testified that he was interested in reducing the excise tax from 4 percent to 1 percent. Would that, in substance, correct part of the difficulty in your opinion?

Mr. Ross. Well certainly 1 percent is a lesser figure than 4 percent. The point I feel, Senator, that I am trying to make is this. The act itself was designed primarily, and I think very rightfully so, to make sure the grant making foundations finally got to work and dispensed charity for a change and put in the 4-percent excise tax as the measure by which—well, actually not the measure, as the method by which the Government could get enough money to police them and see that they did it.

If you consider a home of our nature though, and all of the legislation toward care for the aged and for children, it seems to me a little incongruous to turn around and say on a functional basis you should be charged to be policed, but then on the other side of the coin you appropriate millions of dollars during every session of Congress in the furtherance of care for the elderly.

Senator DOMINICK. Is it not true, Karl, that the excise tax is one part of the problem, but an additional problem is the degree of capital that you have to expend each year?

Mr. ROSS. Yes, section 4942 is probably the more serious problem than the tax, although I will say this, Senator, that some of the correspondence I saw from some of these other homes show the payment of the tax is really causing them difficulties. They are having to cut back their services because of the payments.

Senator HARTKE. You know, I hear what you say. The point of my questioning is this, and I mean without passing judgment, but the 4 percent is an audit tax for the purpose of auditing the foundations.

Mr. ROSS. Right.

Senator HARTKE. Now the amount of that audit expense, of course, if it is going to be strictly for audit purposes, ought to have a direct relationship to the actual cost of the audit and I quite agree with that. I mean, I don't think you ought to collect excise taxes simply from the viewpoint of collecting them under one guise and then using them for another. If you want to put an excise tax on and that is the judgment of the Congress, why that is a different matter.

Mr. ROSS. Sure.

Senator HARTKE. But the payout, let me ask you this. Why does not the payout, as far as you are concerned, satisfy the requirements simply by virtue of the fact that you are making the payout in the form of services? Are you not allowed to claim those?

Mr. ROSS. Oh, yes, we are allowed to claim services.

Senator HARTKE. And that still does not qualify you?

Mr. ROSS. No, Senator, we qualify under that. The point is it is the amount of the payout and the fact that it fluctuates up and down.

Senator HARTKE. Well, I understand that, but if the amount of the payout is at this moment an amount which is relatively small compared to present interest rates which could be available from any type of operation, I mean, you have high interest rates in the market today, which means you have in the market right now an inflationary factor. And I can see that you have this fluctuation, but it seems to me that the percentage of the total type of the payout would be the minimum——

Mr. ROSS. I see what you are saying and the point is, yes, sir, at this time while you can buy certificates of deposit for 10 percent and you can buy long-term bonds, which will run 8¼ percent. If we were to invest the bulk of our assets in such high-income investments and expand our operations, you see, the only way we can spend our money is on the operation of the Myron Stratton Home, and we can't give it away to other charities, and if we were to——

Senator HARTKE. But what happens to the accumulated surplus then? You are accumulating a surplus.

Mr. ROSS. Only basically through capital gains.

Senator HARTKE. Well, as I say, I hear your problem and it is not a unique one. It is the same one we had yesterday with the museums. And I am certainly interested in going into it, and I can understand that you feel there is a discrepancy concerning your operations as related to other types of similar operations which are not funded

through grants or through that type of operation but which are funded through church organizations or something like that, but I think that the purpose of these hearings, partly is to come forward with some type of uniform application. I can see all that, but at the same time I do feel that when you are going ahead and taking advantage—and I don't mean you when I say "you," but I mean the generic you—but whenever there is a tax subsidy to the extent that we have in the marketplace today, there ought to be some type of accountability, No. 1, and second, it ought to have some relationship to the total social value that is going on. And I am not in any way detracting from the social value that goes on, but there might be a question as to whether or not this is a social value which is presently commensurate with what is going on in the general social structure.

Mr. Ross. Well the answer I can give you is that—first, let me digress a little bit on your comment on museums. I think there is quite a distinction between these homes and a museum operation.

In a museum if the payout requirement is increased in any one year, they can go and buy another exhibit and just reduce next year. They don't next year buy the exhibit. But with a home of our nature, if we expand, if we construct another building and take in more people, we are committed to those people and the children, for instance, from the time they are 5 until they are educated and with the old people, for instance, for life, regardless of what the inflationary spiral may do to us. And this is a big danger in all of these homes and that is over expanding.

Senator HARTKE. Well, I am not talking about the normal operation of the home itself.

Mr. Ross. Right.

Senator HARTKE. There is a minimum payout requirement there. And I just don't know. I mean, I would be interested to go into these in detail, but anyway, it would appear to me that the minimum payout is low enough that some place along the line you ought to be able to qualify for that type of recognition, which would be within the framework of the legislation.

Mr. Ross. Well, the point is we felt the 3 percent is basically a legitimate test. The original bill was based on function, you know, is this a proper function so that you should be protected similar to a hospital——

Senator HARTKE. I hear what you say and understand what you say, and I understand your feelings, but I do feel in the totality of what we are talking about somebody has to ultimately come up and say something more than I feel we are doing a good job. I mean, you probably are. I know nothing about that to the contrary, but the point of it is, even though you feel you are doing a good job, is that sufficient to justify the amount of money which is presently being subsidized by the American taxpayers? And that is what it amounts to really.

And I think anyone who feels that the whole question of foundations shouldn't be gone into is ignoring the fact that somebody has to pick up the difference of the taxes which are not being paid by this type of utilization of capital.

Mr. Ross. Well, let me put it on another analogy, which I think is a good one. Suppose we were a profit organization and were permitted to deduct the cost of operation from our investment income. As far as the Myron Stratton Home is concerned, if that was the situation, I would be very happy. I would be very happy to give the Government 52 percent of whatever was left over after the care of these people. And this basically is the situation.

We are tax exempt, yes, on our investment income other than the excxise tax, but if you were to consider this a profit corporation and we subtracted our operating expenses, the amount of income tax would be infinitesimally small and——

Senator HARTKE. Well that is what I am interested in. I think it would be good if you could provide us some type of comparison along that line.

Mr. Ross. Be very happy to.

Senator HARTKE. What I am saying is, I don't mean to imply that all this should be changed. What I am saying very simply to you is I think it has to be explained in a little better context than at the present time.

Well, let me give you an example. In most places throughout the Nation the old county home was paid strictly—and the counties themselves incidentally participated in having a county home—and the county home started out and that was paid strictly by the taxpayers' money and there is no question about that.

And you could probably ask: Well where have all these people gone? Where are these homes? Well, in most cases they have ceased to exist. And they cease to exist very simply beause in the totality of using the tax money in the county they found that they were far more expensive and far more costly and too expensive to operate in relation to the tax value that they were getting. Now that is what we are talking about.

Mr. Ross. Right.

Senator HARTKE. And I don't think you can justify any operation for its continued existence simply on the virtue of the fact that it was here.

Mr. Ross. You mean, Senator, do homes of this nature have any real social value?

Senator HARTKE. I think it is not a question of whether they have real social value, but simply if they have to go ahead and justify themselves in the tax structure, because somebody else has to pay the taxes that they are not paying, then are they justified?

Mr. Ross. That was my point. If we were a profit home——

Senator HARTKE. I know what you are saying, but most people that are bearing the taxes out there now are the individual taxpayers. They are the people bearing the load. They are the people working for a living. In other words, normally they have no chance whatsoever in participating in these tax exempt operations. They will never be the recipients of any of these benefits.

Mr. Ross. I can only say this, Senator. We have no difficulty in finding applications for admissions.

Senator HARTKE. No, but that is not my point. I understand that. But I think you are going to find yourself hard to justify an existence simply on historical grounds unless you can show you are

performing a service commensurate with the tax value you are getting. In effect, you are receiving a tax subsidy. And you can say the fact is it wasn't originally set up for a tax subsidy, but it really is an avoidance of taxes, which is of course, strictly legal. And all I am saying is that I am raising a question of tax policy.

Senator DOMINICK. Mr. Chairman, may I interrupt here? Maybe I am off base, and probably I am because I don't pretend to be a tax expert, but here you've got a sum of money which has been left for a purpose which thereby relieves the taxpayer of having to take care of the people that are being taken care of. So the fact that there is no tax money coming into the home at all and that the taxpayers are being relieved of the burden of supporting these people, which they otherwise would have to take care of through their tax funds, has to be taken into account.

Mr. Ross. That is correct.

Senator HARTKE. Well I think that is a fair assumption. But what is the cost of that commensurate with the tax benefits that are flowing to that operation?

Senator DOMINICK. But it isn't tax money that is being used.

Senator HARTKE. Well, any capital in the marketplace is available for taxation, and so in that sense it is.

Well I understand the situation I think, but I do think it is in a similar vein as the museums, although maybe for a different reason, and also some of the private scholarship funds.

Thank you.

[The prepared statement of Karl R. Ross, with attachments, follows:]

STATEMENT OF KARL R. ROSS, PRESIDENT, THE MYRON STRATTON HOME, COLORADO SPRINGS, COLO.

Mr. Chairman and Members of the Subcommittee: I am appearing today on behalf of The Myron Stratton Home to call your attention to what I believe was an unintended application of certain of the provisions of the Tax Reform Act of 1969 to tax-exempt organizations which provide long-term residential care for permanently and totally disabled persons, elderly persons and children.

FOUNDING AND BACKGROUND OF THE HOME.

The Myron Stratton Home was founded in 1909 in accordance with instructions contained in the Last Will of Winfield Scott Stratton, an early-day miner, who died in 1902. Mr. Stratton's Will directed that his residuary estate be distributed to trustees named in his Will with the direction that they organibe a charitable corporation, expend $1,000,000 of the assets received by them for the construction of a Home in memory of his father Myron Stratton "for poor persons who are without means of support and who are physically unable by reason of old age, youth, sickness or other infirmity to earn a livelihood," and utilize the income from the balance of the assets received by them in operating the Home. The Will further set forth the manner in which applicants for residency were to be accepted, the type of securities in which the endowment should be invested, the method of establishing compensation for the trustees, and their accounting to the public of their administration of the endowment and the operation of the Home.

In accordance with these instructions the original trustees constructed a Home located on a 110 acre campus encompassing an infirmary, 26 cottages for the elderly, 4 large dormitories for children, and the usual activity and support buildings necessary in such an operation. The Home provides accommodations at capacity for 100 elderly people and 68 children. Applicants are accepted on the basis of priority of application from residents of the State of Colorado. The elderly are accepted for life and the children are

accepted at the age of 5 and are cared for and educated until graduation from high school, or college in the case of those showing academic promise. In accordance with Mr. Stratton's directions no charge is made for these services. In addition no governmental assistance has ever been requested or received, and no solicitation of donations from the public has ever been made. The operations have been financed solely from the income generated from endowment.

THE HOME IS CLASSIFIED AS A PRIVATE FOUNDATION

Under the Tax Reform Act of 1969, The Myron Stratton Home is classified as a private foundation, because it does not fall within the category of the so-called 50% organizations described in Section 170(b)(1)(A) of the Code and its investment income constitutes substantially all of its support. In this respect, The Myron Stratton Home is treated exactly the same as a grant-making private foundation notwithstanding that all of its funds must be expended for, and devoted to, the long-term care of its residents.

PROBLEM UNDER SECTION 4942

In addition to incurring a liability for approximately $100,000 of taxes imposed by Section 4940 of the Code on its net investment income over the past four years, a serious problem results from the application to The Myron Stratton Home of the provisions of Section 4942 of the Code, relating to minimum payout requirements. The requirement of the "minimum investment return," included as a part of Section 4942, was to insure that grant-making foundations distribute annually an amount which is not less than the amount that would be received as income if all of the foundations' investment assets were invested in income producing property at current prevailing interest rates. Although Section 4942 does not apply to organizations qualifying as private operating foundations, in order to qualify as an operating foundation an organization must normally expend directly for its operating purposes an amount equal to 85% of its adjusted net income and an amount equal to not less than 2/3rds of the "minimum investment return." This latter requirement, sometimes referred to as the "endowment test," does present problems in connection with the operation of The Myron Stratton Home and similar organizations.

The principal purpose of he "endowment test" is to insure that organizations seeking qualification as private operating foundations apply annually a significant amount of their assets directly in the performance of their exempt function. The required payout fluctuates from time to time, as it is set by the Secretary of the Treasury annually at a rate dependent upon the level of prevailing interest rates. In the case of certain types of operating foundations such as museums, libraries, literary societies and research organizations, the amount expended annually can more readily be adjusted upward or downward. In the case of organizations which have assumed the responsibility for the continuing care of persons who look to the organization as their sole source of support, it is difficult, if not impossible, arbitrarily to expand services and with a dip in the average return on investments curtail such services once expanded. While it is necessary perhaps to have some standard of minimum expenditure in relation to endowment for the proper differentiation of grant-making foundations from operating foundations, the standard in the case of long-term care institutions should be certain and not subject to annual fluctuations.

It is also apparent that organizations providing lifetime care for people who are dependent upon them should have a more substantial "cushion" in the amount of their endowment in relation to the amount of income produced therefrom, so as better to enable them to withstand the economic fluctuations which historically have occurred from time to time and further to combat the crushing burden of inflation. The minimum expenditure to satisfy the "endowment test" should, therefore, be low enough to permit investment in sound growth securities so as to meet these problems.

CONGRESS HAS SHOWN SPECIAL CONCERN FOR PROBLEMS OF THE AGING

The long-term care of elderly persons and children is a subject which has in recent years been of great concern to the Congress. Many federally sup-

ported programs now exist to assist in the care of the elderly. Included among these programs are medicare and subsidized mortgage assistance for construction of residential facilities. Indeed, there are few areas of higher domestic priority in the nation than the well-being of senior citizens.

MANY ORGANIZATIONS ARE EXEMPT FROM THE 4% ANNUAL EXCISE TAX DUE TO THE FUNCTION WHICH THEY SERVE

The Internal Revenue Code has long recognized that certain types of organizations of vital interest to the country deserve special recognition because of the function which they perform, without regard to the sources from which their support is derived. The list of such organizations includes churches, schools and universities, hospitals, medical research organizations and units of government. Of the many hundreds of homes for the elderly and children which exist in the United States, the overwhelming majority are operated or sponsored by churches, fraternal organizations and labor organizations. These organizations receive blanket exemption from private foundation status under the provisions of the Tax Reform Act of 1969 because of such sponsorship. All of these organizations are exempt from the rules relating to private foundations solely because of the function which they serve and the benefits which they confer in our society. Central to exemption from private foundation status is immunity from the 4% annual excise tax on net investment income imposed by Section 4940 of the Code. Very simply, our position is that organizations which operate facilities for the long-term care of elderly persons and children are equally important to society and should also be exempt from the 4% tax.

MANY HOMES OF LONG STANDING ARE TREATED IN THE SAME MANNER AS GRANT-MAKING PRIVATE FOUNDATIONS

There are a substantial number of organizations, similar to The Myron Stratton Home, caring for the elderly and children which are treated as private grant-making foundations simply because they are privately endowed and not sponsored by a church, fraternal organization or labor union.

Several years ago, Senator Allott of Colorado, recognized the problem confronting endowed homes for the elderly and sought to correct it in bills which he introduced in the 91st and 92nd Congresses.

Senator Allott's investigation of the problem, conducted by means of questionnaires submitted to a large number of organizations operating homes for the elderly and children (a summary of the answers to which are in the attachment to this statement), disclosed a significant number of privately endowed organizations whose status under the Tax Reform Act of 1969 was that of a private grant-making foundation. Senator Allott's concern was shared by Congressmen Brotzman, Betts, Burleson and Conable who introduced a companion bill in the House (H.R. 15350) in the 92nd Congress.

It is apparent from the summary of the questionnaires received by Senator Allott that most of the homes which are treated as private foundations have been in existence for over 50 years and that several of them have been in existence for over 100 years. Thus, many of these homes were established long before the existence of any federal income tax laws and were funded without regard to any tax benefits which their creators would hope to obtain. In general, these organizations are able to provide long-term care for their residents with a minimum amount of charges to residents or support from other persons and chiefly by use of income received from their endowment. Although it is always possible for these organizations to increase their charges to their residents or seek contributions from the general public to the point where their current support would meet the test of total exemption from private foundation status, this is certainly not a desirable result either from the standpoint of the residents or from the standpoint of providing the most care for the most persons at the least cost.

S. 3460 PROVIDES APPROPRIATE RELIEF

In an effort to provide legislative relief for organizations operating long-term care facilities for the elderly and for children, bills were introduced in both the Senate (S. 3312) and the House of Representatives (H.R. 2259) in the 92nd Congress which would have treated these organizations in the

same category as hospitals and medical research organizations described in Section 170(b)(1)(A)(iii) of the Code and would thereby have entirely removed these organizations from the category of private foundations. However, when asked to comment on H.R. 2259, the Treasury Department objected to the fact that such treatment would result in having these organizations exempt from the provisions of Section 4941 of the Code (relating to self-dealing), Section 4943 (relating to excess business holdings), Section 4944 (relating to jeopardy investments) and Section 4945 (relating to taxable expenditures). A copy of the comment letter of the Treasury Department on H.R. 2259 is attached to this statement.

In an effort to meet the objections of the Treasury Department, alternate bills were introduced in the Senate (S. 3460) and in the House of Representatives (H.R. 14467) which, I believe, provides the essential relief to organizations operating long-term care facilities, while maintaining the restraints against objectionable conduct of private foundations which Congress imposed in the Tax Reform Act of 1969. S. 3460 amends Section 4942 of the Code by exempting from the operation of that section an "organization operating long-term care facilities." An "organization operating long-term care facilities" is defined in the bill to mean a private foundation which during the taxable year operated and maintained as its principal purpose or function facilities for the long-term care, comfort, or maintenance of resident permanently and totally disabled persons, elderly persons, needy widows, or children, and which normally expends in the operation of its facilities each year an amount equal to or greater than 3% of the value of its investment assets. This latter requirement is to assure a substantial commitment of resources to the question of the long-term care facilities.

S. 3460 also amends Section 4940 of the Code to except organizations operating long-term care facilities from the 4% annual excise tax imposed upon the net investment income of the organization.

I understand that the Treasury Department has indicated that the proposed amendments set forth in S. 3460 satisfy the objections to the previous bill.

CONCLUSION

In summary, I respectfully urge the Subcommittee on Foundations to consider carefully the proposed amendments set forth in S. 3460, so as to insure that the future needs of elderly people and children who rely so heavily on organizations like The Myron Stratton Home for their long-term care will be met, and will remove the present jeopardy to the continuation of the vital services which they now provide.

DEPARTMENT OF THE TREASURY,
Washington, D.C.

Hon. WILBUR D. MILLS,
Chairman, Committee on Ways and Means,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your request for the views of the Treasury Department concerning H.R. 2259, entitled "A BILL To amend the Internal Revenue Code of 1954 with respect to certain charitable contribution."

H.R. 2259 would amend the Internal Revenue Code of 1954 to include certain long-term care facilities in section 170(b)(1)(A)(iii) organizations. Section 170(z)1)(A)(iii) presently includes only hospitals and medical research organizations. H.R. 2259 would add to this category only those long-term care facilities which on May 26, 1969, and continously thereafter have operated in a specified manner for the long-term care of the elderly, disabled, etc., and which normally make: "qualifying distributions (within the meaning of section 4942(g)(1) directly for the active conduct of such purposes of (sic) functions in an amount not less than 8 percent of the amount described in section 4942(e)(1)(A)."

Although H.R. 2259 is in the form of an amendment to section 170 and would therefore have the effect of making charitable contributions to long-term care facilities deductible up to 50 percent (instead of only 20 percent) of the individual donor's contribution base, its principal effect would be to

exempt completely these organizations from the private foundation provisions enacted in 1969. It is to this exemption from private foundation status that this report is primarily addressed.

Among the several private foundation provisions, we understand that those most pertinent to long-term care facilities are:

(i) The requirement in section 4942 that a private foundation distribute or expend a specified percentage of its investment assets or its entire adjusted net income, whichever is greater, and

(ii) The 4 percent tax on private foundation net investment income imposed by section 4940.

Since many such organizations must rely on their endowment to meet their long-term care commitments, too great a distribution requirement, plus the 4 percent tax, can impair an organization's ability to fulfill its long-term care commitments. Accordingly, relief from these two private foundation provisions, as distinguished from the other provisions applicable to private foundations, would be the principal benefit of H.R. 2259 to these organizations.

The Treasury Department recognizes the special needs of these organizations and the efficacy in many cases of stabilizing thei rminimum investment return and distribution requirements at a conservative, constant level, such as the 3 percent level contained in H.R. 2259. We have also consistently favored reduction or elimination of the 4 percent tax on net investment income for all private foundations. The case of homes for the aged is unique in that long-term commitments for care of people who may have no alternative means of self-support create a greater need for conservatism in the husbanding of long-term resources than would exist for other categories of charities, such as museums, libraries, or the like. Accordingly, our recognition of special needs in this case should not be construed to betoken any generalized willingness to look with favor on allowance of special exceptions to the current minimum distribution requirements.

Accordingly, we would not object to H.R. 2259 if it were modified to exclude long-term care facilities from only these two private foundation provisions, but we would favor general reconsideration of the 4 percent tax on net investment income. Also, we see no need to confine the proposed changes to organizations in existence on May 26, 1969.

We would, however, object to exemption of long-term care facilities from the other private foundation provisions, which H.R. 2259 would in its present form accomplish. These additional private foundation provisions are as follows:

1. The tax imposed by section 4941 on acts of self-dealing, such as sales between the organization and related persons;

2. The tax imposed by section 4943 on excess business holdings;

3. The tax imposed by section 4944 on the making of investments which jeopardize the charitable purpose of the organization; and,

4. The tax imposed by section 4945 on the making of certain taxable expenditures, such as payments for carrying on propaganda or attempting to influence an election.

These provisions should apply to organizations, such as long-term care facilities, that are not normally subject to public scrutiny either through broad public representation on a governing body or the necessity of obtaining broad support from the general public.

Moreover, we understand that these institutions receive few contributions, and here appears to be no reason or justification for increasing to 50 percent the deduction limitation for contributions to them.

For the reasons outlined above, the Treasury Department opposes enactment of H.R. 2259 unless it is modified as indicated.

If enacted, H.R. 2259 would result in an estimated revenue loss of not more than $5 million annually.

The Office of Management and Budget has advised the Treasury Department that there is no objection from the standpoint of the Administration's program to the presentation of this report.

Sincerely yours,

JOHN H. HALL,
Deputy Assistant Secretary.

SUMMARY OF RESPONSES TO QUESTIONNAIRES WITH RESPECT TO H.R. 2259

Name and address of organization	Date founded	Meet test of § 509(a)(2)(A)	Meet test of § 509(a)(2)(B)	Operating foundation	Full time residents	Investment income	Revenue from residents	Operating expenses	Market value of endowment	Operating expenses as a percentage of— Investment income	Endowment
1. Hendrick Home for Children, Abilene, Tex	1939	No	No	?	73	$416,177	None	$385,797	$9,524,472	93	4.05
2. Home for Homeless Women, Wilkes-Barre, Pa	1893	Yes	No	?	37	96,800	$6,000	102,500	2,127,497	106	4.82
3. Judson Palmer Home, Findlay, Ohio	1950	No	No	Yes		150,000		135,000	3,000,000	90	4.5
4. Myron Stratton Home, Colorado Springs, Colo	1909	No	No	No	117	438,628	None	475,232	14,450,000	108	3.29
5. Aged Women's Home of Georgetown, Washington, D.C.	1868	Yes	No	Yes	13	14,000	None	18,000	300,000	128	6.0
6. Heritage, San Francisco, Calif	1850	Yes	No	?	97	296,025	350,000	670,000	5,000,000	226	13.4
7. Warner Home, Jamestown, N.Y	1911	No?	No	?	17	36,063	27,444	69,000	709,000	191	9.73
8. Elizabeth Shoemaker Home, Washington, D.C	1952	Yes	No	Yes	21	66,757	25,271	97,810	1,296,000	146	7.55
9. Smith Memorial Home, New London, Conn	1881	No	No	?	15	61,987	16,033	116,202	793,068	187	14.65
10. Guyer Memorial Home, Peoria, Ill	1889	No	No	Yes	17	32,054	15,132	87,665	500,000	273	17.53
11. Sand Springs Home, Oklahoma City, Okla	1908	No	No	No	97	541,753	None	597,000	18,000,000	110	3.32
12. Miriam Osborn Home, Rye, N.Y	1908	No	No	Yes							
13. James Sutton Home, Wilkes-Barre, Pa	1920	No	No	Yes	15	32,000	20,000	52,000	590,000	162	8.81
14. Widows and Old Men's Home, Cincinnati, Ohio	1848	Yes	No	Yes	145	700,000	100,000	850,000	20,000,000	121	4.25
15. Amaza Stone House, Cleveland, Ohio	1877	Yes	No	?	54						
16. Lisner Home, Washington, D.C	1941	No	No	Yes							
17. Society for the Relief of Destitute Orphan Boys, New Orleans, La.	1820	No	No	?	30	134,385	3,431	110,546	3,000,000	82	3.68
18. State Street Children's Home, New Orleans, La.	1866	No	No	?	26	39,500	2,322	55,650	800,000	140	6.96
19. Mopr Children's Home, El Paso, Tex	1959	No	No	No	124	917,998	11,000	460,428	17,114,519	50	2.69
20. Andrew Freedmen Home, Bronx, N.Y	1924	Yes	No	Yes	74	293,000	203,000	697,000		237	
21. Rogerson House, Boston, Mass	1860	No	No	?	46	236,884	80,122	316,826	5,445,886	134	5.81
22. Marcus L. Ward Home, Maplewood, N.J	1921	?	No	Yes	90	413,377	204,613	741,962	4,413,122	179	16.8
23. Cartwell Home, Palestine, Tex	1953	Yes	No	Yes	58	164,232	90,397	213,880	3,207,227	130	6.66
24. Wales Home, Brockton, Mass	1893	?	No	No	15	55,722	20,565	84,789	1,262,800	152	6.71
25. St. Lukes Episcopal Church Home, Highland Park, Mich.	1861	Yes	No	?	64	207,956	196,866	401,474	3,734,233	193	10.73

Senator HARTKE. Our next witness is Joe G. Dempsey, executive director, Los Angeles Inter-Foundation Center. You may proceed.

STATEMENT OF JOE G. DEMPSEY, EXECUTIVE DIRECTOR, LOS ANGELES INTER-FOUNDATION CENTER

Mr. DEMPSEY. Good morning, Mr. Chairman. I am Joe G. Dempsey, executive director of the Los Angeles Inter-Foundation Center, which is an association of grant-making foundations in southern California with particular interest in the Los Angeles area.

I do appreciate the opportunity to testify before this subcommittee today. If I might, I will add to my summary remarks about the impact of the Tax Reform Act of 1969 with some comments on the pending employment pension plan legislation, H.R. 2.

Senator HARTKE. All of that will be in the record.

Mr. DEMPSEY. Just some comments as it might affect the near future of grant-making foundations.

Let me begin with some remarks on the impact of the Tax Reform Act of 1969. In my written statement I enumerated four provisions in the Tax Act that I observed to be adverse as well as beneficial and also the consequences of the provisions to the philanthropic enterprise of southern California. And in these remarks here this morning, Senator, I would like to briefly center my attention only on the consequences of the impact of the Tax Reform Act without making specific or detailed references to the provisions in the legislation itself.

As to an advantageous effect, at the outset let me say that I do observe some healthy consequences developing from the enactment of the Tax Reform Act of 1969. First the act has invoked some needed reforms; reforms acknowledged and fully understood by a large segment of the philanthropic community.

Second, and more particularly, the act has added valuable and necessary reflection as well as self-appraisal by the trustees and staffs as the fundamental purpose and direction, style and pace of their particular foundations.

Third, it has caused greater inter-foundation communication and cooperation, which has led to a significant number of foundations becoming a part of national, regional, state and municipal associations, such as the Los Angeles Inter-Foundation Center.

I have observed that there are some disadvantageous effects that I would like to talk about a little also. Although there has been healthy consequences, on the balance I do not believe the act can be judged altogether beneficial. Some of the important goals and objectives defined for accomplishment in the hearings previous to the enactment of the Trade Reform Act of 1969 were obtained but some were unobtained and in some instances inverted.

Let me enumerate some of those instances. I believe that less than an optimum amount of money is available to philanthropy today as provided in the minimum payout and the excise tax. Second, I think that perfunctory grants are encouraged by this act. Difficult problems, complex problems, are not being sufficiently engaged. This means there is a discouragement of distinctiveness. There is a

preoccupation with the minimum payout. Program restrictions tend to cause this and the expenditure responsibility characteristics of the act.

Third, there is an artificial standard of desirability that is being leaned upon for the sake of ease of administration to take on low-risk proposals, which translates into traditional and well-established and routine projects and programs. It avoids grants that have legislative implications. And foundations, Senator, are prone to steer clear of grants that might have legal, accounting or investment difficulties, which strangely enough preoccupies the attention of the foundations on these administrative problems, rather than looking into the serious problems of feasibility of a proposal or the need that it intends to meet.

The result of all this provides and establishes a kind of gamesmanship atmosphere, which is euphemistically called grants-menship. And I believe this to be a kind of unhealthy atmosphere.

Now, another aspect of this that I believe that is of a disadvantage to the act is that grant makers are being polarized. Activities of the foundations are becoming more conservative and grant makers are becoming more conservative. And there is an unhealthy vacuum in the center that Monsignor Baroni referred to yestrday.

Finally, fewer grant-making foundations are in existence because of this act, either through divesture or merger into public charities and fewer foundations are also being created.

Now let me turn my attention to the employment pension plan legislation as it affects foundations. Briefly, this pending legislation referred to as the pension reform bills, I understand that this legislation is now in conference and committee and I have informed the staff of this conference committee of the nature of my testimony. After I had submitted my written statement to this subcommittee, Commissioner Donald Alexander addressed a conference I attended recently on the subject of this legislation, Senator, and in no way did he relieve the apprehension I have about this bill.

Now, we have three basic criticisms of this legislation. First, we believe that it is incongruous to administratively link employment pension funds to all other exempt organizations. Second, the fundamental flaw of the present administration of regulations on foundations is still being located in the tax collector's office and we believe that this is not the correct place for it, which is to say that the success of that office cannot avoid the standard of the amount of taxes that are collected.

Finally, the unfortunate necessity of constructing a $70 million bureaucracy to administer and enforce regulations, we believe to be not in the best interests of either the country or foundations. This new and expensive agency is being recommended in the face of the IRS statment that 226,172 exempt organizations were audited over a 5-year cycle. Of that number, there were about 30,000 grant-making foundations and there was a subgroup of that of 102–200 special designated foundations that were submitted to a 2-year cycle of auditing. Seventy percent of those audited, according to Commissioner

Alexander, were of such a type and were in the type of grant-making activities that would not require that frequent an audit cycle.

The cost of these auditing practices in 1973 for all tax exempt organizations was $18.6 million. For the grant-making foundations that were audited, cost was $12.3 million. But the admitted decrease of 70 percent, which Commissioner Alexander alluded to in his presentation to the conference I attended, at a cost of $18.6 million and using the revenues of the 4 percent excise tax generated from investment incomes of foundations, who I remind you the cost was $12.3 million. this legislation proposes that the cost of the administration and enforcement will rise to almost double the present cost, $35 million.

In his statement, Commissioner Alexander said that this new agency will seek to provide and to improve these five areas: the auditing practices; regulation enforcement; uniform treatment; direct access to the tax court; and increased understanding.

And except for the understanding that he mentioned and the tax court access, we really don't see too much room for improvement. We are not all that sure that the tax court access and increased understanding is worth $14.4 million.

Finally, I appreciate being invited to give this testimony and I would welcome any questions or comments that you have, Mr. Chairman.

Senator HARTKE. I want to thank you for some very valuable suggestions and I would hope that maybe we could have more organizations similar to yours give us some constructive suggestions, which you have given us today.

I do think when we get that paper work, that we are going to have to try to figure out what we can do to cut down on it. We especially want to cut down on the paper work for the smaller foundations. I am not interested in simply destroying them in the name of trying to create more bureaucracy.

Well, thank you very much.

Mr. DEMPSEY. Thank you.

[The prepared statement of Joe G. Dempsey follows:]

STATEMENT BY JOE G. DEMPSEY, EXECUTIVE DIRECTOR OF THE LOS ANGELES INTER-FOUNDATION CENTER

INTRODUCTION

Mr. Chairman, I am Joe G. Dempsey, Executive Director of the Los Angeles Inter-Foundation Center (LAIFC). LAIFC is an asociation of grantmaking foundations active in Southern California, particularly in the Los Angeles metropolitan area. This asociation provides the means by which philanthropy in this area can be more effectively served through communication and co-operation between foundations.

I appreciate this opportunity to testify before this Sub-Committee today. If I might, I would like to confine my remarks to these subjects: some of the ways that I observe the Tax Reform Act of 1969 (TRA '69) is impacting foundations in the Southern California region and, secondly, I would like to comment on some pending legislation, characterized as HR 2/HR 4200 and presently in conference, that will, if passed in its present form, have a significant impact on philanthropy in the future.

OBSERVATIONS OF THE IMPACT OF TRA 1969 ON SOUTHERN CALIFORNIA FOUNDATIONS

Let me say at the outset that TRA '69 had been a tolerable, if difficult and uncomfortable piece of legislation for foundations. Complaints are numerous, to be sure, but even the most vocal critics will acknowledge some usefulness and need for some of the reforms this Act invokes. From my personal viewpoint, TRA '69 has required some valuable reflection and review by foundations that have produced more than a few salutary effects.

But, of course, the law has also had its negative effects. It has been expensive, and in more than a few cases, debilitating for charity. Clarification of the law through regulations and interpretations has been slow, sometimes confusing and almost always aggravating. Too often, grants are being considered as much on the legal reliability and requirements as on feasibility and impact to meet a crucial need. The net result has been to increase the number of "safe and sure" grants, making the traditional grant recipient the major benefactor of TRA '69.

MINIMUM PAYOUT PROVISION

The short term effects of this provision appear to be advantageous for the grantseekers. But it has come to my attention that at least one study shows that the consequences of this provision over the longer term are questionable. LAIFC is proposing a similar study of foundation investments in Southern California to test the overall benefits to charity if this provision had been applied over the past ten years. When this is done, your subcommittee will be provided the results. For now, we are dubious about the long range advantages that this provision will provide.

More immediately, I observe that this provision diverts the energies of Trustees, especially of smaller foundations, from the important job of evaluating proposals. Too much Trustee time is being channeled into a guessing game with the stock market. The results of this? Perfunctory grant practices, to the detriment of innovative program proposals. By focusing attention on investments, many grant opportunities are being overlooked.

TAX INVESTMENT INCOME

It seems apparent to me that the 4% Excise Tax was a good idea gone awry. That the administrative expense of auditing and monitoring activities of private philanthropy be borne by foundations is generally accepted. Two criticisms are most often leveled: (1) The 4% of net investment income is more than is needed; and (2) Investment income is a poor index by which to measure the cost of enforcement.

A percentage of the asset value that would generate revenues sufficient to meet the costs of auditing would seem more reasonable to me. And, to be straightforward, I believe that it is important to identify such a revenue source for what it is: an audit fee, not an excise tax.

I need not go into who bears the burden of this tax. You are well aware of the fact that charity suffers, not foundations.

PROGRAM RESTRICTIONS

It is my observation that this provision has minimized direct scholarship grants. They are to difficult to administer. Colleges and Universities are being given this responsibility. And one of the most obvious results is the decreasing number of student hardship scholarships being funded. My personal view is that by assigning this responsibility to academic administrators, a valuable contact between the private sector and young people is being unfortunately lost.

Another adverse affect of the Program Restrictions has been frustrating the attempts of my office to relate private philanthropy to city government. Working from the principle that both of these institutions have a common interest in some of the crucial needs of the city, exploratory meetings have been arranged to bring together foundation representatives and Mayor Bradley. In every instance, the threat of "Program Restrictions" has caused timidity, and sometimes withdrawal of a foundation official from this worthwhile con-

sultation. This provision has the tendency to drive the public and private sector apart in those areas where communication and coordination is urgently needed.

EXPENDITURES RESPONSIBILITY

With others, I believe the effects of this provision deserve substantial criticism. There is a general agreement among Trustees of foundations that proposals which require Expenditure Responsibility are less desirable than those which do not. Public charities are the most obvious benefactors of this inclination of Trustees. Those who are adversely affected are, of course, the grantseekers with new and untried proposals. The dilemma reappears: How to asure responsibility without stifling the courageous grantmaker. Surely this is not impossible. Difficult perhaps, but it must not be impossible. But another ingredient has been produced, namely, the grantsmanship phenomena. Professional grantsmen who write books, articles, and conduct seminars have made a mass invasion.

Now, to be sure, commenting on and teaching grant seekers how and where to look for grants is not an evil in itself. My objection is that the underlying philosophy of this activity is "gamesmanship." By making a game out of philanthropy, the purposes that all of us here seek are degraded and dangerous aberations appear. It is as though the "five-percenter" of the war days was revisiting us with a new title: The Professional Grantsman.

But, more to the practical point, the results of this provision are fairly predictable:

1. Routine, status quo grants are encouraged;
2. Activist foundations are generally unaffected;
3. More conservative foundations are being pushed to be even more conservative;
4. An unhealthy vacuum is being formed between the active and conservative grantmakers;
5. The principal victim of this situation is the well-grounded and effective community organization that previously found its support from the middle range or moderate grantmakers;
6. In Los Angeles, National Foundations are attempting to fill this vacuum by making grants almost triple the amount made by local foundations;
7. A cruel expedient called the "clearing house" has been created that can, and has, blackballed qualified proposals on the basis of Expenditure Responsibility.

To summarize concerning this aspect of TRA '69, I doubt if many will quarrel about the reasonableness of monitoring and evaluating the way grant recipients expend their funding. Prudence dictates as much. But the overriding effect that I see in Expenditure Responsibility is, first, paperwork is exhausting staff energies, and second, the anxieties of Trustees and Managers over government sanctions is producing a profound reluctance to make grants for proposals that require Expenditure Responsibility.

CONCLUSION

The IRS is furnishing this Subcommittee statistics on the creation and termination of foundations. I will be surprised if these statistics do not reveal a significant decrease in the number of foundations, if not the grant capacities of foundations, especially in the range of smaller foundations. The reasons should be clear: only those foundations will survive the jurisdiction of the Tax Reform Act of 1969 who can have the constant counsel of lawyers, who can command the expensive attentions of accountants, and who can afford the expert advice of investment counselors.

For the rest, I believe three options are available:

1. Foundations which cannot afford these services join together to share such expenses and, in associations such as the one I represent, cooperate and coordinate their grant activities with other foundations;
2. Merge their corpus with a Public Charity, or
3. Go out of existence by divestiture.

COMMENTS ON HR 2/HR 4200

Now, let me turn my attention very briefly to the pending legislation referred to as the Pension Reform Bills. It is my understanding that this legislation is now in conference with the Joint Internal Revenue Taxation Committee and I have informed the staff of this conference committee of the nature of my testimony on this legislation.

A committee on legislation representing Los Angeles foundations has voiced several criticisms of these Bills that I would like to bring to your attention. Since the Finance Committee has considered this Bill, I will not burden you with a description of that part affecting foundations. Let me only make these points:

1. We fail to see the logic of coupling, administratively, Employee Pension Plans with private philanthropy. We foresee in this incongruity more problems than resolutions for the philanthropic enterprise.

2. We are extremely dubious over the value of creating a $35 million bureaucracy to do the work that IRS is presently spending under $19 million to do. Surely, you can understand the apprehensiveness of foundation officials when they learn that a government supervisory agency is going to double its size.

3. We understood one of the primary motivations behand this legislation was to remove the punitive principle of "tax collector" from the agency supervising philanthropy. We see little in this legislation that will remove this debilitation.

If further legislation is needed, let it enhance and embolden rather than punish and confound philanthropy. I commend to you the suggestions Alan Pifer and Sheldon Cohen made in their testimony before this Subcommittee in October of 1973. When legislation incorporates these suggestions to affirm, strengthen, encourage, and build public confidence in the philanthropic endeavors that seek to accomplish the "public good," we will both applaud and support it.

Senator HARTKE. Our next witness is Mr. Philip Wain, President, the Wain Foundation.

Good morning, sir, and madam.

STATEMENT OF PHILIP WAIN, PRESIDENT, THE WAIN FOUNDATION; ACCOMPANIED BY MRS. PHILIP WAIN, SECRETARY

Mr. WAIN. Would you permit me, Mr. Chairman, to introduce Mrs. Philip Wain, who is the secretary of the Wain Foundation. I must also confess that I invited her to accompany me here for another reason, which was perhaps rather selfish, namely, because I recognize that the chairman of this subcommittee is the Senator from Indiana, I thought it might be helpful if I had my wife here, who is also a Hoosier having been brought up most of her life in the State of Indiana. I bring her here to help me in this presentation, at least by psychological support.

Senator HARTKE. Now, you will have to pull that microphone up to you so we can hear you.

Mr. WAIN. Can you hear me now?

Senator HARTKE. Can you all hear him back in the room? Okay, fine, that is better.

Mr. WAIN. This hearing exemplifies the democratic process in action.

I, Philip Wain, the creator and manager of probably one of the smallest private foundations in existence, am permitted to appear before this august body to present my views under the same rules

that govern the appearance of the Ford Foundation. When my parents fleeing the pogroms and persecution of Jews in czarist Russia brought me to this country at the age of 4½ years, did their dreams of the U.S.A. encompass this possibility? Not in particular perhaps, but in principle, yes.

In the light of the same democratic process, I urge you to allow the pluralism, the openness, the varied points of view which characterize our democracy to be uppermost in your mind and heart as you consider the private foundations.

I attempt through the Wain Foundation to support those causes which raise the quality of life by feeding the human spirit.

In my most pretentious moments, I imagine myself to be in pursuit of wisdom. But, I confess, no greater truth in my concept of "quality of life" nor in my concept of "food for the human spirit" than in the concept of other individuals or other foundations public or private. And this brings me to the principal reason for my appearance before you.

I urge that all individuals and all foundations, public and private, continue to exercise the widest possible freedom of personal expression in their charitable gifts and deeds for public benefit.

The modesty and humility exemplified by this committee in inviting our views is the best possible start toward a better understanding of this complex creature we call a human being and gives me the temerity to make a few suggestions.

One, encourage the formation and continuation of private foundations. Limitation of individual contributions to private foundations to 20 percent of adjusted gross income versus 50 percent limitation to public foundations discriminates against private foundations.

Every public foundation is an outgrowth of the efforts of individuals and private foundations. All are an expression of the broad spectrum of human opinions, convictions, motivations, which constitute the strength of our society.

I and everyone associated with the Wain Foundation give our services free of charge. The human drives—including ego—which lead to formation of private foundations release material resources and human efforts and compassion in the service of the public good.

Two, the 4 percent excise tax won't kill foundations, but equity would call for its reduction to actual cost of assuring compliance with law and regulations and perhaps changing the title from "tax" to "fee."

Three, the concept of a "minimum rate of investment income" is good, but a greater incentive to exceed that minimum is required, particularly for the smaller private foundations. I suggest that allowing deferral of distribution of income exceeding the minimum rate for an additional number of years would be a wholesome incentive.

You have invited "comment on the way the Internal Revenue Service administers the tax laws pertaining to private foundations."

The Wain Foundation was audited by the Internal Revenue Service quite shortly after the enactment of the 1969 Tax Reform Act.

The Internal Revenue agent who made the audit displayed an understanding of the laws and regulations to a degree that I considered remarkable in view of the short time elapsed since the enactment of the act and the state of flux of the regulations.

I also had occasion to ask for an opinion of the Los Angeles office of the Internal Revenue Service and was again impressed with the promptness and competence of the reply.

You have also invited "comment on the way the Tax Reform Act of 1969 has affected the ability of foundations to serve grantees."

I conferred with other private foundations after the enactment of the act. I received the impression that they were frozen by fright into almost complete inability to act on any but the most traditional requests for grants. This gradually melted as interpretations and regulations were issued.

I fancy myself to be a maverick, so I considered myself free of this "chill." However, I must confess that in preparing the Wain Foundation Federal form 990–P.F. for calendar year 1973, I reviewed the schedule of contributions, that I reported on that form. Now, I am going to share a thought that occurred to me and I hope it is only my imagination, but it seems to me that list was less innovative than in past years.

Perhaps it may prove that even I need some assurance from you that you don't dislike private foundations and even love us.

Respectfully submitted.

Senator HARTKE. All right, we love you.

Now, let me ask you what do you support generally?

Mr. WAIN. Well, I find for the most part we support colleges; things having to do with education. I can give you some illustrations if you wish?

Senator HARTKE. I just wondered generally.

Mr. WAIN. Examples would be the University of Chicago, Clarmont Men's College, private colleges, mentioned here by many others, the Center for the Study of Democratic Institutions, the Council on Religion and International Affairs, and so on. We support the kind of things that I in hope my own opinion, do something more than merely add to the quantity of life, but really add something to sustain and add to the quality of life. It is the long-term view.

This is made more difficult under the grant-making provisions for private foundations because, as several of the witnesses have indicated, these provisions encourage a tendency, and it is one from which I am not entirely free either, that once we become accustomed to something, it seems natural and something to which we are not accustomed seems unnatural. Instead, grant-making provisions for private foundations should encourage support for innovative endeavors.

Senator HARTKE. I do thank you for coming here. We will give your testimony consideration.

The final witness is Mr. Rollin N. Hadley, director, Isabella Stewart Gardner Museum, representing the Association of Art Museum Directors.

First you want to pull that mike up to you because the mike will not work unless you have it right in front of you.

You may proceed.

STATEMENT OF ROLLIN VAN N. HADLEY, DIRECTOR, ISABELLA STEWARD GARDNER MUSEUM

Mr. HADLEY. My name is Rollin van N. Hadley, and I am director of the Isabella Steward Gardner Museum in Boston. I am here on behalf of the Association of Art Museum Directors, consisting of directors from 84 of the country's leading art museums.

Beside me here today is Mr. Kenneth H. Liles, who is counsel.

My testimony concerns the provisions of the Tax Reform Act of 1969 which impose a 4 percent excise tax on the investment income of certain art museums, for example, the Clark Art Institute in Williamstown, Mass., the Frick Collection in New York City, Winterthur in Wimlington, Del., and my own museum, the Gardner Museum in Boston.

Museums such as these, because they are wholly or mostly supported by private endowments, are taxed as foundations under the Tax Reform Act. However, they offer cultural and educational services to the public of the same kind and quality as museums that depend on public contributions for their support, such as the Metropolitan Museum in New York and the Museum of Fine Arts in Boston.

We believe it is inequitable and contrary to public interest to require the endowed museums to pay a tax on their investment income. I am here to urge on behalf of the association that the situation be remedied by corrective legislation.

Although I appear on behalf of the association, I believe I can best illustrate our position by using as an example the situation of the museum I know best, the Isabella Stewart Gardner Museum, of which I am director.

Mrs. Gardner herself assembled the remarkable and internationally known collection, and she built a striking building to house the collection as a museum in the style of a 15th century Venetian palace.

When she died in 1924, she left the museum and the collection to the trustees under her will—seven distinguished businessmen and scholars who were not related to her—and she also left them an endowment for the support of the museum.

Mrs. Gardner's original trustees now have been succeeded by a charitable corporation managed by seven trustees who are a retired businessman, an investment advisor, a professor of music, a professor of classics, an architect, a lawyer, and the Republican floor leader of the Massachusetts House of Representatives.

It is obvious that Mrs. Gardner, in establishing and endowing her museum, had not thought of seeking any of the improper tax advantages at which the Tax Reform Act is aimed. Her sole purpose was to create a marvelous and unique cultural and educational resource for the benefit of the public.

I hope I may be excused for saying, as the present director of her museum, that she succeeded brilliantly in doing so. I invite the members of this committee, when visiting Boston, to see the collection of paintings and other objects of art, the lofty Venetian courtyard banked with flowers, and to hear one of our concerts of classical music.

The endowment Mrs. Gardner gave has been well managed, and so far it has been sufficient to pay for the operation of the museum without having to seek support from the public. However, as with most endowed institutions, our investment income has not kept pace with inflation, and we are inevitably approaching the day when our expenses will exceed our income.

Unfortunately that day will be considerably accelerated by the tax on our investment income imposed under the Tax Reform Act. Beginning in 1970, we have had to provide for taxes of about $25,000 a year out of an income of $600,000, and if the law is not changed, that tax will continue even when we are operating at a deficit.

To compensate for the tax, we will be forced either to curtail services to the public, or to seek public support in competition with other museums and charities, inevitably to their detriment. We do not believe this is in the public interest.

As I understand it, the purpose of the excise tax on foundation income is to pay the expenses of administering the reform measures aimed at foundations in the Tax Reform Act.

Educational institutions and musums supported by contributions from the public are not required to pay the tax, presumably because such institutions have not created the abuses that are the subject of the foundation provisions in the act.

I submit that it is just as inappropriate to extract such a tax from similar museums just because they happen to have been privately endowed.

I am not a lawyer and I shall not attempt to describe in detail the corrective measures that we recommend. These are described in the written statement I have submitted to the committee. I should emphasize, however, that these corrective measures contain safeguards which, for example, should prevent a foundation from escaping the tax by merely posing as a museum.

I appreciate very much the privilege of appearing before your committee.

Senator HARTKE. This is the same problem that we have been discussing here and really discussed yesterday with other museums.

Mr. HADLEY. Essentially the same problem that Kyran McGrath brought up yesterday.

Senator HARTKE. Well, we will certainly give this our sincere consideration. We appreciate your testimony and we understand the problem, but do not necessarily understand the solution.

Mr. LILES. Well, I would say, if I may, sir, on the solution, not that we disagree with Mr. McGrath and if you wanted to take his proposal that would be fine with us, but we believe that we presented a narrower approach.

Senator HARTKE. A narrower approach?

Mr. LILES. Our approach goes to the technical problem that we are mainly concerned with, which is the 4-percent tax, rather than trying to write a provision which would exempt all museums from all provisions of the foundation rules. The only one we are aiming our proposal at is the 4-percent tax, which is the main concern we have. And, in doing that we have tried to work with the staffs to narrowly define what we are talking about, so as to not go beyond what is needed to accomplish it.

Thank you.

Senator HARTKE. All right, fine. I understand and appreciate that.

[Mr. Hadley's prepared statement and subsequent relative communications follow:]

STATEMENT ON BEHALF OF THE ASSOCIATION OF ART MUSEUM DIRECTORS

My name is Rollin N. Hadley. I am Director of the Isabella Stewart Gardner Museum, of Boston, Massachusetts. I am appearing today on behalf of the Association of Art Museum Directors (the Association), of which I am a long time member. The Association consists of representatives from 84 of the leading art museums of the country. As a group, the Association's members are vitally concerned about the way the Tax Reform Act of 1969 the 1969 Act), as interpreted by the Treasury Department in its revised regulations, discriminates against certain art museums by treating them as private "operating foundations" rather than as "publicly supported" organizations. As a result of being relegated to private operating foundation status, the art museums concerned are subjected to certain inequities, the most serious being the imposition of the four percent excise tax on their investment income. This in turn adversely affects their ability to carry out their exempt function of educating the public. Legislatve relief is needed.

1. THE PROBLEM

The difficulty with which we are concerned arose because the Treasury Department, after the enactment of the 1969 Act, revised its regulations defining publicly supported organizations (under section 170(b)(1)(A)(vi) of the Internal Revenue Code) to require that a museum normally receive at least 10 percent of its support from the general public before it can be considered as qualifying under the "facts and circumstances" test as a publicly supported organization. While many museums meet this 10 percent test, a significant number cannot do so, including some of the most outstanding art museums of our country. Examples of well-known art museums which face this problem are the Clark Art Institute in Williamstown, Massachusetts, the Frick Collection in New York City, the Winterthur in Wilmington, Delaware, and the Gardner Museum in Boston.

I might say that this change in the regulations was made even though there was no change by Congress in the statutory language of the pertinent provision, section 170(b)(1)(A)(vi) of the Code. Thus, a number of art museums which had assumed they would not be treated as private foundations found they were in fact so classified by the Treasury even though no change in the statutory definition on which they had relied was made by the Congress.

Generally, the museums facing this problem were established many years ago, usually by wealthy donors who left them substantial endowments designed to meet their anticipated future needs. Over the years, control of these museums has passed beyond the families of the principal donors so that today their governing bodies are broadly representative of the interests of the general public.

Since the above-listed museums provide the same kind of museum services directly for the benefit of the public as do the museums which Treasury treats

as publicly supported, such as the Metropolitan Museum in New York City and the Boston Museum of Fine Arts, to name but two, the Association sincerely questions the wisdom of subjecting these endowed museums to the penalty of the four percent private foundation excise tax and to the other disadvantages of private foundation status, to which publicly supported museums are not subject.

The Gardner Museum offers an example of how the four percent excise tax, when applied to museums, can work against the interests of the public. The Museum is in the style of a 15th Century Venetian palace, a striking setting for its internationally famous art collection. It receives about 200,000 visitors a year without charge for admission. Special tours by school groups are encouraged, including groups from the Boston Public Schools. Concerts of classical music are offered each week to the public free of charge. So far, the Museums has not had to seek public support because it was substantially endowed by Mrs. Gardner and its endowment income has generally been sufficient to meet operating expenses. However, with rising costs, it is probable that income will not continue to be sufficient to meet expenses and pay the four percent excise tax. It seems inevitable that the four percent tax will do a disservice to the public by causing, for example, curtailment of services, the imposition of an admission charge, or requests for public support in competition with other charitable organizations.

The Association firmly believes it is inequitable to differentiate for tax purposes between museums which are treated as publicly supported and those which were fortunate enough to be richly endowed and thus are not heavily dependent upon public support. Essentially, we believe, the test should be based on *services rendered* to the public rather than on the source of funds so used. Application of the four percent excise tax necessarily reduces the funds available to the privately endowed museums to continue to provide their public services, thereby defeating the public's interest.

2. PROPOSED LEGISLATIVE REMEDY

To remedy this situation, Representative Koch of New York, on January 3, 1973, introduced H.R. 704, the provisions of which would exempt from the four percent excise tax imposed by section 4940, added to the Code by the 1969 Act, "any private foundation which is organized and operated exclusively as a library or museum furnishing facilities or services directly to the public." The Association presented last year detailed testimony before the House Ways and Means Committee on H.R. 704, and later proposed to the House Committee modifications to the Bill, mainly designed to require stricter standards for exemption from the tax. As so modified, the Bill would add a new subsection (d) to section 4940 of the Code, reading substantially as follows:

"(d) *Exemption for Libraries and Museums.*—Subsection (a) shall not apply to any operating foundation (as defined in section 4942(j)(3)) which is organized and operated primarily as a library or museum furnishing facilities or services directly to the public and which is not controlled directly or indirectly by one or more substantial contributors (as defined in section 507(d)) or any member of the family of a substantial contributor (as defined in section 4946(d))."

3. OUTLINE OF REASONS FOR AMENDMENT

Mr. Charles van Ravenswaay, Director of Winterthur, in his statement last year to the House Committee on behalf of the Association, made essentially the following points in support of the enactment of H.R. 704. (See Public Hearings on General Tax Reform, Committee on Ways & Means, 93d Cong., 1st Sess., Part 15, pp. 6097-6105.)

(a) In contrast to the great European museums, which are state owned and supported, most American museums have been and are dependent on philanthropy for their support.

(b) In recent years, however, the Congress, and Federal and state governmental agencies have come to recognize that our museums perform important educational and cultural functions on a large scale, and to recognize that

museums should expand their public services and should receive public support to make this possible.

(c) Imposing an excise tax on the income of endowned museums is directly contrary to the public interest, which is to have museums expand their facilities and services. The effect of the tax is to curtail their functions.

(d) The functions of museums are closely akin to and interrelated with the educational activities of schools and colleges, which are exempted from being classified as "private foundations."

(e) Since endowed museums offer public services and benefits of the same kind as museums which are not taxed as private foundations, it is inequitable to tax the endowed museums just because they happen to be supported by endowment income.

The endowed museums are not the kind of foundations which gave rise to the abuses envisaged by the 1969 Act. The Clark Art Institute, the Frick Collection, the Gardner Museum, Winterthur, and others like them were founded as collections for the educational and cultural benefit of the public and clearly not as a means for misusing the income tax laws for private benefit through self-dealing, retaining control of a family corporation, improperly accumulating income, and the like. There is no need for "reforms" where such institutions are concerned, and it seems particularly inappropriate to penalize them with an excise tax to pay for enforcing the law aimed at abuses these institutions have had nothing to do with.

It is necessary, of course, to distinguish between institutions which genuinely are conducted as museums, and foundations not conducted *primarily* for such purposes, but which might call themselves museums in order to secure exemption from the excise tax. The proposed amendment would limit the exemption to genuine museums. In order to be exempt from the tax, a museum (or library) would have to meet the tests for an "operating foundation," so no foundation not expending substantially all of its income for museum or library purposes could qualify for the exemption. Furthermore, the requirement that the museum not be controlled by substantial contributors or their families would serve to prevent the use of the museum's resources for a private purpose and ensure a governing body which would represent the interests of the public.

The proposed amendment would exempt museums only from the four percent excise tax and not from the other provisions of the Tax Reform Act concerning foundations, which penalize abuses such as self-dealing, failure to distribute income, improper investments, and political expenditures.

4. OTHER RECOMMENDATIONS

In addition to the above amendments to Mr. Koch's bill, consideration should be given to the following related matters.

(a) *Amend section 4945 to relieve private foundation grantors from "expenditure responsibility" with respect to grants to operating foundations of the type described in the foregoing amendment.*—The presence of the "expenditure responsibility" requirement discourages some private foundations from supporting museums which fail to meet the 10 percent public support requirement which in turn hinders their meeting such requirement. No good purpose is served in applying such a restriction against grants by private foundations to museums which qualify as operating foundations and as publicly controlled.

(b) *Restortion of charitable contribution deduction for donor-artists.*—The Association has gone on record as supporting the enactment of legislation which will provide a Federal income tax charitable contribution deduction for the fair market value of donor-created works of art that are given to museums or other charitable organizations for a use related to the donee's exempt purpose or function.

In this connection, it is noted that Mr. Mills' bill (H.R. 3152, relating to contributions of donor-created works of art), permits deduction of one-half of the unrealized appreciation and covers only gifts to organizations qualifying under section 170(b)(1)(A)(ii) (a school), (v) (a governmental unit), or (vi) (a publicly supported organization). The Association favors restoration

of the full deduction for contributions of original works by artists to museums. Moreover, since no distinction in the present law is made as to gifts by individuals to museums which qualify as publicly supported organizations under section 509(a)(2) or (3), rather than under section 170(b)(1)(A)(vi), or as "operating foundations" under section 4942(j)(3), there is no reason for drawing such a distinction here between publicly supported museums which qualify under section 170(b)(1)(A)(vi) and those which otherwise qualify as public charities or as operating foundations.

THE HENRY FRANCIS DUPONT WINTERTHUR MUSEUM,
Winterthur, Del., June 11, 1974.

HON. VANCE HARTKE,
Chairman, Subcommittee on Foundations,
U.S. Senate, Washington, D.C.

DEAR SIR: Rollin N. Hadley, director of the Isabella Stewart Gardner Museum, appeared on May 14 before your Subcommittee on Foundations on behalf of the Association of Art Museum Directors.

You have asked him for a statement of total assets of art museums adversely affected by the foundation section of the Tax Reform Act of 1969. Winterthur Museums to which Mr. Hadley referred.

Enclosed is a copy of the Winterthur Museum audited financial statement that will appear in the 1973 Annual Report which is now being printed. You will note that total assets were $82,892,708 at December 31, 1973. This is exclusive of collection objects and library holdings.

Winterthur Museum has recently received the enclosed advance ruling to terminate foundation status under the 60-month termination procedure. If, at the end of the 60 months (December 31, 1978), we have not maintained the required 10-percent public financial support, we will have to pay the 4-percent excise taxes on investment income for the five-year period. We are, therefore, very much interested in a change in the law that would exclude qualified museums from the 4-percent excise tax provision.

For years 1970, 1971, 1972, and 1973, Winterthur Museum paid 4-percent excise taxes amounting to $478,903. Maintenance, security, utilities, and related expenditures are rather well fixed. One cannot reduce them wthout closing down parts of the Museum. Excise taxes are, therefore, not paid by reducing basic operating expenses, but rather are taken from funds that normally would be available for educational programs.

Sincerely yours,

CHARLES VAN RAVENSWAAY, *Director.*

FRANK A. GUNNIP & COMPANY,
Wilmington, Del., February 26, 1974.

ACCOUNTANTS' OPINION

THE EXECUTIVE COMMITTEE OF THE BOARD OF TRUSTEES—THE HENRY FRANCIS DUPONT WINTERTHUR MUSEUM, INC.

We have examined the balance sheet of The Henry Francis duPont Winterthur Museum, Inc., as of December 31, 1973, and the related statement of changes in fund balances for the year then ended. Our examination was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned statements present fairly the financial position of The Henry Francis duPont Winterthur Museum, Inc., at December 31, 1973, and the results of its operations for the year then ended, in conformity with generally accepted accounting principles appropriate for nonprofit organizations applied on a basis consistent with that of the preceding year.

FRANK A. GUNNIP.

The Henry Francis duPont Winterthur Museum, Inc. balance sheet, Dec. 31, 1973

Assets:	
Cash	$303, 322
Accounts receivable	40, 839
Bookstore inventory	87, 321
Prepaid expenses	9, 182
Investments:	
Corporate notes	1, 441, 038
U.S. Government securities	1, 151, 997
Corporate bonds	9, 049, 610
Mortgages	947, 218
Preferred stock	70, 241
Common stock	53, 064, 237
Total	65, 724, 341
Land and buildings	16, 727, 703
Total	82, 892, 708
Liabilities and fund balances:	
Accounts payable	$85, 224
Accrued payroll taxes and withholdings	5, 274
Provision for Federal excise tax	121, 924
Fund balances:	
Current	1, 099, 674
Restricted	1, 208, 346
Endowment	63, 644, 563
Capital	16, 727, 703
Subtotal	82, 680, 286
Total	82, 892, 708

The Henry Francis duPont Winterthur Museum, Inc., changes in fund balances for the year ended Dec. 31, 1973

Increases:	
Admissions	$174, 189
Gifts	196, 329
Investment income	3, 132, 470
Trust income	108, 102
Bookstore sales, food sales and other receipts	392, 903
Total	4, 003, 993
Decreases:	
Collection objects, library materials, fellowship grants and publishing	67, 415
Curatorial, educational and research expenses	878, 482
General and administrative expenses	1, 027, 851
Maintenance and security of buildings and grounds	1, 464, 524
Federal excise tax	120, 650
Book loss from investment transactions	96, 723
Total	3, 755, 645
Net change in fund balances	248, 348
Fund balances, Jan. 1, 1973	82, 431, 938
Fund balances, Dec. 31, 1973	82, 680, 286

THE HENRY FRANCIS DUPONT WINTERTHUR MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS, DECEMBER 31, 1973

Summary of significant accounting policies

Inventories.—Inventories are valued at the lower of cost or market. The Revolving Account for Publishing Activities in the Restricted Funds maintains an inventory of publications with The University Press of Virginia and in storage at Winterthur. The total cost of the inventory, not shown in the financial statements at December 31, 1973, was approximately $135,000 (1972—$125,000). Publication costs are recorded as decreases in fund balances when paid.

Depreciation.—For financial statement purposes there is no provision for depreciation of fixed assets.

Capital funds.—Land and buildings are reported at estimated value on acquisition date and have been consistently recorded in the accounting records upon acquisition or completion of construction. The value of collection objects and library holdings is not included in the accounting records.

Investments.—Investments are shown in the balance sheet at cost or fair market value on date of receipt. The total market value of investments at December 31, 1973, was approximately $63,700,000. The Museum has consistently followed the policy of not accruing income on investments.

Pension.—A noncontributory pension plan is in effect for all eligible employees. The Museum's policy is to fund pension cost accrued. The total pension contribution to the plan was $95,000 in 1973 (1972—$90,605).

DEPARTMENT OF THE TREASURY,
INTERNAL REVENUE SERVICE,
Washington, DC., May 3, 1974.

Key District: Philadelphia, Pennsylvania.
Advanced Ruling Period Ending: December 31, 1978.

THE HENRY FRANCIS DUPONT WINTERTHUR MUSEUM, INC.,
Winterthur, Del.

GENTLEMEN: This is in reply to your request for an advance ruling under the provisions of Regulations section 1.507–2(e) permitting you to terminate your private foundation status.

Our records indicate that you operate a museum of early American culture, Winterthur, which is open to the public. You also conduct many research, educational, and cultural programs for the benefit of the public. You were recognized as exempt from Federal income taxes under section 501(c)(3) of the Internal Revenue Code by letter dated May 19, 1953.

Winterthur was created by Henry Francis du Pont, who was your only substantial contributor until his death in 1969. Your support is derived from an endowment fund, admission fees, and contributions of cash and collection pieces.

We have further determined you can reasonably be expected to be an organization of the type described in sections 170(b)(1)(A)(vi) and 509(a)(1). Accordingly, you will be treated as a publicly supported organization and not a private foundation, for an advanced ruling period beginning January 1, 1974.

Regulations section 1.507–2(d) provides that in order to meet the requirement of section 507(b)(1)(B) of the 60 month termination period as a section 509(a)(1) organization, you must meet the requirements of section 509(a)(1) for a continuous period of at least 60 calendar months.

For purposes of section 507(b)(1)(B) of the Code, you will be considered to be a section 509(a)(1) organization described in section 170(b)(1)(A)(vi) for a continuous period of 60 calendar months only if you satisfy the provisions of Regulations section 1.170 A–9(e) based upon aggregate data for such entire period, rather than for any shorter period set forth in section 1.170A–9(e). (In our letter issued June 19, 1973, we ruled that you cannot terminate your private foundation status in a 12 month termination under section 507(b)(1)(B)).

At the end of your 60 month termination, however, you must establish with your key District Director, Philadelphia, Pennsylvania, that for such 60 months you were in fact an organization of the type described in section 170(b)(1)(A)(vi). If you establish this fact, you will be classified as a section 509(a)(1) organization as long as you continue to meet the requirements of section 170(b)(1)(A)(vi).

If you fail to satisfy the requirements of section 509(a)(1) for the contin-

uous 60-month period, but you satisfy the requirements of section 509(a)(1) for any taxable year or years during such 60-month period, you will be treated as a section 509(a)(1) organization for such taxable year or years. Grants or contributions made during such taxable year or years shall be treated as made to an organization described in section 509(a)(1).

In addition, sections 507 through 509 and Chapter 42 shall not apply to such organization for any taxable year within such 60-month period for which it does meet such requirements.

Grantors and donors may rely on the determination that you are not a private foundation for your 60-month period. However, if notice that you will no longer be treated as a section 509(a)(1) organization is published n the Internal Revenue Bulletin, grantors and donors may not rely on this determination after the date of such publication. Also, a grantor or donor may not rely on this determination if he was in part responsible for, or was aware of, the act or failure to act that resulted in your loss of section 509(a)(1) status, or acquired knowledge that the Internal Revenue Service had given notice that you would be removed from classification as a section 509(a)(1) organization.

We are informing your key District Director of this action. Please keep this ruling letter in your permanent records.

Sincerely yours,

MILTON CERNY,
Chief, Rulings Section 1, Exempt Organizations Branch.

THE FRICK COLLECTION
New York, N.Y., June 13, 1974.

Senator VANCE HARTKE,
Chairman, Subcommittee on Foundations,
U.S. Senate, Committee on Commerce, Washington, D.C.

DEAR SENATOR HARTKE: Mr. Rollin Hadley, director of the Gardner Museum in Boston, who testified before the Subcommittee on Foundations on May 14th, has asked me to respond directly to your letter of May 28th asking for certain information for the hearing record from museums adversely affected by the 4% excise tax.

The endowment assets of The Frick Collection had a market value as of May 31, 1974 of $50,917,000.

For the years 1970 to 1973, The Frick Collection paid excise taxes of $66,727, $52,935, $77,513 and $70,000 (estimate), respectively.

For your further information, admission to the Collection and to the frequent lectures and concerts has always been free. During 1973, 256,245 people visited the museum.

We are very grateful that your subcommittee is considering legislative relief from the 4% tax for those museums which serve a broad public. If I can give you any further information about The Frick Collection and the adverse effect on it of the excise tax, please do let me know.

Sincerely,

DAVID MONROE COLLINS.

ISABELLA STEWART GARDNER MUSEUM,
Boston, Mass., June 14, 1974.

Senator VANCE HARTKE,
Chairman, Subcommittee on Foundations,
U.S. Senate, Washington, D.C.

DEAR SENATOR HARTKE: In answer to your request for assets of this institution in support of my testimony on 14 May before the Senate Committee on Finance, Subcommittee on Foundations, I enclose the audited report for 1973. Appraised valuation here shown was made in 1936.

In 1971 when the museum was required to prove that it qualified as an *operating* foundation the Art Dealers Associations made an appraisal at no little expense to the museum. Out of the approximately 2,000 objects in the collection 142 objects appraised were valued at $47,661,000.00 (see attached).

I have asked other institutions named in the testimony to write directly to you in response to your request.

Sincerely yours,

ROLLIN VAN N. HADLEY, *Director.*

Enclosure.

ART DEALERS ASSOCIATION OF AMERICA, INC.,
New York, N.Y., January 6, 1971.

Mr. ROLLIN VAN N. HADLEY,
Director,
Isabella Stewart Gardner Museum,
Boston, Mass.

DEAR MR. HADLEY: Pursuant to our agreement, a panel of four members of this Association, Mssrs. Eugene V. Thaw, Frederick Mont, Clyde Newhouse and Eric Stiebel, visited the Isabella Stewart Gardner Museum where they examined the works listed on the annexed Schedule. Each member of th panel was and is fully familiar with the market values, in the United States and abroad, of works of the nature and period of the listed works. The appraised value shown after each work on the Schedule is believed to be the fair and reasonable present market value of the work.

Very truly yours,

By Gilbert S. Edelson,
Secretary and Treasurer.

The Isabella Stewart Gardner Museum, Inc., trustee under the will of Isabella Stewart Gardner: Statements of net assets and fund balances Dec. 31, 1973 and 1972

Net assets	1973	1972
Cash	$18,628	$46,482
Commercial paper, at cost which approximates market	1,811,326	
Investments, at cost (note 1):		
Bonds (quoted market price at Dec. 31, 1973—$2,331,054)	2,351,101	3,612,315
Stocks (quoted market price at Dec. 31, 1973—$8,985,011)	9,344,653	8,554,293
Total	11,695,754	12,166,608
Museum property (note 2):		
Museum building and underlying land	366,400	366,400
Contents of Museum building	4,015,000	4,015,000
Old greenhouse and underlying land		49,000
New greenhouse and underlying land	585,426	572,237
Total	4,966,826	5,002,637
Total assets	18,492,534	17,215,727
Less, accrued real estate and income taxes (note 5)	42,486	54,953
Net assets	18,450,048	17,160,774
Fund balances:		
Operating (note 3)	266,638	115,545
General	16,445,680	15,229,191
Pension (note 4)	1,055,169	1,097,929
Maintenance and depreciation	682,561	718,109
Total	18,450,048	17,160,774

Senator HARTKE. Well, unless there are other questions, we thank all of you.

That concludes our witness list for this morning, and we will recess again, subject to the call of the Chair and the availability of dates with the committee.

This committee is part of the Finance Committee as you know, and we are going into the question of medical care and so we have a problem on scheduling.

[Whereupon, at 11:15 a.m., the subcommittee recessed, subject to the call of the Chair.]

PRIVATE FOUNDATIONS

MONDAY, JUNE 3, 1974

U.S. SENATE,
SUBCOMMITTEE ON FOUNDATIONS,
COMMITTEE ON FINANCE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 2:15 p.m., in room 2221, Dirksen Senate Office Building, Senator Vance Hartke (chairman of the subcommittee) presiding.

Present: Senators Hartke and Bentsen.

Senator HARTKE. The committee will please come to order.

This is the third day in a series of hearings being held by this subcommittee to attempt to get the facts which we need concerning private foundations. Our previous 2 days of hearings revealed a microcosm of the public's attitude toward philanthropy in the United States.

We had witnesses who described the many accomplishments which were made possible by foundation money. We had witnesses who recognized the positive contributions of foundations, but who encouraged foundations to do much more, and we had witnesses who concluded that foundations were little more than a tax dodge for the wealthy.

I suspect that there is more than a little bit of truth in each of these viewpoints. What is most disturbing to me is the almost complete absence of hard facts. Congress acted in 1969 with only the barest of facts when we established a set of new requirements for private foundations. There were abuses in 1969, and they had to be corrected.

I do not dispute the wisdom of those who proposed the provisions of the Tax Reform Act of 1969 which apply to private foundations. What I do say is that none of us knew in 1969 just how extensive those abuses were, nor could we have known just what the impact of the new requirements would be.

Our hearing today gets right to the heart of this question. Witness after witness before this subcommittee has pointed out the continuing lack of information about private foundations. We have had hearings on the impact of the 1969 act on foundations, but there have been, as I said, precious few facts.

In other words, have the changes adopted in 1969 caused some foundations to go out of business?

Have they discouraged new foundations from being established?

Have they simply encouraged private foundations to change their status to public charities?

Most important of all, have the changes made in 1969 discouraged the unnecessary accumulation of capital and resulted in more money going to charitable purposes?

These are basic questions. The answers to these questions are essential if Congress is to evaluate both the effects of the 1969 Tax Act and the role of foundations in our society today.

Our witness today is Mr. Donald C. Alexander, who is Commissioner of the Internal Revenue Service. He is in a position to provide this subcommittee and the public with much of the information we need.

The IRS is charged with the responsibility of administering private foundations. Those organizations seeking tax exempt status, be they private foundations or public charities, must make application to the Service. Once they achieve tax exempt status, they must file annual information returns and they also become subject to audit by the IRS. We therefore look forward to his testimony today.

Mr. Alexander, would you please come forward. I submitted, as you know, a list of questions to you on March the 22d, and you have submitted answers. Bring whoever you want to with you.

What we will do is put those questions into the record at this time with your replies to those questions.

[The information referred to follows:]

U.S. SENATE,
COMMITTEE ON FINANCE,
March 22, 1974.

Hon. DONALD C. ALEXANDER,
Commissioner,
Internal Revenue Service,
Washington, D.C.

DEAR COMMISSIONER ALEXANDER: The Subcommittee on Foundations plans to hold hearings on the subject of problems raised by the administration of private foundations by the Internal Revenue Service, in the latter part of April. We would appreciate having your comments on this subject during our hearings and I would specifically like you to direct your attention to the series of questions which follows.

1. (a). How is the Internal Revenue Service presently organized with respect to exempt organizations?

(b) What functions are performed?

(c) How many people are involved?

(d) How many man-hours are involved?

(e) What activities are undertaken?

(f) How much money is budgeted for this activity?

(g) How often are audits performed?

(h) What was the impact on your normal exempt organization audit activities of programs related to the Economic Stabilization Act and the energy program?

2. (a) In your auditing activities do you treat private foundations differently from other exempt organizations?

(b) How much of your budget goes to auditing private foundations?

(c) How many man-hours are involved in audits of private foundations?

3. (a) What changes do you anticipate in your activities related to exempt organizations if the Special Assistant Commissioner proposed by both House and Senate pension bills become law?

(b) What plans does the Service have for recruiting, employing and training specialized personnel in the exempt organization field?

4. (a) How many organizations are exempt under section 501(c)(3)?

(b) How many of these organizations came into existence after 1969?

(c) How many were already in existence but first brought forth their existence to I.R.S. after 1969?

5. (a) Of the section 501(c)(3) organizations now registered with I.R.S., how many are so-called "public charities" under *each* of the clauses (i) through (v) of section 170(b)(1)(A)?

(b) How many are "publically supported" under clause (vi) of section 170 (b)(1)(A)?

(c) How many are section 509(a)(2) organizations?

(d) How many are section 509(a)(3) organizations?

(e) 1. How many are private operating foundations?

2. How many are non-operating foundations?

3. What is the asset value of operating foundations and of non-operating foundations?

4. What is the asset value of foundations formed after the 1969 Tax Act?

(f) What figures does the Service have on foundation terminations, including a breakdown based upon operating and non-operating foundations and the assets of each?

(g) The answers to the above questions are based on information as of what date?

6. (a) Of the section 509(a)(3) organizations, what are the patterns of relationship to "public" charities, and to section 509(a)(2) organizations?

(b) How many qualify because they are "operated in connection with" a public charity?

7. How many of the 509(a)(3) organizations provide funds as their sole or primary service to their public charity or section 509(a)(2) organization?

8. (a) How frequently have each of the categories of public charities and private foundations been audited since 1969?

(b) How many man-hours or man-years have been used in performing these audits?

(c) Have these audits generally been conducted by personnel whose primary activity is the auditing of taxable income?

9. (a) How much has been collected under each of the categories of private foundation taxes other than the tax on investment income in each of the years since the 1969 Act?

(b) Of this amount, how much constituted "first-level" taxes and how much constituted "second-level" taxes?

(c) How much constituted penalties under section 6684?

(d) How much constituted "wringer" taxes under section 507?

(e) How many proceedings are still outstanding or a "first-level" tax has been determined but the case has not yet been closed?

10. Generally, are "first-level" taxes determined as a result of the exempt organization volunteering the information, information received from State authorities, or information developed from I.R.S. examination of returns and I.R.S. audits? To what extent has State authorities participated in the closing of cases so as to avoid the necessity for "second-level" taxes?

11. To what extent does I.R.S. coordinate the audits of charitable organizations and individual taxpayers?

12. Why does the federal tax return no longer require disclosure of the names of specific charitable organizations to which the taxpayer contributed if he has retained cancelle dchecks?

13. (a) To what extent does I.R.S. monitor the requirement that private foundations publish a notice of the availability of their report for public inspection and that it be available?

(b) Have you found any situation in which a foundation was not in compliance with this requirement?

(c) If so, list each such foundation and any subsequent corrective action.

14. What evidence is there that the payout requirement has resulted in an increased amount of current expenditures for charity by private foundations?

15. Of the organizations on the Treasury Department's cumulative tax exempt list, how many use the term "foundation," "fund," or "trust" in their name? How many of these organizations are not classified by the I.R.S. as private foundations?

16. (a) How many rulings have been issued under the Tax Reform Act which affect private foundations?

(b) How many of these rulings have been published?

17. Please supply the Subcommittee with the I.R.S. regulations applying to the requirements of the Freedom of Information Act.

To expedite the preparation for the Subcommittee's hearings, I would appreciate if you would designate a member of your staff to work with Howard Marlowe of my staff. Please have your designee contact Mr. Marlowe at the earliest possible time by calling 225–4814.

With my best wishes, I am

Sincerely,

VANCE HARTKE,
Chairman, Subcommittee on Foundations, Senate Finance Committee.

DEPARTMENT OF THE TREASURY,
INTERNAL REVENUE SERVICE,
Washington, D.C., May 30, 1974.

Senator VANCE HARTKE,
Chairman, Subcommittee on Foundations,
Senate Finance Committee,
U.S. SENATE,
Washington, D.C.

DEAR SENATOR HARTKE: In accordance with our understanding with Mr. Marlowe of your staff, we are forwarding a background paper summarizing the areas of your inquiry contained in your letter of March 22, 1974.

We look forward to consulting with you and the other members of your Subcommittee on the very complex issues involved in the administration of the statutes relating to private foundations.

With kind regards,

Sincerely,

DONALD C. ALEXANDER.

Enclosure.

BACKGROUND MATERIAL FOR SENATOR HARTKE

1. ORGANIZATION STRUCTURE AND RESPONSIBILITIES

The Internal Revenue Service's present organization with respect to exempt organizations involves several principal functional areas: Compliance, Technical, and Accounts, Collection and Taxpayer Service (ACTS). Personnel are located at the National Office in Washington, D.C., and at selected offices throughout the country.

The Assistant Commissioner (Compliance) has responsibility for the audit portion of our exempt organization program. Specifically, the Exempt Organizations Examination Branch within the Audit Division plans, monitors, and evaluates nation-wide programs for the examination of exempt organization returns and records. It issues procedural material to guide exempt organization examinations, and it reviews certain revenue agent reports to ensure quality and uniformity of examinations. It also has responsibility for the Exempt Organization Master File.

The Internal Revenue Service has seven regional offices. Within the office of each Regional Commissioner, there is an exempt organization program manager on the staff of the AsAsistant Regional Commissioner (Audit). The program manager monitors the exempt organization program of the key districts within the particular region.

The actual field operations are carried out by the Office of International Operations and sixteen key districts located throughout the country:

Region:	*Key districts*
North-Atlantic	Boston, Manhattan.
Mid-Atlantic	Baltimore, Philadelphia.
Southeast	Atlanta.
Central	Cincinnati, Cleveland, Detroit.
Midwest	Chicago, St. Louis, St. Paul.
Southwest	Austin, Dallas.
Western	Los Angeles, San Francisco, Seattle.

Within the audit divisions of these key districts, there are exempt organization groups which process applications for recognition of exemption and conduct examinations of exempt organizations. When an organization disagrees with an examiner's decision, a conferee specializing in exempt organization work will hear the case. The districts also have specialists to review the exempt organization cases for accuracy and completeness before they are closed.

The current audit program has private foundations audited on a five-year cycle, with the largest, most complex ones examined every two years. Other exempt organizations are audited on a scale designed to provide representative coverage. The programs related to the Economic Stabilization Act and the energy program had very little impact on our exempt organization activities.

The Assistant Commissioner (Technical) is primarily responsible for providing basic principles and rules for the uniform interpretation and application of the Federal tax laws administered by the Service. The Miscellaneous and Special Provisions Tax Division, through its Exempt Organizations Branch, carries out this function in the area of exempt organizations. The Branch's activities include providing rulings to taxpayers, furnishing technical advice to IRS district offices, reviewing regulations, preparing Revenue Rulings and Procedures, and conducting in-depth studies of difficult technical issues.

Also in Technical, the Tax Forms and Publications Division works with the Exempt Organizations Branch in developing explanatory publications, forms, form letters, and other materials for the use and guidance of Service personnel and the public.

The Assistant Commissioner (Accounts, Collection, and Taxpayer Service) has responsibility for the computer processes necessary to administer the exempt organization program and for the collection of delinquent returns and accounts due by exempt organizations. The Accounts and Data Processing Division writes and maintains the computer programs and provides the necessary instructions to process all exempt organization returns, forms, and related attachments filed with the Service.

The documents are actually received at the Philadelphia Service Center where the processing takes place. Data from the documents are transcribed to be posted to the Exempt Organization Master File (EOMF). This EOMF is maintained and updated periodically through a series of computer programs at the National Computer Center at Martinsburg, West Virginia.

For fiscal year 1974, budgeted figures for the exempt organization program are summarized below.

	Audit	Technical	ACTS
Man-years	845	160	206
Man-hours	1,757,600	332,000	428,480
Amount	$15,198,000	$3,100,000	$2,840,000

The number of man-years times 2,080, the number of hours a full-time employee is paid for per year, equals the man-hours on the above chart. Of course, some of this time will represent leave, holidays, and indirect program requirements such as training, staff meetngs, etc. The man-year figure also allows for the portion of time management must devote to the program.

These three functions carry the principal portion of the exempt organization program. Other functions become involved as necessary. For example, the office of the Chief Counsel handles legal interpretations and litigation matters involving an exempt organization, and the office of the Assistant to the Commissioner (Public Affairs) issues news releases on exempt organization matters. The Assistant Commissioner (Administration) provides support services of training, personnel, facilities management, and fiscal management.

2. CONDUCT AND EXTENT OF PRIVATE FOUNDATION EXAMINATION PROGRAM

Concerning the conduct of private foundation examinations, our examiners seek to apply the law fairly and impartially. There is no difference in treatment of private foundations as opposed to other kinds of exempt organizations.

With regard to the extent of our private foundation audit program, we have had more extensive coverage than of other organizations. By December 31, 1974, we plan to have audited substantially all private foundations at least once during the previous five-year period. The largest, most complex private foundations are audited on a two-year cycle rather than the five-year cycle.

Audit coverage of other exempt organizations is not done on the basis of 100% coverage. Through a classification system, we select the returns of organizations whose affairs most need to be examined. Areas which show patterns of noncompliance are stressed.

The Service's private foundation audit activity for fiscal year 1974 involves approximately 1,123,000 man-hours. The amount budgeted for this audit program was $9,711,522. These figures represent 63.9% of the total exempt organization examination program.

3. ANTICIPATED CHANGES IF THE BILL TO PROVIDE A SPECIAL ASSISTANT COMMISSIONER BECOMES LAW

Establishment of a new office of employee plans and exempt organizations headed by an Assistant Commissioner would elevate responsibility for these activities within the Service and increase coordination between headquarters and the field. The resultant internal changes would be primarily organizational. We do not expect major changes in our activities of enforcing the exempt organizations provisions of the Internal Revenue Code which do not relate to pension matters. However, the new organizational structure would permit more unified policy guidance and more uniform treatment of cases involving the status of tax-exempt organizations.

We also do not anticipate any major changes in our recruiting and training of exempt organization personnal. At the present time, we fill vacancies in the field by selecting people from our revenue agnt and tax auditor ranks and providing them with the necessary specialized training. They are then assigned to exempt organization groups.

Employees presently under the Assistant Commissioner (Technical) are typically recruited from lawyers, recent law school graduates, people with accounting backgrounds, and people with experience in the field of exempt organizations. New employees are required to complete a formal training program.

4. NUMBER OF SECTION 501(C) (3) ORGANIZATIONS

As of March 31, 1974, our Exempt Organization Master File (EOMF) lists 226,122 active organizations as exempt under section 501(c)(3). However, this figure does not represent the universe of such organizations. For example, organizations which aer not private foundations and whose gross annual receipts are normally not more than $5,000 need not apply for recognition of exemption with the Service unless they wish to receive a ruling. If they do not have an exemption letter, they will not be on the EOMF. Churches, their integrated auxiliaries, and conventions or associations of churches are also excepted from having to file an exemption application, and, thus, they may not be listed either.

As of March 31, 1974, there are 68,682 more section 501(c)(3) organizations on the EOMF than on January 1, 1970. However, this figure is not equal to the number that came into existence after 1969 because there have also been deletions from the EOMF during this period and some additions have been made to correct previous omissions. We don't have a figure for how many post-1969

organizations were created, nor are we able to tell how many were in existence before 1969 but only became known to us after that date.

5. TYPE AND NUMBER OF PUBLIC CHARITIES, NUMBER OF OPERATING AND NON-OPERATING FOUNDATIONS, ASSET VALUES OF PRIVATE FOUNDATIONS, AND FOUNDATION TERMINATIONS

As of March 31, 1974, we have classified 174,186 organizations as being "public charities." For our present administrative purposes, we need to classify charitable organizations only as to their status as a private foundation or a public charity. Because organizations described in Code section 170(b)(1)(A)(i) through (vi), 509(a)(2), and 509(a)(3) are only subclasses of public charities, it has not been necessary to code our EOMF to provide a count of these particular categories.

As of March 31, 1974, there were 28,326 private foundations consisting of 27,301 non-operating foundations and 1,025 operating foundations. Because information as to the asset value of each category would serve no purpose in our administration of the statute, none is maintained. The Service also does not compile statistics as to the asset value of foundations formed after the 1969 Tax Reform Act. However, our EOMF does provide statistical data as to book value of assets reported by all private foundations. These assets for the returns processed during calendar year 1973 were in the amount of $26 billion.

Concernng private foundation terminations, many organizations discontinued operations before they were classified as private foundations under the 1969 Tax Reform Act. Thus, no reliable figures are available.

6. RELATIONSHIPS OF SECTION 509(a)(3) ORGANIZATIONS

We don't compile information to show patterns of relationship between section 509(a)(3) organizations and ether section 509(a)(1) or section 509(a)(2) organizations. All three categories are considered public charities. As indicated in the answer to Question 5, it has not been necessary for us to code our EOMF to provide a count of the subclasses of public charities. Thus, we do not have information as to how many qualified under Code section 509(a)(3) because of being operated in connection with an organization described in either section 509(a)(1) or (2).

7. SECTION 509(a)(3) ORGANIZATIONS PROVIDING FUNDS

The actual number of 509(a)(3) organizations providing funds as their sole or primary service has not been tabulated, nor is it available.

8. FREQUENCY AND EXTENT OF AUDIT COVERAGE

By December 31, 1974, substantially all private foundations will have been audited at least once since 1969. From fiscal year 1970 through fiscal year 1973, about 9,000 public charities were examined. As a point of reference, approximately 80,000 public charities filed returns last year.

During fiscal years 1970 through 1973, 889 man-years were expended in the conduct of these examinations. Examinations of exempt organization returns are performed by exempt organization specialists who work exclusively in this area.

9. PRIVATE FOUNDATION INITIAL EXCISE TAX COLLECTIONS

[In thousands of dollars]

	Fiscal years—				
	1970	1971	1972	1973	1974 [1]
Sec. 4941—Self-dealing		8	45	78	89
Sec. 4942—Failure to distribute income				94	37
Sec. 4943—Excess business holdings		27	51	13	
Sec. 4944—Investments which jeopardize charitable purposes				16	2
Sec. 4945—Taxable expenditures		1	7	1	

[1] July 1, 1973 through Jan. 31, 1974.

We are unable to identify how much of the above taxes are initial or additional excise taxes. Nor do we compile data from tax collections under section 6684 or section 507.

Also, since our statistics are kept on the basis of closed cases, we are unable to provide information as to the number of cases in progress (either in audit or in the process of appeal) in which initial tax liability under sections 4941–4945 has been determined upon audit.

10. DETERMINATION OF "FIRST-LEVEL" TAXES, AND PARTICIPATION OF STATE AUTHORITIES IN CLOSING CASES TO AVOID "SECOND-LEVEL" TAXES

There is not available sufficient data to state whether "first-level" taxes are, as a general rule, voluntarily reported by exempt organizations as opposed to resulting from an audit. While there may be isolated instances with regard to state participation in closing cases, we have no records reflecting any significant participation by the states in this area.

11. COORDINATION OF AUDITS OF CHARITABLE ORGANIZATIONS AND INDIVIDUAL TAXPAYERS

It is general Service practice that an examiner extends an audit as far as is necessary to determine a taxpayer's correct tax liability. In examining a charitable organization, the audit is directed towards determining whether or not an organization is operating within the exemption requirements.

We do coordinate the audits of charitable organizations and individual taxpayers where necessary in the judgment of the examining officer. For example, this action would be taken in instances involving funds used for personal benefit or where there is a question of the value of a donor's contribution. The decision to extend an examination of a charitable organization to include individual taxpayers is made on a case by case basis.

12. DISCLOSURE OF SPECIFIC CHARITABLE DEDUCTIONS

The Federal tax return filed by individuals no longer requires itemizing of the names of specific charitable organizations to which the taxpayer contributed. The change was meant to make tax return preparation easier by simplifying the tax return form.

13. MONITORING COMPLIANCE WITH SECTION 6104(d) OF THE CODE

A private foundation may use Form 990–AR for the annual report required to be filed under Code section 6056. The instructions to Form 990–AR state that there be attached a copy of the published notice of availability of the annual report required by section 6104(d) of the Code. These annual reports are filed with the Philadelphia Service Center. Upon their receipt, the Service Center checks to see that the copy of the notice of availability is attached, or it follows up as necessary. In addition, if the foundation's return has been assigned to the Audit Division for examination, the examining officer is required to verify that the public inspection notice has been published.

The Service does not keep a separate record of the organizations which required follow-up action to solicit proof of publication of a notice of availability. Thus, we are unable to identify specific cases as you requested because they cannot be separated from the records which are kept.

14. EVIDENCE THAT THE PAYOUT REQUIREMENT HAS RESULTED IN AN INCREASED AMOUNT OF CURRENT EXPENDITURES FOR CHARITY BY PRIVATE FOUNDATIONS

We have no figures to show whether payouts by private foundations have increased for charitable purposes.

15. USE OF CERTAIN TERMS IN CUMULATIVE LIST

The *Cumulative List of Organizations* contains approximately 131,000 names, of which 103,000 are not classified as private foundations. The organizations are listed alphabetically exclusive of such terms as "foundation," "fund," or

"trust," so that a listing of organizations based on their use of such terms is possible only by visual inspection.

We do not believe that such a list would be particularly useful. While a name may serve to identify a private foundation in many instances, it is not a reliable indicator. To illustrate with examples from Page 1 of the *Cumulative List*, AAA Scholarship Foundation, Inc., is a public charity; Aaronsburg Story, Inc., is a private foundation.

16. PRIVATE FOUNDATION RULINGS

As of March 1974, approximately 28,000 organizations have been ruled to be private foundations, and some 174,000 organizations (including approximately 74,000 subordinates of central organizations) have been ruled to be nonprivate foundations. Although no records are maintained on the number of rulings issued under the Tax Reform Act that affect private foundations, the chart below lists the number of requests received for rulings under provisions of the Act and is an indication of the number of such rulings issued. (These statistics do not include foundation status classification rulings.) The recent increase in ruling requests is primarily in the area of section 4945 of the Internal Revenue Code regarding private foundation scholarship programs.

Period:	*Ruling requests*
Month of December 1970	20
Calendar year 1971	380
Calendar year 1972	416
Calendar year 1973	1,221
Months of January, February, and March 1974	314
Total ruling requests, December 1970 through March 1974	2,351

Twenty-two Revenue Rulings have been published on provisions of the Reform Act that affect private foundations. The Revenue Ruling publication program in this area has been limited because many regulations affecting private foundations were not published until late 1973 and others have yet to be finalized and published.

17. I.R.S. REGULATIONS APPLYING TO THE FREEDOM OF INFORMATION ACT

Copies of Regulations 601.701 and 601.702 which pertain to the Freedom of Information Act are attached. Because reference is made therein to Regulation 301.6104 which specifically applies to the publicity of information on certain exempt organizations and trusts, we have attached a copy of this regulation too.

SUBPART G—RECORDS

§ 601.701 Publicity of information

Section superseded by Part 71 of Title 27 of the Code of Federal Regulations to the extent that it applied to alcohol, tobacco, firearms, and explosives records.

(a) General. Effective July 4, 1967, section 552 of title 5 of the United States Code is amended to prescribe revised provisions regarding the publicizing of information by Federal agencies. Generally, such section divides agency information into three major categories and provides methods by which each category is to be made available to the public. The three major categories, for which the disclosure requirements of the Internal Revenue Service are set forth in § 601.701, are as follows:

(1) Information required to be published in the Federal Register;

(2) Information required to be made availble for public inspection and copying or, in the alternative, to be published and offered for sale; and

(3) Information required to be made available to any member of the public upon specific request.

The revised provisions of section 552 are intended to protect, subject to specified safeguards, the right of the public to information. Section 552 is not authority to withhold information from Congress.

(b) Exemptions—(1) In general. Under 5 U.S.C.A. § 552(b), the disclosure requirements of section 552 do not apply to certain matters described in nine specific exemptions, as follows:

(i) Matters specifically required by Executive order to be kept secret in the interest of the national defense or foreign policy;

(ii) Matters related solely to the internal personnel rules and practices of an agency, such as staff manuals or instructions, or parts thereof, which set forth guidelines, operating rules, or other criteria for officers or employees in auditing or inspection procedures, or in the selection or handling of cases, such as operational tactics, allowable tolerances, or criteria for the defense, prosecution, or settlement of cases;

(iii) Matters specifically exempted from disclosure by statute, as described in subparagraph (2) of this paragraph;

(iv) (a) Trade secrets and (b) commercial, financial, or other information, which is privileged or confidential and thus would not customarily be made public by the person from whom it is obtained, such as business sales statistics, inventories, customer lists, scientific or manufacturing processes or development, personal correspondence, or matter which the agency has obligated itself in good faith not to disclose;

(v) Interagency or intraagency memorandums or letters which would not be available by law to a party in litigation with an agency, including communications (such as internal drafts, memorandums between officials or agencies, opinions and interpretations prepared by agency staff personnel or consultants for the use of the agency, and records of the deliberations of the agency or staff groups) which the agency has received from another agency, or which the agency generates, in the process of issuing an order, decision, ruling, or regulation, drafting proposed legislation, or otherwise carrying out its functions and responsibilities, if such communications would not routinely be available to such party through use of the discovery process;

(vi) Personnel and medical files and similar files the disclosure of which would constitute a clearly unwarranted invasion of the personal privacy of any officer or employee of an agency or of any other person;

(vii) Investigatory files compiled for any law enforcement purpose, including files prepared in connection with related Government litigation and adjudicative proceedings, except to the extent available by law to a party other than an agency;

(viii) Matters contained in or related to examination, operating, or condition reports prepared by, on behalf of, or for the use of an agency responsible for the regulation or supervision of financial institutions; or

(ix) Geological and geophysical information and data, including maps, concerning wells, such as seismic reports and other exploratory findings of oil companies.

(2) Matters specifically exempted from disclosure by statute. For purposes of subparagraph (1)(iii) of this paragraph, statutory provisions which either specifically exempt certain matters from disclosure by officers or employees of the Internal Revenue Service or specifically provide for disclosure under appropriate circumstances include the following sections of the Code and the regulations thereunder:

(i) Section 4102, relating to inspection by certain State or local government officers of records with respect to taxes on petroleum products;

(ii) Section 6103, relating to publicity of certain returns and disclosure of information as to persons filing income tax returns;

(iii) Section 6104, relating to publicity of information required from certain exempt organizations and certain trusts;

(iv) Section 6106, relating to publicity of unemployment tax returns;

(v) Section 66108, relating to the publication of statistics of income; and

(vi) Section 7213, relating to penalties for unauthorized disclosure of information by Federal officers or employees or other persons.

(3) Application of exemptions. Even though an exemption described in subparagraph (1) of this paragraph may be fully applicable to a matter in a

particular case, the Internl Revenue Service may, if not precluded by law, elect under the circumstances of that case not to apply the exemption to such matter. The fact that the exemption is not applied by the Service in that particular case has no precedential significance as to the application of the exemption to such matter in other cases but is merely an indication that in the particular case involved the Service finds no compelling necessity for applying the exemption to such matter.

As amended July 1, 1967, 32 F.R. 9543; Apr. 12, 1969, 34 F.R. 6433; Feb. 23, 1973, 38 F.R. 4973.

§ 601.702 Publication and public inspection

Section superseded by Part 71 of Title 27 of the Code of Federal Regulations to the extent that it applied to alcohol, tobacco, firearms, and explosives records.

(a) Publication in the Federal Register—(1) Requirement. Subject to the application of the exemptions described in paragraph (b) of § 601.701 and subject to the limitations provided in subparagraph (2) of this paragraph, the Internal Revenue Service is required under 5 U.S.C.A. § 552(a)(1) to separately state and currently publish in the Federal Register for the guidance of the public the following information:

(i) Descriptions of its central and field organization and the established places at which, the persons from whom, and the methods whereby, the public may obtain information, make submittals or requests, or obtain decisions, from the Service;

(ii) Statements of the general course and method by which its functions are channeled and determined, including the nature and requirements of all formal and informal procedures which are available;

(iii) Rules of procedure, descriptions of forms available or the places at which forms may be obtained, and instructions as to the scope and contents of all papers, reports, or examinations;

(iv) Substantive rules of general applicability adopted as authorized by law, and statements of general policy or interpretations of general applicability formulated and adopted by the Service; and

(v) Each amendment, revision, or repeal of matters referred to in subdivisions (i) through (iv) of this subparagraph.

Pursuant to the foregoing requirements, the Commissioner publishes in the Federal Register from time to time a statement, which is not codified in this chapter, on the organization and functions of the Internal Revenue Service, and such amendments as are needed to keep the statement on a current basis. In addition, there are published in the Federal Register the rules set forth in this part (Statement of Procedural Rules), such as those in Subpart E of this part, relating to conference and practice requirements of the Internal Revenue Service; the regulations in Part 301 of this chapter (Procedure and Administration Regulations); and the various substantive regulations under the Internal Revenue Code of 1954, such as the regulations in Part 1 of this chapter (Income Tav Regulations), in Part 20 of this chapter (Estate Tax Regulations) and, in Part 31 of this chapter (Employement Tax Regulations).

(2) Limitations—(i) Incorporation by reference in the Federal Register. Matter which is reasonably available to the class of persons affected thereby, whether in a private or public publication, will be deemed published in the Federal Register for purposes of subparagraph (1) of this paragraph when it is incorporated by reference therein with the approval of the Director of the Federal Register. The matter which is incorporated by reference must be set forth in the private or public publication substantially in its entirety and not merely summarized or printed as a synopsis. Matter the location and scope of which are familiar to only a few persons having a special working knowledge of the activities of the Internal Revenue Service may not be incorporated in the Federal Register by reference. Matter may be incorporated by reference in the Federal Register only pursuant to the provisions of 5 U.S.C. A. § 552(a)(1) and 1 CFR Part 20.

(ii) Effect of failure to publish. Except to the extent that a person has actual and timely notice of the terms of any matter referred to in subparagraph (1) of this paragraph which is required to be published in the Federal

Register, such person is not required in any manner to resort to, or be adversely affected by, such matter if it is not so published or is not incorporated by reference therein pursuant to subdivision (i) of this subparagraph. Thus, for example, any such matter which imposes an obligation and which is not so published or incorporated by reference will not adversely change or affect a person's rights.

(b) Public inspection and copying—(1) In general. Subject to the application of the exemptions described in paragraph (b) of § 601.701, the Internal Revenue Service is required under 5 U.S.C.A. § 552(a) (2) to make available for public inspection and copying or, in the alternative, to promptly publish and offer for sale the following information:

(i) Final opinions, including concurring and dissenting opinions, and orders, if such opinions and orders are made in the adjudication of cases;

(ii) Those statements of policy and interpretations which have been adopted by the Internal Revenue Service but are not published in the Federal Register; and

(iii) Its administrative staff manuals and instructions to staff that affect a member of the public.

The Internal Revenue Service is also required by 5 U.S.C.A. § 552(a) (2) to maintain and make available for public inspection and copying current indexes identifying any matter described in subdivisions (i) through (iii) of this subparagraph which is issued, adopted, or promulgated after July 4, 1967, and which is required to be made available for public inspection or published. No matter described in subdivisions (i) through (iii) of this subparagraph which is required by this subparagraph to be made available for public inspection or published may be relied upon, used, or cited as precedent by the Internal Revenue Service against a party other than an agency unless such party has actual and timely notice of the terms of such matter or unless the matter has been indexed and either made available for inspection, or published, as provided by this subparagraph. This subparagraph applies only to matters which have precedential significance. It does not apply, for example, to administrative manuals on roperty or fiscal accounting, vehicle maintenance, personnel administration, and similar proprietary functions of the Interal Revenue Service. Nor does it apply to any ruling or advisory interpretation which is issued to a taxpayer on a particular transaction or set of facts and applied only to that transaction or set of facts. This subparagraph does not apply to matters which have been made available pursuant to paragraph (a) of this section.

(2) Deletion of identifying details. To prevent a clearly unwarranted invasion of person privacy, the Internal Revenue Service will, in accordance with 5 U.S.C.A. § 552(a) (2), delete identifying details contained in any matter described in subparagraph (1) (i) through (iii) of this paragraph before making such matter available for inspection or publishing it. However, in every case where identifying details are so deleted, the justification for the deletion must be explained in writing. The written justification for deletion will be placed as a preamble to the document from which the identifying details have been deleted, except in the case of any matter which is published in the Internal Revenue Bulletin. An introductory statement will be placed in each Internal Revenue Bulletin providing that identifying details, including the names and addresses of persons involved, and information of a confidential nature are deleted to prevent unwarranted invasions of personal privacy and to comply with statutory provisions, such as section 7213 and 18 U.S.C.A. § 1905, dealing with disclosure of information obtained from members of the public.

(3) Public reading rooms—(i) In general. The National Office and each regional office of the Internal Revenue Service will provide a reading room or reading area where the matters described in subparagraph (1) (i) through (iii) of this paragraph which are required by such subparagraph to be made available for public inspection or published, and the current indexes to such matters, will be made available to the public for inspection and copying. In addition, the reading rooms wll contain other matters determined to be helpful for the guidance of the public, including a complete set of the rules and regulations (except those pertaining to alcohol, tobacco, firearms, and explosives) contained in this title, any internal revenue matters which may be incorporated

by reference in the federal register pursuant to paragraph (a) (2) (i) of this section, a set of Cumulative Bulletins, and copies of various Internal Revenue Service publications, such as the description of forms or publications contained in Publication No. 481. Fees will not be charged for the use of the materials in the reading rooms, but fees will be charged for copying and certification services, as provided in subdivision (iii) of this subparagraph. The public will not be allowed to remove any record from a reading room.

(ii) Addresses of public reading rooms. The addresses of the reading rooms are as follows:

National office

Mail address: Director, Public Information Division, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, D.C. 20224.

Location: Same as mail address.

North Atlantic region

Mail address: Regional Public Information Officer, Room 1102, 90 Church Street, New York, N.Y. 10007.

Location: Same as mail address.

Mid-Atlantic region

Mail address: Regional Public Information Officer, Post Office Box 12805, Philadelphia, Pa. 19108.

Location; 401 North Broad Street.

Southeast region

Mail address: Regional Public Information Officer, Post Office Box 926, Atlanta, Ga. 30801.

Location: Federal Office Building, 275 Peachtree Street.

Midwest region

Mail address: Regional Public Information Officer, 17 North Dearborn Street, Chicago, Ill. 60602.

Location: Same as mail address.

Central region

Mail address: Regional Public Information Officer, Room 7106, Federal Office Building, 550 Main Street, Cincinnati, Ohio 45202.

Location: Same as mail address.

Southwest region

Mail address: Regional Public Information Officer, 1114 Commerce Street, Dallas, Tex. 75202.

Location: Same as mail address.

Western region

Mail address: Regional Public Information Officer, Flood Building, 870 Market Street, San Francisco, Calif. 94102.

Location: Same as mail address.

(iii) Copying facilities. The National Office and each regional office will provide facilities whereby a person may obtain copies of material which is on the shelves of the reading room. Certification services with respect to copies will also be provided. The fees in respect of material on the shelves of the reading rooms are as follows:

Photocopies: each page	$0.10
Certification of photocopies by appropriate official; each certification	1.00
Sale of unpriced printed material; each 25 pages or fraction thereof	.25
Minimum charge applicable when one or more of the above charges is assessed	1.00

Generally, forms and instruction described in § 601.602 which may be obtained from district directors will not be available in the reading rooms. However, where such forms or instructions are available for distribution in the reading rooms, the fee listed in this subdivision for the sale of unpriced printed material will not apply. While certain relevant publications which are available for

sale through the Government Printing Office will be placed on the shelves of the reading rooms, such publications will not be available for sale in the reading rooms. Persons desiring to purchase such publications, for example, Internal Revenue Bulletins and Cumulative Bulletins, should contact the Superintendent of Documents, U.S. Government Printing Office, Washington, D.C. 20402. However, copies of pages of such publications on the reading shelves may be obtained at the reading rooms in accordance with the schedule of fees set forth in this subdivision.

(iv) Inability to use public reading rooms. If a person is unable or unwilling to visit a reading room in person but wishes to inspect identifiable reading room material, he may request permission to inspect such material at any office of the Internal Revenue Service. To the extent that requested material is available for inspection at the reading rooms and is also readily available for inspection at the office where the request is made, such material will promptly be made available for inspection at such office to the person making the request for inspection and, where facilities are available, for copying in accordance with the schedule of fees prescribed by subdivision (iii) of this subparagraph. Copies of the requested material may also be mailed to such person by such office upon request. If the requested reading room material is not readly available for inspection at the office where the request is made, then the request will be referred by such office to one of the reading rooms of the Internal Revenue Service.

(c) Specific requests for other identifiable records—(1) In general. Subject to the application of the exemptions described in paragraph (b) of § 601.701, the Internal Revenue Service is required under 5 U.S.C.A. § 552(a) (3) to make identifiable records, other than those made available pursuant to paragraphs (a) and (b) of this section, promptly available to any person upon request. The request for records under section 552(a) (3) must be made in accordance with the rules set forth in this paragraph. This paragraph applies only to records in being which rae in the possession or control of the Internal Revenue Service. Where a record in the possession or control of the Internal Revenue Service is the paramount or exclusive concern of another agency, the request for such record will be transferred to that agency, and the requester notified to that effect, to insure that the determination to disclose or withhold the record will be made by that agency. In applying this paragraph, the Internal Revenue Service will not compile a record pursuant to a request, or procure a record from sources outside the Service.

(2) Form of request. The request for records must be in writing and signed by the person making the request. The request is required to identify the requested records in accordance with subparagraph (4) of this paragraph. The request must set forth the address where the person making the request desires to be notified of the determination by the Internal Revenue Service as to whether the request will be granted. If the requester desires to make the inspection in an office other than the office to which the request is delivered or mailed, the request should designate the office of the Internal Revenue Service where inspection is desired. Where the person making the request desires to have a copy of the requested records sent to him without first inspecting such records, his request should so state.

(3) Time and place for making request. The request for records may be made at any office of the Internal Revenue Service. A request delivered to an office in person must be delivered during the regular office hours of that office. The person making the request should allow a reasonable period of time for processing the request.

(4) Identification of records. The request for records must describe the records in reasonably suffcient detail to enable personnel of the Interal Revenue Service to locate the records. While no specific formula for adequate identification of a record may be established, it will generally suffice if the requester gives the name, subject matter, and, if known, the date aand location of the requested record. However, the person making the request is advised to furnish the Internal Revenue Service with any additional information which will more clearly identify the requested records, since he has the burden of properly identifying them. The identification requirement will not be used by

officers or employees of the Internal Revenue Service as a device for improperly withholding records from the public.

(5) Fees. A schedule of fees for the services and costs required of the Internal Revenue Service in locating, making available, copying, and certifying records pursuant to this paragraph is as follows:

Record search; each hour or fraction thereof	$3.50
Photocopies: each page	.10
Certification of photocopies by appropriate official; each certification	1.00
Minimum charge with respect to photocopies	1.00

If the Internal Revenue Service estimates that the total fees for costs incurred in complying with the request will amount to $50 or more, the person making the request may be required to enter into a contract for the payment of actual fees with respect to the request before the Service will undertake actions necessary to comply with the request.

(6) Processing a request—(i) In general. The person making a request will be promptly advised in writing that the request has been received, that action is being taken thereon, and that he will be notified in writing of the determination as to whether the request is granted. If the request does not sufficiently identify a record, the person making the request will be promptly advised of such fact and notified that a more detailed description of the record is required by the Internal Revenue Service in order to proceed with the request.

(ii) Determination by National Office. Except in a case described in subdivision (iii) of this subparagraph, a request sufficiently identifying records will be immediately transmitted to the Assistant Commissioner (Compliance), Attention: CP:D for prompt consideration. A copy of the requested records or a description thereof will also be transmitted to the Assistant Commissioner (Compliance) for consideration in connection with the request. The Assistant Commissioner (Compliance) will notify the requester in writing of his determination with respect to the request.

(iii) Determination by a field office. Where disclosure authorization with respect to the requested records has been delegated to an officer or employee of the Internal Revenue Service other than the Assistant Commissioner (Compliance), such other officer or employee will make the determination as to whether the request for records should be granted or denied and will notify the requester in writing of his determination with respect to the request.

(7) Granting of request. If it is determined that the request is to be granted, the person making the request will be notified in writing of the determination, of the fees involved in complying with the request, and of the locations where such fees are payable. Upon receipt by the Internal Revenue Service of the fees stated in its reply, the person making the request will be promptly advised, in writing, of the time and place where inspection may be made; or, if he has requested that a copy of the records be sent to him without first inspecting the records or if it has been necessary to reproduce the records in order to provide for inspection, a copy of the records will be mailed to him for his retention. In the usual case, the records will be made available for inspection at the office of the Internal Revenue Service where the request was made. However, if the person making the request has expressed a desire to inspect the records at an office of the Service other than the office where the request was made, every reasonable effort will be made to comply with the request. Records will be made available for inspection at such reasonable and proper times as not to interfere with their use by the Internal Revenue Service or to exclude other persons from making inspections. In addition, reasonable limitations may be placed on the number of records which may be inspected by a person on any given date. The person making the request will not be allowed to remove the records from the office where inspection is made. If, after making inspection, the person making the request desires copies of all or a portion of the requested records, copies will be furnished to him upon payment of the established fees prescribed by subparagraph (5) of this paragraph. Prepayment of fees is not required where the total fees with respect to the request are $5 or less and the request is filled by mail.

(8) Denial of request. If it is determined that the request for records should be denied, the person making the request will be notified of such de-

termination by mail. The letter of notification will specify the city or other location where the requested records are situated, contain a brief statement of the grounds for denial, and advise the requester of his right to appeal to the Commissioner in accordance with subparagraph (9) of this paragraph.

(9) Administrative appeal. At any time within 30 days after the date of the letter of notification described in subparagraph (8) of this paragraph, the person making the request may file an appeal to the Commissioner. The appeal must be in the form of a statement signed by the appellant and mailed to the Commissioner of Internal Revenue, 1111 Constitution Avenue NW., Washington, D.C. 20224. The statement must contain the following information:

(i) The appellant's name and address,

(ii) The identification of the records requested,

(iii) The date of the request and the date of the letter denying the request, and

(iv) A request that the Commissioner consider the denial.

The appeal will be promptly considered by the Commissioner and the request either granted or denied by the Commissioner or referred by him to the Secretary for determination. The appellant will be notified of the determination by mail, and such determination shall be final.

(10) Judicial review. If the request is denied upon appeal pursuant to subparagraph (9) of this paragraph, or if no determination is made on the appeal within 30 days after filing, the appellant may commence an action in a U.S. district court pursuant to 5 U.S.C.A. § 552(a)(3). The statute authorizes an action only against the agency. With respect to records of the Internal Revenue Service, the agency is the Internal Revenue Service, not an officer or employee thereof. Service of process in such an action shall be in accordance with the Federal Rules of Civil Procedure (28 U.S.C.A.App.) applicable to actions against an agency of the United States. Where provided in such Rules, delivery of process upon the Internal Revenue Service must be directed to the Commissioner of Internal Revenue: Attention: CC:OP:OS, 1111 Constitution Avenue NW, Washington, D.C. 20224. The district court will determine the matter de novo, and the burden will be upon the Internal Revenue Service to sustain its action in not making the re quested records available.

(d) Rules for disclosure of certain specified matters—(1) Inspection of certain tax returns. The inspection of certain returns is governed by the provisions of the internal revenue laws and rules promulgated by the President or by the Secretary of the Treasury and approved by the President pursuant to such provisions. See section 6103 and the regulations thereunder in Part 301 of this chapter (Procedure and Administration Regulations).

(2) Information as to persons filing income tax returns. Informations as to whether any person has filed an income tax return for a particular taxable year will be furnished to an inquirer. See section 6103(f).

(3) Record of seizure and sale of real estate. Record 21, "Record of seizure and sale of real estate',, is open for public inspection in offices of district directors and copies are furnished upon application, as provided in § 301.9000–1 (e) of this chapter. However, Record 21 does not list real estate seized for forfeiture under the internal revenue laws (see sec. 7302).

(4) Public lists of mployers making returns under the Federal Unemployment Tax Act. Information as to whether an employer has made an annual return on Form 940 under the Federal Unemployment Tax Act (chapter 23 of the Code) will be furnished to an inquirer. See sections 6103(f) and 6106.

(5) Information returns of certain tax-exempt organizations and certain trusts. Information furnished on Form 990, Form 1041–A, and on the annual report by private foundations pursuant to sections 6033, 0634, and 6056, which are filed after December 31, 1969, is available for public inspection for a 4-year period. This information shall be available for public inspection in the office of the Director, Public Affairs Division, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC 20224, as well as in the office of a district director or Director of the Mid-Atlantic Regional Service Center. See section 6104(b) and § 301.6104–2 of this chapter.

(6) Applications of certain organizations for tax exemption. Applications, and certain papers submitted in support of such applications, filed by organizations described in section 501(c) or (d) and determined to be exempt from

taxation under section 501(a) are open to public inspection in the Office of the Director, Public Affairs Division, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC 20224. Copies of such applications filed after September 2, 1958, are open to public inspection in the offices of district directors. See section 6104(a) and § 301.6104–1 of this chapter.

(7) Accepted offers in compromise. For a period of 1 year, a copy of the Abstract and Statement for each accepted offer in compromise in respect of income, profits, capital stock, estate, or gift tax liability is made available for inspection (a) in the Office of the Director, Public Affairs Division, Internal Service, 1111 Constitution Avenue NW., Washington, DC 20224, when the offer covers a liability of $5,000 and over, and (b) in the office of the appropriate district director when the offer covers a liability of less than $5,000. See § 301.6103(a)–1(j) of this chapter and section 10 of Rev. Proc. 64–44 (C.B. 196–2, 974, 979).

Information will not be disclosed, however, concerning any trade secrets, processes, operations, style of work or apparatus, or confidential data or any other matter within the prohibition of U.S.C. 1905.

(8) Publication of statistics of income. Statistics with respect to the operation of the income tax laws are published annually in accordance with section 6108 and § 301.6108–1 of this chapter.

(9) Comments received in response to a notice of proposed rulemaking. Written comments received in response to a notice of proposed rulemaking may be inspected by any person upon compliance with the provisions of this subparagraph (9) unless such comments are exempt from disclosure under law. Comments which may be inspected are located in the Office of the Chief Counsel, Legislation and Regulations Division, Technical Section, Room 4317, 1111 Constitution Avenue, Washington, D.C. 20224. The request to inspect comments must be in writing and signed by the person making the request and should be addressed to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224. Upon delivery of such a written request to the place where the comments are located during the regular business hours of that office, the person making the request may inspect those comments (or portions thereof) which are not exempt from disclosure. Copies of comments (or portions thereof) which are not exempt from disclosure may be obtained by a written request addressed to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224. The person making the request for copies should allow a reasonable time for processing the request. The provisions of paragraph (c)(5) of this section, relating to fees, shall apply with respect to requests made in accordance with this subparagraph. The provisions of this subparagraph shall apply in the case of requests for the inspection of, or copies of comments that are made after April 29, 1973, regardless of when the comments were submitted or regardless of when the related notice of proposed rulemaking was published in the FEDERAL REGISTER.

(e) Other disclosure procedures. For procedure to be followed by officers and employees of the Internal Revenue Service upon receipt of a request or demand for certain internal revenue records or information the disclosure procedure for which is not covered by this section, see § 301.9000–1 of this chapter.

As amended May 10, 1958, 23 F.R. 3125; Feb. 14, 1959, 24 F.R. 1157; Dec. 28, 1960, 25 F.R. 13766; July 29, 1961, 26 F.R. 6813; Dec. 29, 1961, 26 F.R. 12688; Mar. 26, 1963, 28 F.R. 2955; Feb. 17, 1966, 31 F.R. 2832; July 1, 1967, 32 F.R. 9543; May 4, 1968, 33 F.R. 6819; Apr. 12, 1969, 34 F.R. 6433; Sept. 19, 1969, 34 F.R. 14604; May 6, 1970, 35 F.R. 7117; Apr. 22, 1971, 36 F.R. 7587, 8149; Feb. 23, 1973, 38 F.R. 4973; Mar. 30, 1973, 38 F.R. 8246.

MISCELLANEOUS PROVISIONS

§ 301.6104 Statutory provisions; publicity of information required from certain exempt organizations and certain trusts.

SEC. 6104. *Publicity of information required from certain exempt organizations and certain trusts*—(a) *Inspection of applications for tax exemption*—(1) *Public inspection*—(A) *In general.* If an organization described in section

501 (c) or (d) is exempt from taxation under section 501 (a) for any taxable year, the application filed by the organization with respect to which the Secretary or his delegate made his determination that such organization was entitled to exemption under section 501 (a), together with any papers submitted in support of such application, shall be open to public inspection at the national office of the Internal Revenue Service. In the case of any application filed after the date of the enactment of this subparagraph, a copy of such application shall be open to public inspection at the appropriate field office of the Internal Revenue Service (determined under regulations prescribed by the Secretary or his delegate). Any inspection under this subparagraph may be made at such times, and in such manner, as the Secretary of his delegate shall be regulations prescribe. After the application of any organization has been opened to public inspection under this subparagraph, the Secretary or his delegate shall, on the request of any person with respect to such organization, furnish a statement indicating the subsection and paragraph of section 501 which it has been determined described such organization.

(B) *Withholding of certain information.* Upon request of the organization submitting any supporting papers described in subparagraph (A), the Secretary or his delegate shall withhold from public inspection any information contained therein which he determines relates to any trade secret, patent, process, style of work, or apparatus, of the organization, if he determines that public disclosure of such information would adversely affect the organization. The Secretary or his delegate shall withhold from public inspection any information contained in supporting papars described in subparagraph (A) the public disclosure of which he determines would adversely affect the national defense.

(2) *Inspection by committees of Congress.* Section 6103 (d) shall apply with respect to—

(A) The application for exemption of any organization described in section 501 (c) or (d) which is exempt from taxation under section 501 (a) for any taxable yera, and

(B) Any other papers which are in the possession of the Secretary or his delegate and which relate to such application, as if such papers constituted returns.

(b) *Inspection of annual information returns.* The information required to be furnished by sections 6033, 6034, and 6056, together with the names and addresses of such organizations and trusts, shall be made available to the public at such times and in such places as the Secretary or his delegate may prescribe. Nothing in this subsection shall authorize the Secretary or his delegate to disclose the name or address of any contributor to any organization or trust (other than a private foundation, as defined in section 509(a)) which is required to furnish such information.

(c) *Publication of State officials*—(1) *General rule.* In the case of any organization which is described in section 501(c)(3) and exempt from taxation under section 501(a), or has applied under section 508(a) for recognition as an organization described in section 501(c)(3), the Secretary or his delegate at such times and in such manner as he may by regulations prescribe shall—

(A) Notify the appropriate State officer of a refusal to recognize such organization as an organization described in section 501(c)(3), or of the operation of such organization in a manner which does not meet, or no longer meets, the requirements of its exemption,

(B) Notify the appropriate State officer of the mailing of a notice of deficiency of tax imposed under section 507 or chapter 42, and

(C) At the request of such appropriate State officer, make available for inspection and copying such returns, filed statements, records, reports, and other information, relating to a determination under subparagraph (A) or (B) as are relevant to any determination under State law.

(2) *Appropriate State officer.* For purposes of this subsection, the term "appropriate State officer" means the State attorney general, State tax officer, or any State official charged with overseeing organizations of the type described in section 501(c)(3).

(d) *Public inspection of private foundations' annual reports.* The annual report required to be filed under section 6056 (relating to annual reports by private foundations) shall be made available by the foundation managers for inspection at the principal office of the foundation during regular business hours by any citizen on request made within 180 days after the publication of notice of its availability. Such notice shall be published, not later than the day prescribed for filing such annual report (determined with regard to any extension of time for filing), in a newspaper having general circulation in the county in which the principal office of the private foundation is located. The notice shall state that the annual report of the private foundation is available at its principal office for inspection during regular business hours by any citizen who requests it within 180 days after the date of such publication, and shall state the address of the private foundation's principal office and the name of its principal manager.

[Sec. 6104 as amended by sec. 75(a), Technical Amendments Act 1958 (72 Stat. 1660), secs. 101(e) and 101(j)(36), Tax Reform Act 1969 (83 Stat. 523)]

§ 301.6104-1 Public inspection of applications for tax exemption.

(a) *Applications open to inspection*—(1) *In general.* An application for exemption, together with any supporting documents, filed by an organization described in section 501 (c) or (d) (or in the corresponding provisions of any prior revenue law) shall be open to public inspection on or after November 3, 1958, in accordance with section 6104(a)(1) and the provisions of this section, if the Commissioner or district director has determined, on the basis of such application, that such organization is exempt from taxation for any taxable year under section 501(a) (or under the corresponding provisions of any prior revenue law). Certain applications for exemption have been destroyed pursuant to Congressional authorization and therefore will not be available for inspection.

(2) *Claim for exemption filed under section 503 or 504 and the regulations thereunder.* Claims for exemption filed to reestablish exempt status after denial thereof under the provisions of section 503 or 504 (or under the corresponding provisions of any prior revenue law), relating to denial of exemption because of certain prohibited transactions or an unreasonable accumulation of income, are considered to be applications for exemption for purposes of section 6104 (a) (1) and this section.

(3) *Requirement of exempt status.* An application for exemption and supporting documents shall not be available for public inspection before the organization filing such application has been determined, on the basis of such application, to be exempt from taxation for any taxable year. On the other hand, if the organization has been determined to be exempt for any taxable year, the application for exemption with respect to which such determination was made shall not be withheld from public inspection on the grounds that such organization is determined not to be entitled to exemption for any other taxable year or years.

(b) *Meaning of terms*—(1) *Application for exemption.* (i) For purposes of this section, the term "application for exemption" means the documents described in subdivision (ii) of this subparagraph which the organization was required to file when it applied for exemption.

(ii) (*a*) With respect to an organization for which an application for exemption form is prescribed, the application for exemption includes such form and all documents and statements required to be filed by such form.

(*b*) With respect to an organization described in section 501 (c) or (d) for which no application for exemption form is prescribed, the application for exemption includes the application letter and a conformed copy of the articles of incorporation, declaration of trust, or other instrument of similar import, setting forth the permitted powers or activities of the organization, the bylaws or other code of regulations, and the latest financial statement showing the assets, liabilities, receipts, and disbursements of the organization, and statements showing the character of the organization, the purpose for which it was organized, its actual activities, source of income and receipts and the disposition thereof, and weather or not any of its income or receipts is credited to surplus or may insure to the benefit of any private shareholder or individual.

(c) With respect to a mutual insurance company, the application for exemption shall, in addition to the statements and documents required to be submitted by the form, include copies of the policies or certificates of membership issued by such company.

(d) With respect to a title holding company described in section 501 (c) (2), if the organization for which title is held has not been specifically notified in writing by the Internal Revenue Service that it is held to be exempt under section 501 (a), the application for exemption shall, in addition to the statements and documents required to be submitted by the form, include the statements or documents which would be considered to be included in the application for exemption of the organization for which title is held.

(e) With respect to a State chartered credit union described in section 501 (c) (14), the application for exemption shall, in addition to the statements and documents indicated in (b) of this subdivision, include a statement indicating the State and date of incorporating and showing that the State credit union law with respect to loans, investments, and dividends, if any, is being complied with.

(f) With respect to an organization which is described in section 501(c)(3) and which files its application for exemption after July 26, 1959, the application for exemption shall, in addition to the statements and documents required to be submitted by the form, include a detailed statement of the proposed activities of such organization.

(iii) The term "application for exemption" does not include a request for a ruling as to whether a proposed transaction is a prohibited transaction under section 503 (or under the corresponding provisions of any prior revenue law).

(2) *Supporting document.* For purposes of this section, the term "supporting document" means any statement or document submitted by an organization in support of its application for exemption which is not specifically required by subdivision (ii) of subparagraph (1) of this paragraph. For example, a legal brief submitted in support of an application for exemption is a supporting document.

(c) *Withholding of certain information*—(1) *Trade secrets, patents, processes, styles of work, or apparatus*—(i) *In general.* Any information which is submitted by an organization whose application for exemption is open to inspection under this section and which is determined by the Commissioner to relate to any trade secret, patent, process, style of work, or apparatus of the organization submitting such information shall, upon request in writing of such organization, be withheld fro mpublic inspection under section 6104 (a) (1) and this section, if the Commissioner determines that the disclosure of such information would adversely affect the organization.

(ii) *Request for withholding of information.* Requests for the withholding of information from public inspection as provided in subdivision (i) of this subparagraph shall—

(a) In the case of applications for exemption filed before November 3, 1958, be made to the Commissioner of Internal Revenue, Attention: Public Information Division, Washington 25, D. C.; or

(b) In the case of applications for exemption filed on or after November 3, 1958, be filed with the office with which the taxpayer filed the documents in which the material to be withheld is contained.

The request shall clearly identify the material desired to be withheld (the document, page, paragraph, and line) and shall include the reasons for the organization's position that the information is of the type which may be withheld from public inspection.

(iii) *Determination.* An organization which has filed a request under the provisions of this subparagraph will be notified of the determination as to whether the information to which the request relates will be withheld from public inspection.

(2) *National defense material.* The Internal Revenue Service shall withhold from public inspection any information which is submitted by an organization whose application for exemption is open to inspection under this section the public disclosure of which the Commissioner determines would adversely affect the national defense.

(d) *Place of inspection.* Applications for exemption, together with any supporting documents, which are open to public inspection under section 6104 (a) (1) shall be available for inspection on or after November 3, 1958, in the Office of the Director, Public Information Division, Internal Revenue Service, Washington 25, D. C., regardless of when or where such applications were filed except for such applications as have been destroyed pursuant to Congressional authority. In addition, in the case of an application for exemption filed on or after September 3, 1958, a copy of such application (as defined in paragraph (b)(1) of this section), but not the supporting documents, shall also be available for public inspection on or after November 3, 1958, in the office of the district director with whom the application was required to be filed.

(e) *Procedure for public inspection of applications for exemption*—(1) *Request for inspection.* Applications for exemption and the supporting documents shall be available for public inspection only upon request. If inspection at the national office is desired, the request shall be made in writing to the Commissioner of Internal Revenue, Attention: Director, Public Information Division, Washington 25, D.C. Requests for inspection in the office of a district director shall be made in writing to the appropriate district director. All requests for inspection must include the name and address of the organization which filed the application for exemption the inspection of which is requested. In addition, is such organization has more than one application for exemption open to public inspection under the provisions of section 6104 (a)(1) only the most recent of such applications shall be made available for inspection unless the request for inspection specifically states otherwise.

(2) *Time and extent of inspection.* A person requesting public inspection in the manner specified in subparagraph (1) of this paragraph shall be notified by the Internal Revenue Service when the material he desires to inspect will be made available for his inspection. An application for exemption will be made available for public inspection at such reasonable and proper times as not to interfere with its use by the Internal Revenue Service or to exclude other persons from inspecting it. In addition, the Commissioner or district director may limit the number of applications for exemption to be made available to any person for inspection on a given date. The public inspection authorized by section 6104(a)(1) will be allowed only in the presence of an internal revenue officer or employee and only during the regular hours of business of the Internal Revenue Service office.

(3) *Copies.* Notes may be taken of the material opened for inspection under this section, and copies may be made manually but not photographically. Copies of such material will be furnished by the Internal Revenue Service to any person making request therefor. Requests for such copies shall be made in the same manner as requests for inspection (see subparagraph (1) of this paragraph) to the office of the Internal Revenue Service in which such material is available for inspection as provided in paragraph (d) of this section. If made at the time of inspection, the request for copies need not be in writing. Any copies furnished will be certified upon request. The Commissioner may prescribe a reasonable fee for furnishing copies of applications and supporting documents pursuant to this section.

(f) *Statement of exempt status.* A statement setting forth the following information with respect to an organization shall be furnished to any person upon request in writing, after the application for exemption of such organization is open to public inspection under section 6104(a)(1):

(1) The subsection and paragraph of section 501 (or the corresponding provision of any prior revenue law) under which the organization has been determined, on the basis of such application, to qualify for exemption from taxation; and

(2) Whether the organization is currently held to be exempt.

Request for such information may be made in writing to the Commissioner of Internal Revenue, Attention: Public Information Division, Washington 25, D.C., or to the district director with whom the organization's application for exemption was required to be filed.

§ 301.6104–2 Publicity of information on certain information returns and annual reports.

(a) *In general.* The following information, together with the name and address of the organization or trust furnishing such information, shall be a matter of public record:

(1) Except as otherwise provided in section 6104 and the regulations thereunder, the information required by section 6033 and the information furnished on Form 4720.

(2) The information furnished pursuant to section 6034 (relating to returns by certain trusts) on Form 1041–A.

(3) The information furnished on the annual report required by section 6056 (relating to annual reports of private foundations). The names, addresses, and amounts of contributions or bequests of contributors to an organization other than a private foundation shall not be made available for public inspection under section 6104(b). The names, addresses, and amounts of contributions or bequests of persons who are not citizens of the United States to a foreign organization described in section 4948(b) shall not be made available for public inspection under section 6104(b).

(b) *Place of inspection.* Information furnished on the public portion of returns and annual reports (as described in paragraph (a) of this section) shall be available to any person in the National Office, Office of the Director, Public Information Division, Internal Revenue Service, Washington, D.C. 20224, in the Office of the Director, Mid-Atlantic Regional Service Center, Philadelphia, Pa., and in the office of the district director of the district serving the principal place of business of the organization.

(c) *Procedure for public inspection*—(1) *Requests for inspection.* The information furnished pursuant to section 6033 and 6034, the annual report required by section 6056, and Form 4720 shall be available for public inspection under section 6104(b) only upon request. If inspection at the National Office is desired, the request shall be made in writing to the Commissioner of Internal Revenue, Attention: Director, Public Affairs Division, Washington, D.C. 20224. Requests for inspection in the office of a district director or Director of the Internal Revenue Service Center, Philadelphia, Pennsylvania, shall be made in writing to the district director or Director of the Service Center. All requests for inspection must include the name and address of the organization which filed the return or report, the type of return or report, and the taxable year for which filed, except that requests for inspection of entire sections of the microfilm file need only designate the appropriate section desired.

(2) *Time and extent of inspection.* A person requesting public inspection in the manner specified in subparagraph (1) of this paragraph shall be notified by the Internal Revenue Service when the material he desires to inspect will be made available for his inspection. Information on returns required by sections 6033 and 6034, the annual report required by section 6056 and the information furnished on Form 4720 will be made available for public inspection at such reasonable and proper times, and under such conditions, that will not interfere with their use by the Internal Revenue Service and will not exclude other persons from inspecting them. In addition, the Commissioner, Director of the Service Center, or district director may limit the number of returns to be made available to any person for inspection on a given date. Inspection will be allowed only in the presence of an internal revenue officer or employee and only during the regular hours of business of the Internal Revenue Service office.

(3) *Returns available.* Returns filed before January 1, 1970, shall be available for public inspection only pursuant to the provisions of section 6104 in effect for such years. The information furnished on all returns and reports filed after December 31, 1969, pursuant to the requirements of section 6033, 6034, or 6056, shall be available for public inspection in accordance with the provisions of section 6104.

(4) *Copies.* Notes may be taken of the material opened for inspection under this section. Copies may be made manually or photographically in the National Office subject to reasonable supervision by the Public Information Division with regard to the facilities and equipment to be employed; and copies may be

made manually but not photographically in the offices of the district directors or directors of regional service centers (except that copies may be made photographically at the Mid-Atlantic Regional Service Center). Copies of the material opened for inspection will be furnished by the Internal Revenue Service to any person making request therefor. Request for such copies shall be made in the same manner as requests for inspection (see subparagraph (1) of this paragraph) to the office of the Internal Revenue Service in which such material is available for inspection as provided in paragraph (b) of this section. If made at the time of inspection, the request for copies need not be in writing. Any copies furnished will be certified upon request. The Commission may prescribe a reasonable fee for furnishing copies of information pursuant to this section.

§ 301.6104-3 Disclosure of certain information to State officers.

(a) *Notification of determinations*—(1) *Automatic notification.* Upon making a determination described in paragraph (c) of this section the Internal Revenue Service will notify the Attorney General and the principal tax officer of each of the following States of such determination without application or request by such State officer—

(i) In the case of any organization described in section 501(c)(3), the State in which the principal office of the organization is located (as shown on the last-filed return required by section 6033, or on the application for exemption if no return has been filed), and the State in which the organization was incorporated, or if a trust, in which it was created, and

(ii) In the case of a private foundation, each State which the organization was required to list as an attachment to its last-filed pursuant to § 1.6033-2(a)(2)(iv).

(2) *Applications for notification by other State Officers.* Other officers of States described in subparagraph (1) of this paragraph, and officers of States not described in such subparagraph, many request that they be notified (either generally or with respect to a particular organization or type of organization) of determinations described in paragraph (c) of this section. In such cases, these State officers must show that they are appropriate State officers within the meaning of section 6104(c)(2). The required showing may be made by presenting a letter from the Attorney General of the State setting forth (i) the functions and authority of the State officer under State law, and (ii) sufficient facts for the Internal Revenue Service to determine that such officer is an appropriate State officer within the meaning of section 6104(c)(2).

(3) *Manner of notification.* A State officer who is entitled to be notified of a determination under this paragraph will be notified by sending him a copy of the communication from the Internal Revenue Service to the organization which informs such organization of the determination.

(b) *Inspection by State Officers*—(1) *In general.* After a determination described in paragraph (c) of this section has been made appropriate State officers within the meaning of section 6104(c)(2) may inspect the material described in subparagraph (3) of this paragraph. Such material may be inspected at an office of the Internal Revenue Service which will be designated upon receipt of a request for inspection; the location of such office will be determined with due consideration of the needs of the Internal Revenue Service and the needs of the State officer entitled to inspect.

(2) *State officers who may inspect material.* Any State officer entitled to be notified of a determination without application (under paragraph (a)(1) of this section) may inspect the material described in subparagraph (3) of this paragraph upon demonstrating that he is so entitled. Any State officer who has in fact been notified by the Internal Revenue Service of a determination may inspect such material without further demonstration, unless it shall be determined by the Internal Revenue Service that such officer was not entitled to be so notified. Other State officers must demonstrate to the satisfaction of the Internal Revenue Service that they are entitled to be notified under paragraph (a)(2) of this section before they may inspect such material.

(3) *Material which may be inspected.* (i) Except as provided in subdivision (ii) of this subparagraph, a State officer who is so entitled under subparagraphs (1) and (2) of this paragraph will be permitted to inspect and copy all

returns, filed statements, records, reports, and other information relating to a determination described in paragraph (c) of this section which is relevant to a determination under State law, and which is in the hands of the Internal Revenue Service.

(ii) The following material will not be made available for inspection by State officers under section 6104(c) and this section—

(*a*) Interpretations by the Internal Revenue Service or other federal agency of federal laws (including the Internal Revenue Code of 1954 and its predecessors) which would not otherwise be made available to State officers under section 6103(b),

(*b*) Reports of informers, or any other material which would disclose the identity, or threaten the safety or anonymity, of an informer,

(*c*) Returns of persons (other than those exempt from taxation) which would not be available under section 6103 (b) to the State officer requesting inspection, or

(*d*) Other material the disclosure of which the Commissioner has determined would prejudice the proper administration of the internal revenue laws.

(4) *Statement by State Officer.* Before any State officer will be permitted to inspect material described in this paragraph, he must submit a statement to the Internal Revenue Service that he intends to use such material solely in fulfilling his functions under State law relating to organizations of the type described in section 501(c)(3); material is made available to State officers under this section in reliance on such statements. For provisions relating to penalties for misuse of information which is made available under section 6104(c) and this section, see 18 U.S.C. 1001.

(c) *Determinations defined.* For purposes of this section, a determination means a final determination by the Internal Revenue Service that—

(1) An organization is refused recognition as an organization described in section 501(c)(3), or has been operated in such a manner that it will not, or will no longer, be recognized as meeting the requirements for exemption under that section, or

(2) A deficiency of tax exists under section 507 or chapter 42.

For purposes of this paragraph, a determination by the Internal Revenue Service is not final until all administrative review with respect to such determination has been completed. For purposes of this section, a waiver of restrictions on assessment and collection of deficiency in tax is treated as a final determination that a deficiency of tax exists when such waiver has been finally accepted by the Internal Revenue Service. For example, a final determination that a deficiency of tax exists under section 507 or chapter 42 is made when the organization is sent a notice of deficiency with respect to such tax.

(d) *Effective date.* The provisions of this section apply with respect to all determinations made after December 31, 1969.

§ 301.6104–4 Public inspection of private foundations' annual reports.

(a) *In general.* The annual report which a private foundation must file under section 6056 shall be made available by its foundation managers for inspection at its principal office during regular business hours by any citizen on request made within 180 days after the publication of notice of the availability of such report. Such notice shall be published not later than the day prescribed for filing such report (determined with regard to any extension of time for filing) in a newspaper having general circulation in the county in which the foundation's principal office is located. The notice shall state that the annual report is available at the foundation's principal office for inspection during regular business hours by any citizen who requests inspection within 180 days after the date of such publication, and shall state the address of the foundation's principal office and the name of its principal manager.

(b) *Definitions and special rules*—(1) *Principal office.* For purposes of the notice described in section 6104(d), a private foundation may designate in addition to its principal office, or (if the foundation has no principal office or none other than the residence of a substantial contributor or foundation manager) in lieu of such office, any other location at which its annual report shall be made available in the manner and at the time prescribed therefor in section 6104(d).

(2) *Newspaper having general circulation.* The term "newspaper having general circulation" in section 6104(d) shall include any newspaper or journal which is permitted to publish statements in satisfaction of State statutory requirements relating to transfers of title to real estate or other similar legal notices.

(3) *Principal manager.* A private foundation may furnish the name of its "principal manager" in the notice required by section 6104(d) by furnishing the name of the individual foundation manager who is responsible for publishing such notice or for making the annual report available for inspection under section 6104(d).

(c) *Cross-reference.* For additional rules with respect to private foundations' annual reports and their public inspection, see section 6056 and the regulations thereunder.

Senator HARTKE. Mr. Alexander.

STATEMENT OF DONALD C. ALEXANDER, COMMISSIONER OF THE INTERNAL REVENUE SERVICE; ACCOMPANIED BY LAWRENCE B. GIBBS, ASSISTANT COMMISSIONER (TECHNICAL); JOSEPH TEDESCO, CHIEF OF THE EXEMPT ORGANIZATION BRANCH OF THE MISCELLANEOUS AND SPECIAL TAX DIVISION; HOWARD SCHOENFELD, CHIEF OF PROCEDURES SECTION EXEMPT ORGANIZATION EXAMINATION BRANCH, AUDIT DIVISION; ROBERT McCAULEY, CHIEF OF THE EXEMPT ORGANIZATION EXAMINATION BRANCH

Mr. ALEXANDER. Mr. Chairman, we have no prepared statement. I am glad to be with you this afternoon.

I would like to introduce my colleagues. On my immediate left is Lawrence Gibbs, Assistant Commissioner—Technical. On his left is Joseph Tedesco, who is Chief of Exempt Organization Branch of Miscellaneous and Special Tax Division in Mr. Gibbs' office. On my immediate right is Howard Schoenfeld, who put much of the reply to your questions together, and he is in Exempt Organization Examination Branch in our Audit Division under our Assistant Commissioner—Compliance; Mr. Robert McCauley, who is Chief of the Exempt Organization Examination Branch, is also here to the right rear of Mr. Schoenfeld.

I would like to call to your attention, Mr. Chairman, the letter submitted to you today by the Secretary of the Treasury in response to a question with respect to the relationship of the tax on private foundation investment income under section 4940 of the Code and the cost of the activities of the Internal Revenue Service in connection with administering the provisions with respect to all exempt organizations as well as private foundations.

This letter concludes by stating, Mr. Chairman, that the Treasury would support a measure to reduce the tax under section 4940 of the Code from 4 to 2 percent. Mr. Chairman, we would like to make a part of the record, as I understand to be the case, the letter dated May 30 in which I replied to the list of questions you posed on March 22 and the document entitled, "Background Material for Senator Hartke" which is attached to that letter. We will be glad to explain and clarify and develop any of the answers that we have made to your questions. We will be glad to go through the material

which we have submitted and answer any further questions that you may have.

Senator HARTKE. All right.

In your statement itself, in answer to the questions you tell us that you cannot give us an indication of anything more than the net additions to the list of exempt organizations since 1969.

Is it not possible to tell us how many rulings IRS has given which granted exempt status since 1969?

Mr. ALEXANDER. Mr. Chairman, I will ask Mr. Gibbs and Mr. Tedesco to respond to this issue after asking Mr. Schoenfeld to clarify the response that we have already made.

Mr. Schoenfeld?

Mr. SCHOENFELD. Thank you.

You asked if it is possible to tell the number of additions made since 1969. I assume you are referring to just private foundation additions. There are a number of problems that we have in this regard.

First, we have a lot of organizations which were unclassified until the regulations pertaining to the definition of a private foundation became final. This was not until, generally speaking, March of 1973. We had a lot of organizations that may have gone out of existence. If an organization that was in exixstence before 1969 considers itself to be a private foundation, we are not required to give that organization a ruling as it is not required they ask us for one. We simply assume that it is unless we hear from the organization otherwise. For this reason, it has not been possible to make a precise count since 1969 that would show the additions——

Senator HARTKE. The regulations were not finalized until 1973, is that right?

Mr. SCHOENFELD. At different stages; yes, sir.

Mr. ALEXANDER. Some of the regulations still are not finalized, Mr. Chairman.

Senator HARTKE. Let me come back to the letter in a moment.

What has been the problem?

Why has it been difficult to finalize the regulation?

Mr. ALEXANDER. I do not think you find any of us eager to take the microphone in response to that question, Mr. Chairman, so I will.

Part of the problem which, of course, started in 1969 when you had a different group of faces in these spots before you, and developed from the very great complexity of the 1969 Tax Reform Act provisions relating to exempt organizations in general and to private foundations in particular. As a practitioner in the field at the time that these provisions became law and at a time when many of the regulations were proposed, I grappled with some of these complexities in an effort to try to understand what the law really required for compliance by my clients. Now I am trying to understand what the law really requires of us for administering these provisions effectively, fairly, and responsively.

For we have a regulatory duty to perform here rather than a tax collecting duty, and we have a regulatory duty in an area which perhaps is the greatest single morass in the English language. Now,

that is not an effort to be caustic at the expense of the drafters. The drafters, I think, did a fine job in trying to cope with solving a very difficult problem of meshing duties on one hand with equities on the other, making sure that the statute reached what it should reach but did not overreach, entering into a new definitional area by having such statements as one which, in trying to bring support organizations for C(4)'s into the law, managed to create a sentence that all of us treasure and which I can supply for the record.

Now, we have had some problems in producing regulations which carried out the intent of the statute and at the same time would not in turn overreach and would recognize equities. We did recognize that we have a duty to understand that the law should not put all charities in a straightjacket, should not insist that the only thing a foundation can do is take the safe action when another action, perhaps not so safe, would be better for the community and better to serve the interest of the community, the State, and the Federal Government. That is the condition, I suppose the purpose, of tax exemption in the first place.

We have been slow in getting these regulations finalized. I wish we had been able to do this job faster. In certain cases the provision does not take effect, or did not take effect, for a substantial period of time after enactment. Section 4943, I suppose, is an example. Accordingly, those regulations were given fairly low priority on the list of priorities that our predecessors produced after the 1969 act.

I signed off on a proposed regulation, I hope one of the finals, Saturday afternoon in this area.

Senator HARTKE. Is that because these hearings were coming up?

Mr. ALEXANDER. Sir?

Senator HARTKE. Is that because these hearings were coming up?

Mr. ALEXANDER. No, that is because it was the first time it got to my desk.

Senator HARTKE. Well, let me ask you:

What seems to be the problem here?

In other words, so it is a difficult area. You know, there are a lot of difficult areas, and I grant you that this may be one of the most difficult in the English language.

But is it lack of information, lack of sufficient personnel, lack of facts, lack of understanding, lack of diligence, or is it just impossible to do?

Mr. ALEXANDER. No, I do not think it is impossible to do, Senator Hartke, and I do not think it is lack of diligence. Perhaps part of this problem is lack of sufficient hours of the week to do the jobs that certain people have, and then have the final responsibility for signing off on regulations. The work outpaces the time available to do the work. The 40-hour day has not yet been invented, but when it is I will be very happy to see it arrive.

Senator HARTKE. Let me ask you a question:

Are you saying in substance that the Congress has placed this responsibility into the hands of individuals who are already overburdened?

Mr. ALEXANDER. I am saying the individuals are overburdened in a way. I am also saying that I think they are capable of meeting these burdens. I recognize that these regulations have been delayed, and I regret that.

Mr. Gibbs, do you have anything to add to my thoughts on the subject?

Mr. GIBBS. Senator Hartke, my responsibility with the Service as Assistant Commissioner—Technical—is primarily one of having responsibilities for forms, publications, for rules, letter rulings to the taxpayers, and for revenue rulings that are to be published. And it seems to me in my experience, and I was a practitioner like the Commissioner while the legislation was passed, it seems to me that this is an occurrence that, as the Commissioner said, is complex and complex in perhaps some sort of a unique way, in the sense that especially with the excise tax provisions and the approach of using excise tax provisions to get a better enforcement—this is somewhat of a new approach by the Internal Revenue Service in terms of going into an area.

As you probably know, this is being picked up now in the pension area, and I think this is one of the reasons, with the complexity of the provisions in the new approach, that you are seeing some time lag in getting final regulations and in getting, indeed, final information that is being produced from the forms that themselves generate the information.

Senator HARTKE. Have you made any suggestions to the Congress as to how to alleviate this problem?

Mr. ALEXANDER. I think that the problem has been alleviated, Mr. Chairman, by the publication of regulations. I think we have made substantial progress, although surely not as quickly as any of us would want. I think that the public is getting much in the way of guidance, perhaps more than some would like, in these areas at this time. So I think that this problem is not one that would require any legislative solutions, because the problem itself is nearing solution by publication of final regulations. There are certain sticky problems, certain sticky questions, that remain for final decision. Those are few in number.

Most of the questions have been solved, not as early as we would have liked. Much guidance has been given. More will be forthcoming. But this problem is being resolved.

Senator HARTKE. Let me ask you, as a practical matter are we to the place now where, say within a specified period, you could really give us some answers to the questions which we submitted, which pretty generally you will have to admit, answers which said practically, we do not know?

Mr. ALEXANDER. In many cases we did say to you, Mr. Chairman, that we did not know. One of the reasons we said that was because we do not keep certain statistics which were requested from us.

Another aspect of the matter related generally to our audit and enforcement programs. We are completing one phase of the examination of private foundations. We propose to shift to, we think, a more efficient and more effective audit program which should yield

better and more comprehensive data for future questions from your committee, Mr. Chairman. We are shifting to a TCMP approach, rather than an effort which we have been making, as you know, to audit all private foundations over a 5-year period irrespective of whether those foundations really needed audit.

Senator HARTKE. Let me ask again the question in a different form that I asked you first.

Will you be able to tell us how many organizations have come into existence since the 1969 act was passed and how many have gone out of existence since 1969 at a specified period of time?

Mr. ALEXANDER. Mr. Chairman, we hope to and expect to get better data. Now, some organizations do not file with us because we exempt them from the requirement of filing. Let us take subordinate organizations of churches. We believe that one church has about 70,000 subordinates. We are not about to require 70,000 of them to file with us and secure individual exemptions.

So I cannot give a flat, unilateral answer to your question. If your question relates solely to private foundations, Mr. Chairman, we will do our best to obtain material for you which your letter of March 22 pointed out and you have pointed out this afternoon is important to this Committee.

Senator HARTKE. What you are saying in substance is that you do not know all of the organizations, so therefore we do not know what the effect of the 1969 act is, so therefore we do not know what the impact has been on revenue, we do not know how much money at the present time is being put aside and not being utilized for the purposes for which it was intended.

Is that a fair statement or is that an unfair criticism?

I saw one of your——

Mr. ALEXANDER. I think that might be a little bit of an overstatement, Mr. Chairman.

Senator HARTKE. Well, I am putting it in that form, and you straighten it out.

Mr. ALEXANDER. I will try to.

First, you are quite right. We do not know——

Senator HARTKE. You do not know.

Mr. ALEXANDER. Unless Mr. Schoenfeld wants to correct me about how many new organizations have been created.

Mr. SCHOENFELD. We will never know the number of section 501 (c)(3) organizations that come into existence, Senator.

Senator HARTKE. You never will know?

Mr. SCHOENFELD. Not under present legislation, because there are exceptions from these organizations notifying the Service that they exist. For example, a church does not have to come to the Internal Revenue Service and notify that it would like to be recognized as being tax exempt. It can go on and be tax exempt without the benefit of a ruling from the Internal Revenue Service.

Similarly, if an organization has receipts, normally not more than $5,000—little small clubs, charitable in nature—they do not have to come in and get a ruling from us either. So therefore we have no way of getting a handle on these organizations.

Senator HARTKE. Do you know about those who have filed?

Mr. SCHOENFELD. Yes, sir.

Senator HARTKE. What is that?

Mr. SCHOENFELD. The number that are in existence?

Senator HARTKE. That were in existence in 1969, those who have come into existence since that time, and those that have gone out since that time.

Mr. SCHOENFELD. As to charitable organizations, yes, sir. I think we have given you that figure. As to section 501(c)(3) organizations, not just private foundations, because before 1969 there really was not a statutory definition of a private foundation.

Mr. ALEXANDER. Mr. Chairman, referring to——

Senator HARTKE. The point of it is that the difference between a charitable organization and a private foundation, what is public charity and what is a private foundation, there is a lot of difference in the ultimate effect?

Do you agree?

Mr. SCHOENFELD. Yes, sir.

Senator HARTKE. Now, what I am trying to find—and evidently you do not know, and I guess it is sort of futile to push at this point for something you do not know—but I am trying to find out what the effect of the act was and how we can even deal with the act and how the Secretary can come in here and say that he does not need but 2-percent money to audit this in accordance with the legislation when we do not even know what we are talking about.

Is that what we are saying?

Mr. ALEXANDER. No, we are not saying that.

Senator HARTKE. In other words, let me put it in a different light.

Are we saying we did not know what we were talking about in 1969 and we know even less today?

Mr. ALEXANDER. I would doubt that. I think, Mr. Chairman, that you did not legislate in a vacuum in 1969. I am suggesting we are not talking in a vacuum today. What we seem to be hung up on, Mr. Chairman, is something that we really do not know sitting before you this afternoon. No amount, really, of further discussion on my part would conjure up knowledge where there is not the knowledge that I wolud like to have. The specific knowledge——

Senator HARTKE. All right, let me ask you: Are you planning to get that information?

Mr. ALEXANDER. We are going to try, Mr. Chairman, to get information as to terminations. I would like to point out, on page 9 of the statement we submitted to you, Mr. Chairman, as of March 31, 1974, there were 28,326 private foundations consisting of 27,301 nonoperating foundations and 1,025 operating foundations.

We do have numbers, Mr. Chairman. There is not a vacuum, Mr. Chairman. We do not have as complete numbers as we would like to have.

Mr. SCHOENFELD. And we also tell you the gross increase from 1970 to March 31, 1974.

Mr. ALEXANDER. What Mr. Schoenfeld mentioned is on page 8 of the statement.

As of March 31, 1974, there are 68,682 more section 501(c)(3) organizations on the exempt organizations master file than on January 1, 1970.

Mr. SCHOENFELD. And for the record, as of March 31, 1974, according to our records, there are 226,122 active organizations recognized as being exempt under section 501(c)(3).

Senator HARTKE. And do you know the fair market value of those assets involved in those organizations?

Mr. SCHOENFELD. I do not have that figure with me, Senator.

Senator HARTKE. Do you think you could——

Mr. ALEXANDER. Senator, I would like to refer you to page 9, the answer to question 5 that you put to us, pointing out that our exempt organizations master file shows that the book value of the assets reported by all private foundations for calendar year 1973, were in the amount of $26 billion, approximately. So we do have an aggregate. That aggregate is as stated on page 9.

Senator HARTKE. Well, is it not fair to say that within the provisions of the act, that book value does not have much meaning?

Mr. SCHOENFELD. Senator, I think as we may have explained in some prior correspondence with you, the way we gathered the information from the returns did not permit us to tabulate fair market value. Beginning in 1974, this processing year, we will be getting information as to fair market value;

Senator HARTKE. Yes, right.

Let us come now to the question of exempt classification. Organizations now are classified as to private foundations must meet stricter requirements than organizations classified as public charities. For instance, private foundations must pay the 4-percent tax, must meet the 6-percent payout requirement, must refrain from lobbying—other things of that sort—while other exempt organizations need not meet that requirement.

Now, we have asked you to tell us how many organizations are classified within each one of the separate classifications. But let me ask you this question: When we passed the act, we made an effort to assure that donors would not use the exempt status of foundations and the tax benefit from their donations for their own personal and selfish purposes.

Now, what we wanted to do was to make sure that the people did not have to wait for 10 to 20, 25 years to get the benefit from the tax subsidy that the donor got. Now is it not possible that someone could get his foundation declared a medical research organization and thereby get out from underneath the strict requirements that the law places on private foundations?

Mr. ALEXANDER. Do you want to respond to that, Mr. Gibbs?

Mr. GIBBS. Well, the response I guess I would make is this: That if—and perhaps, Mr. Chairman, I am not responding to your question, dig deeper—but it seems to me that the answer to the question is that if the classification tests for medical research facilities, which are thereby exempt from the private foundation classification, are met, that the organization would be so classified. And as long as they continue to meet those requirements under audit, that they

would continue under a classification that would relieve them from the burdens of complying with the private foundation provisions of the code.

Senator HARTKE. Are you familiar with—I am going to insert in the record at this time the Evening Journal articles under date of Tuesday, March 19, 1974, and March 29, 1974. This deals with Nemours Foundation.

[The articles referred to follow:]

[From the Wilmington, Del., Evening Journal]

WHILE PATIENTS PAY, EXPANSION STANDS STILL: NEMOURS FOUNDATION STOCKPILES $35 MILLION

(By Curtis Wilkie)

Few foundations are backed by wealth more vast than the Nemours Foundation, which was established in the will of the late Alfred I. du Pont to provide care for cripple children and the elderly.

However, the relatively modest charitable activities of the Nemours Foundation belie its potential.

The foundation's sole operation is the Alfred I. du Pont Institute outside Wilmington, a crippled children's hospital which has seen little growth since 1970 although the income of the foundation has gone up tenfold.

In the meantime, the trustees of the foundation have built up a mammoth surplus fund estimated at $35 million.

While the foundation has been stockpiling millions of dollars, up to three quarters of the patients at the Institute are being charged for services on the basis of their ability to pay.

The foundation has not only failed to broaden appreciably its services to crippled children, but it has been reluctant to diversify its operation to include care for the elderly as called for in Du Pont's will.

A month-long investigation by the Evening Journal into the affairs of the Nemours Foundation has also disclosed:

The foundation reclassified itself as a "hospital" in 1971 to avoid new regulations of the 1969 Tax Reform Act.

By slipping through a loophole in the tax law, the Nemours Foundation is avoiding more than $500,000 a year in federal excise taxes.

The Nemous Foundation, by operating as a "hospital," also escapes a provision of the tax law which prohibits the inordinate accumulation of surplus funds and forces foundations to spend a certain percentage of its assets each year. It also eludes restrictions against self-dealing, such as depositing surplus funds in the Florida First National Bank of Jacksonville, which is controlled by Edward Ball, president of the Nemours Foundation.

In order to qualify as a "hospital," the Nemours Foundation had to terminate its program of contributing to other charitable organizations leaving it with only one philanthropic outlet, the Du Pont Institute.

Although the annual income of the foundation skyrocketed from $1.2 million to more than $14 million following the dealth of Mrs. Jessie Ball du Pont in 1970, the institute's budget has not increased accordingly. Less than $3 million a year is being spent for medical services at the institute and less than $500,000 in capital expenditures have gone into the facility in the last three years.

Despite claims made in 1971 when the Nemours Foundation petitioned a Florida court for permission to expand its medical services, little has been done. A $20 million building program, which was supposed to have started at the hospital site in 1972, has never gotten off the ground.

"We have moved slowly—perhaps too slowly," concedes an official of the foundation.

However, others interviewed by the Evening Journal have less charitable judgment about the Nemours Foundation.

"Its so-called philanthropic programs have been farcical," said Waldemar A. Nielsen, author of "The Big Foundations" and an early critic of the Nemours Foundation. "The Alfred I. du Pont Institute is a philanthropic appendage to Ed Ball's empire, which he throws a few crumbs to."

A Washington tax specialist called the recent activities of the foundation "a terrible abuse" of the tax laws, although he added that it appeared to be

legal. "Ed Ball is bright enough, with that much involved, that his lawyers would have gone to great pains to dot each 'i' and cross each 't'."

The manipulation of the Nemours Foundation directly involves the Alfred I. du Pont estate, a conglomeration of corporate stocks, banks, railroad companies, paper mills and landholdings which may be worth as much as $2 billion. The Florida-based dominion is run with an iron fist by Ball, the 85-year-old brother-in-law of the late Alfred I. du Pont.

Officials of the Nemours Foundation are so intimidated by Ball that they were unwilling to discuss publicly their activities when contacted by a reporter.

In an interview at his Jacksonville office, Ball also refused to answer questions regarding the Nemours Foundation and suggested that any queries be submitted in writing to the of directors.

The board of the Nemours Foundation doubles as trustees of the estate of Alfred I. du Pont. Their first meeting in more than six months is scheduled tomorrow in Jacksonville.

The dual structure to oversee both the estate and the foundation was set up in the will of Alfred I. du Pont, which gave the trustees of his estate "full charge of the management and policy" of the foundation.

The foundation was started with a $1 million bequest after Du Pont's death in 1935. His widow was the chief beneficiary of the estate. However, the will provided that upon her death virtually all of the income from the estate would be channeled to the Nemours Foundation.

Delawareans are to get first consideration for care at the institute, according to the will.

Mrs. du Pont sustained the foundation for more than three decades by assigning 12 per cent of the income from the estate to the foundation. For example, in 1968 the income from the estate was nearly $11 million. Mr. du Pont received $9.5 million and the foundation was funded $1,144,000.

When Mrs. du Pont died in 1970, the foundation fell heir to her share of the estate's income.

According to the trustees' latest annual report, on file with the Duval County Circuit Court in Jacksonville, the estate had an income of $15.2 million in 1972. From the figure, $14.7 million was reported to have been given to the Nemours Foundation. (The remaining $500,000 was spent on legal fees, Florida taxes and annuities to a handful of survivors named in the original Du Pont will.)

The Nemours Foundation's tax return for the same year, the latest available from the Internal Revenue Service, showed the receipt of $13.2 million from what appears to be listed as "income from the testamentary trust of Alfred I. du Pont." These words are marked through on the IRS return and an officer of the foundation could give no immediate explanation for the apparent discrepancy in the foundation's income for 1972.

At any rate, only $3.3 million of the income was spent during the year. More than $500,000 of this amount went to maintain the houses and grounds of the sprawling Nemours estate. Its 275 acres, which include the hospital and the former home of Du Pont, are located off Rockland Rd. behind a 12-foot wall crowned with broken glass.

Du Pont's will instructed the trustees of the estate "to care for the mansion and grounds and gardens surrounding 'Nemours' in order that they be maintained for the pleasure and benefit of the public. . . ."

The public is restricted from the grounds. Guards seen visitors at the one gate to the Versailles-like complex.

Inside the walls, the medical staff of the Du Pont Institute is operating on a budget that is not much higher than it had in the late 1960s when rising costs forced the institute to cut back its free services and begin charging patients who were able to pay.

As a result, the institute's medical budget of roughtly $2.5 million in 1972 was supplemented by $1.1 million paid by patients. Last year only 27 per cent of the admissions at the institute were treated as full charity patients.

Aside from an increase in the institute's staff to accommodate a growing number of out-patients and a few capital improvements, there have been no new expenditures by the Nemours Foundation.

Instead of charity, the funds of the foundation are going into certificates of deposit.

The foundation's tax returns for the past 5 years show an astonishing growth in assets of cash, saving and interest bearing accounts.

In 1969, the surplus was $310,977. In 1970, the year of Mrs. du Pont's death, the funds swelled to $1,815,430. In 1971, the figure was $8,756,015. By the end of 1972, the surplus had reached $20,610,006. At this rate, the foundation had accumulated more than $30 million through 1973 and today the amount of surplus on hand is believed to be $35 million.

In addition, the foundation holds another $2 million in liquid assets of stocks, bonds and accounts and notes receivable.

"It's all accumulating in a bank," said a foundation official. "It's drawing interest at a very good rate . . . It's not being spent for anything or misued in any way."

STABLER SAYS NEMOURS NEAR COMPLIANCE, PLANS NO ACTION

(By Curtis Wilkie)

No state action will be taken against the Nemours Foundation, Atty. Gen. W. Laird Stabler Jr. said yesterday, because he is satisfied that the foundation is now moving to comply with will of the late Alfred I. du Pont.

Stabler's statement came after the foundation revealed a proposal to expand facilities at the Alfred I. du Pont Institute, and indicated that new programs for the elderly and plans to open the Du Pont estate to the public are under consideration.

At the same time, Stabler promised to "keep a closer eye" on the operation of the foundation, which has accumulated a surplus estimated at $35 million over the last three years while spending less than 20 percent of its income to support the Du Pont Institute, its only charitable outlet.

Meanwile, U.S. Atty. Ralph F. Keil confirmed that he has asked the Internal Revenue Service to make a formal review of the Nemours Foundation's tax-exempt status as a hospital.

The foundation received routine approval from the IRS for reclassification as a hospital on April 20, 1971. The ruling affected the foundation's tax return for 1970 and subsequent years in which a massive surplus fund has been built.

Two major events converged in 1970 which caused the foundation to seek a classification as a hospital instead of a foundation:

Mrs. Jessie Ball du Pont, the widow of the benefactor of the Nemours Foundation, died, leaving the foundation almost the sole beneficiary of the income of Du Pont's trust. The annual income of the foundation thus went up from $1.2 million to nearly $15 million.

The 1969 Tax Reform Act took effect. The law imposed a 4-percent excise tax on foundations and established other regulations to insure that foundations were engaged in consequential, charitable activities.

To avoid the taxes and regulations, the Nemours Foundation asked the IRS to change their designation to a hospital. There is no evidence that the IRS reviewed the Nemours request closely before approving it and sparing the foundation more than $500,000 in taxes each year.

During a month-long investigation of the Nemours Foundation by the EveningJournal, contradictory statements regarding the status of the foundation were made by IRS officials in Washington.

The IRS had difficulty locating the tax records of the foundation, and in one listing Nemours was categorized by the IRS as a "public charity." Because the foundation receives no public support through a solicitation campaign, it does not qualify as a "public charity."

The IRS finally provided the Evening Journal with 37-year-old documents involved in the Nemours Foundation's original application for a tax exemption instead of the most-recent application.

In order to qualify as a hospital under the new tax laws, Nemours had to terminate its program of making grants to charitable organizations invovled in work with crippled children and the elderly in Delaware, Florida and Virginia. Up until the changeover, the foundation's annual grants amounted to more than $70,000.

The foundation is now limited to the operation of the Du Pont Institute, a crippled children's hospital.

Following last month's News-Journal Report on the Nemours Foundation, questions have been raised about whether the intent of Du Pont's will has been subverted by the action of the foundation officials.

The will called for the foundation to carry out programs for crippled children and the elderly and to maintain the grounds of the estate for the "pleasure and benefit of the public." The will also authorized the foundation directors to spend any surplus funds "in contributions to other worthy charitable institutions."

By functioning as simply a crippled children's hospital, the foundation has no program for the elderly and is prohibited from using its surplus in contributions to other agencies. The public also is barred from the estate.

Alfred du Pont Dent, a director of the foundation, said this week after meeting with the attorney general that Nemours is planning to open the area to the public and considering programs for the elderly "in the framework of geriatric medicine" to protect the foundation's hospital status.

[From the Wilmington, Del., Evening Journal]

U.S. Probes Nemours Switch To Tax-Exempt Hospital Status

(By Curtis Wilkie)

Federal investigators are exploring the possibility that the Nemours Foundation violated the law by obtaining a new tax-exempt status in 1971.

In that year the Internal Revenue Service approved a request by the foundation to be reclassified as a "hospital" in order to avoid taxes and regulations imposed on "foundations" under the 1969 Tax Reform Act.

To win the favorable ruling, the Nemours Foundation had to restrict its activities to one operation—the Alfred I. du Pont Institute, a crippled children's hospital near Wilmington. The foundation was no longer eligible to make grants to charitable agencies.

As a result, a question has arisen over whether the foundation is in compliance with the will of the late Alfred I. du Pont, which spelled out a broader range of activities in establishing the Nemours Foundation.

U.S. Atty. Ralph F. Keil said he had directed his staff to investigate the Nemours case after publication of a News-Journal Report on the foundation which appeared in the Evening Journal last week.

Keil said he also had alerted the U.S. Department of Justice "and other appropriate agencies of the federal government" to review the situation.

Meanwhile, U.S. Rep. Pierre S. du Pont IV, R-Del., yesterday said he was "disturbed . . . for it seems that the intent of Alfred I. du Pont, as expressed in his will, is not being carried out."

He is asking Rep. Wilbur Mills, D-Ark., chairman of the House Ways and Means Committee which has jurisdiction over tax legislation, for comment on the case. Du Pont said he is interested in learning about the provision in the law which permitted the Nemours Foundation to switch to become a "hospital," and if there is any pending legislation to change the law.

Alfred I. du Pont's will specified that the foundation should work in three basic areas:

- Maintain a charitable institution for the care and treatment of crippled children;
- Or provide care for the elderly;
- And to maintain the mansion and grounds of the Nemours estate off Rockland Road "for the pleasure and benefit of the public."

The foundation is funded by the annual income of Du Pont's vast estate, which has been estimated as worth as much as $2 billion. Since the death of Du Pont's widow in 1970, the foundation has received approximately $40 million.

However, the investigation by the Evening Journal disclosed that the foundation is actually:

Spending less than 20 percent of its annual income on the crippled children's operation.

Spending nothing on the elderly. (Before the IRS reclassification, token grants were made to programs for the elderly).

Spending upwards of $600,000 a year to keep up the lavish grounds of the estate, but not permitting the public behind the 12-foot stone walls which encircle its 275 acres.

Instead, officers of the foundation—most of whom are residents of Florida—are stockpiling the income in a gigantic surplus fund which is believed to be near $35 million now and is expected to approach $50 million by the end of 1974.

In Du Pont's will, he directed the trustees of his estate to use surplus funds "in contributions to other worthy charitable institutions."

But such contributions to outside institutions are forbidden to any "foundation" operating as a "hospital."

As a "hospital," the Nemours Foundation also is escaping more than $500,000 in federal excise taxes each year as well as avoiding restrictions against an inordinate accumulation of surplus funds.

If the Nemours Foundation still was classified as a "foundation" for tax purposes, it also would be limited in its business dealings with the bank, railroad and paper-company empire controlled by Edward Ball of Jacksonville, Fla. Ball, a brother-in-law of Alfred I. du Pont, is president of the Nemours Foundation.

Aside from the federal investigation, Delaware Atty. Gen. W. Laird Stabler Jr. said yesterday there is the possibility of state action against the foundation unless "they get on the stick."

Stabler said he had twice written Alfred du Pont Dent of Wilmington, the only Delawarean on the Nemours board, to express concern over the handling of the foundations money.

In a December 1971 letter the attorney general pointed out that Delaware residents were to be given "first consideration" for services and observed that the money should not be spent elsewhere. Stabler's original letter came after entreaties by Delaware charitable organizations interested in obtaining funds from the Nemours Foundation.

Stabler followed up with another letter last December asking for an explanation of the foundation's failure to spend its available funds.

After a meeting of the Nemours board last week, Stabler was told that Dent had been authorized to move as expeditiously as possible to advance the foundation's current programs for carrying out the instructions contained in Mr. du Pont's will."

The correspondence to Stabler did not indicate whether this included projections for services to the elderly.

At their meeting last week, the foundation officers agreed to submit plans for expansion of the Du Pont Institute's crippled children's facilities to the Delaware Health Planning Council, Inc.

However, the plans have not been submitted yet and officials would not give details of the proposal.

Stabler, who also has been asked by Rep. du Pont to investigate the case, said he planned to meet with Dent next week when he returns to Wilmington from a Florida vacation.

Rep. du Pont, whose grandfather was a first cousin of Alfred I. du Pont, said, "It is both unfortunate, and, in my opinion contrary to the intent of the will that money should be stockpiled in a bank rather than used for the benefit of children and the elderly."

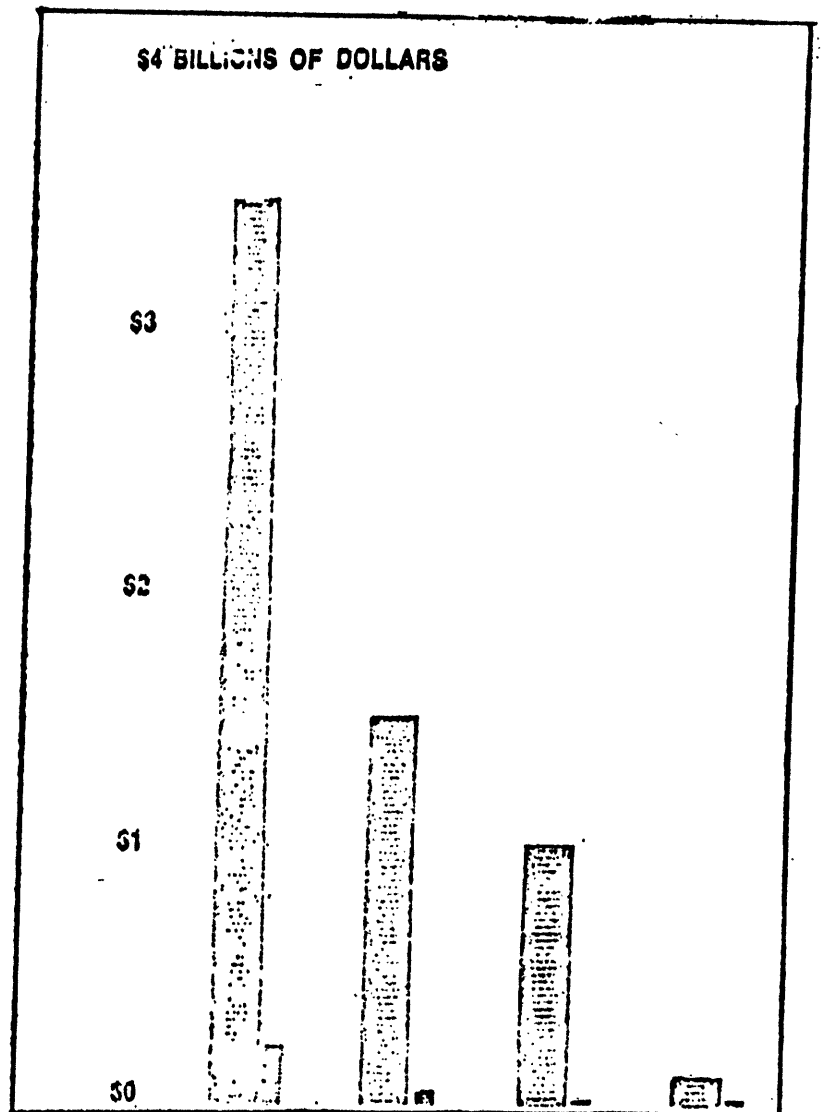
He was the only member of Delaware's congressional delegation to comment on the Nemours case. Other than Stabler, no state official has publicly expressed interest in the matter.

During their meeting last week, the officers of the Nemours Foundation ignored a list of questions from the Evening Journal submitted at the request of Ball, who refused to answer the questions during an interview.

The questions dealt with such subjects as lack of care provided the elderly; inaction on proposals to expand crippled children's facilities; inaccessibility of the grounds to the public; business deals between the foundation and Ball's enterprises; and a $.6 million discrepancy between the income the foundation reported in its 1972 IRS return and the income it reported for the same period in paper on file with a Florida court.

Although one foundation official said a Florida attorney had been instructed to respond to the questions, the attorney himself said he knew nothing about it.

Ball, who is 86, is said to be "traveling around on a plane on business" and unavailable for comment. Other officers have refused to return repeated telephone calls by the Evening Journal.



	FORD FOUNDATION	JOHNSON FOUNDATION	NEMOURS FOUNDATION	LONGWOOD FOUNDATION
ENDOWMENT	$3.4 billion	$1.5 billion	$1 billion	$153 million
GRANTS	$215 million	$28 million	$3 million	$4 million

This graph compares the total endowment and the 1972 charitable contributions of the Nemours Foundation with the Ford Foundation and the Johnson Foundation—the two largest in the country—and the Longwood Foundation, the second largest in the Wilmington area. Although the exact size of its endowment cannot be determined, the Nemours Foundation is believed to be the fourth richest in the United States.

Estate's Assets Too Much for Adding Machine

When Alfred I. du Pont died in 1935, the paper value of the assets of his estate was $39 million. Today the value of the estate is almost incalculable. An auditor for a Florida court said his adding machine was unable to accommodate all of the digits in the accounts of the Du Pont Estate.

According to the latest report of the trustees, a book value of $160 million was set for the estate. Actually, the value is probably closer to $1 billion, and the estate controls assets valued at another $1 billion.

The estate's holdings in common stock of the Du Pont Co. alone is worth $130 million. It owns another $60 million in General Motors stock.

The estate also holds $40 million in the stock of the Florida National Banks, but is under government orders to divest itself of these assets by the end of the year. Edward Ball has been "coordinator" of the bank holding company and controls, through the Du Pont estate, his late sister's estate and his own holdings, more than 35 percent of the bank combine.

The estate owns more than $3 million in common stock of the Florida East Coast Railway and another $2.5 million in bonds. However, the Securities and Exchange Commission recently obtained a federal injunction involving the railroad company and the estate. As a result, the estate—which was charged with purchasing the bonds on inside information—has agreed to offer $476,000 worth of the bonds back to the previous owners. Ball is chairman of the board of the railroad.

The estate owns 70 percent of the St. Joe Paper Co., which is not a public company. The paper company, in turn owns 52 percent of the railroad. The company also owns more than 1 million acres of priceless undeveloped timberland in Florida. Although the land draws no yield, its potential is limitless. Ball is chairman of the executive committee of the paper company.

The estate has $63 million invested in certificates of deposit—$4.1 million with the Florida First National Bank. Another $51,000 in cash was deposited there at the end of 1972.

The estate also owns substantial real estate in Delaware and Florida as well as thousands of scattered shares of other stocks.

Nemours Eyes Care for Aged, Public Tours

(By Curtis Wilkie)

The Nemours Foundation, under federal and state investigation for failing to provide services for the elderly and for barring the public from the grounds of the Alfred I. du Pont estate, is contemplating action in both areas, a foundation official said yesterday.

Alfred du Pont Dent, a directtor, said the Nemours Foundation is "considering doing something in the field of older people." The subject was "discussed in a favorable light" at last month's board meeting, he said and will be studied again at another meeting in May.

In addition, the grounds of the 275-acre estate off Rockland Rd. will be opened to the public "in the not-too-distant future," Dent said.

Dent, the only Delawarean on the Nemours board, said he met with Atty. Gen. W. Laird Stabler Jr. Tuesday to discuss the situation.

Stabler had made inquiries earlier about the foundation's apparent failure to follow the terms of the will of Alfred I. du Pont regarding services for the elderly.

Following a News-Journal report on the foundation which appeared in the Evening Journal last month, Rep. Pierre S. du Pont IV, R-Del., asked Stabler to look into the advisability of bringing a class-action suit against the foundation on behalf of the people of Delaware.

The will of Alfred I. du Pont, which established the foundation, stipulated that the funds be used to care for crippled children or the elderly and to maintain his estate "for the pleasure and benefit of the public." Delawareans were to get "first consideration" for treatment.

The News-Journal report showed that the foundation has accumulated an estimated $35 million in surplus funds over the last three years while spend-

ing less than 20 percent of its annual income on the operation of the Alfred I. du Pont Institute, a crippled children's hospital. Nothing is being done for the elderly and the public is not permitted on the estate.

After its March 21 board meeting, the foundation announced plans for expanding its facilities for children at the institute. Although details have not been released, Dent said yesterday that it would involve an increase in beds and the medical staff would be more than doubled.

The addition will provide services for problems and diseases which are not now treated at the institute. Construction may start within six months, according to Dent.

The institute is on the grounds of Du Pont's estate, which is enclosed behind 12-foot stone walls. The area was to have been opened to the public after the death of Du Pont's widow in 1970. But foundation officials continued to guard the area because the Du Pont mansion is run down and no orderly plan to handle visitors has been developed.

"If you just open the gates and say 'come on in,' what's going to happen is a line of people back to the Brandywine. And a question of how do you get them out," Dent said.

There are plans to renovate the mansion and install a system for visitors similar to that used at Hagley Museum, where a jitney hauls passengers from a parking lot.

The foundation also is considering the establishment of a program geared to the elderly. However, Dent said it would have to be "in the framework of geriatric medicine" in order for Nemours to retain its tax-exempt status as a "hospital."

U.S. Atty. Ralph F. Keil last week touched off a federal investigation into Nemours' classification as a "hospital"—which the foundation received from the Internal Revenue Service in 1971 in order to avoid new taxes and regulations aimed at foundations.

"I think there's no question that the IRS will review it now." Dent said of the reclasification as a "hospital," which restricts the activities of the foundation.

By operating as a "hospital" the foundation escapes more than $500,000 a year in federal excise taxes.

Senator HARTKE. Are you familiar with this organization?

Mr. SCHOENFELD. We have seen the articles, Senator.

Senator HARTKE. Have you investigated the articles and the charges made in the articles?

Mr. SCHOENFELD. We consider all relevant information; and I assure you we have looked over very carefully what is contained in those newspaper articles.

Senator HARTKE. Did you come to any conclusions?

Mr. ALEXANDER. Mr. Chairman, we have a disclosure problem here.

Senator HARTKE. You have a what?

Mr. ALEXANDER. We have a disclosure problem here. We are forbidden under section 6103 of the Internal Revenue Code, and 7213 of the Internal Revenue Code, from discussing specific audits of specific taxpayers, except to the extent that those taxpayers may have already discussed audits, and then only within the four corners of the taxpayer's statement.

Mr. Chairman, we are mindful of that particular article. I read that article. We are mindful of our responsibilities in this area. We are doing our best to fulfill our responsibilities.

Senator HARTKE. Do I take from what you are saying that you would prefer not to discuss it further at this time?

Mr. ALEXANDER. That is correct, Mr. Chairman.

Senator HARTKE. I gathered that was what you said.

Mr. ALEXANDER. Mr. Chairman, I think the medical research regulations have not yet been published. I think they are among those regulations that I mentioned to you that were under consideration.

As Mr. Gibbs pointed out if an organization truly qualifies for treatment as a medical research organization or as any other public charity, then it is entitled to that treatment. But it is not entitled to that treatment simply because it claims it is entitled to it; it is not entitled to it simply because it has a name that might indicate that.

Senator HARTKE. Well, let me ask you a question, within the framework of the legislation, do your auditors, when they audit a situation, do they pay any attention to a situation of this kind? Would they look into that? Would that be within the framework, or simply because of the situation, they make the claim and push it aside and no regulation; therefore, it does not come within your purview?

Mr. ALEXANDER. No. The fact that there are no regulations does not mean that there is not a statute. In the absence, before regulations were issued, we had a number of audits, a number of private rulings and requests for technical advice in this rather difficult area. It does mean we tread with care; it does not mean that we abdicate our responsibilities.

Mr. Schoenfeld?

Senator HARTKE. Well, here is a situation where Nemours as I understand it, according to the allegations, changes its situation from a foundation—had itself declared a hospital in 1971, after the passage of this act; is that right or is that wrong?

Mr. ALEXANDER. Mr. Chairman, I would much prefer not to comment upon individual situations. Now, as you know, there are some limited exceptions to the anti-disclosure role in the area of exempt organizations. Public review is not only permitted, but, indeed, access to the public is required of returns filed by these organizations and exemption applications filed by these organizations. Those things are a matter of public record. And our audit activity is not.

Senator HARTKE. I will postpone any further inquiry on this matter at this time. I will not say I will not pursue it at some later date; I will just postpone it now; all right?

Mr. ALEXANDER. Thank you, Mr. Chairman.

Senator HARTKE. Let me ask you, what about the so-called satelite organizations which are described in 509(a)(3)? Is it not important to know whether any of these organizations set up by a donor who then turns around and sits on his money, to what extent is this classification being used by organizations to escape private foundation status?

Mr. ALEXANDER. Well, we have an audit responsibility here, Mr. Chairman, to make sure that 509(a)(3) organizations live up to the statutory restrictions and responsibilities placed upon them. I think we are doing our best to fulfill that responsibility.

Mr. Schoenfeld?

Mr. SCHOENFELD. Commissioner Alexander indicated that we will be conducting a TCMP program, which is taxpayer compliance measurement program; and as part of that program, we will be looking into the relationships that exist between section 509(a)(3) organizations and other organizations. And one of the purposes of this special program is to let us know whether or not we have a special compliance problem in this area.

Senator HARTKE. Well, let me ask you, are the Section 509(a)(3) organizations actually responsible to the public, as required by the law, and to the public charities that they allege they support?

Mr. SCHOENFELD. We would issue a ruling to an organization based on the information that it furnishes, and part of the information is to spell out the nature of the relationship between the support-type organization and the public charity. We look into this, these statements, on audit. And we would take appropriate action if we find out that the organization needs to be reclassified.

Senator HARTKE. Do you have any instances where you have taken action in this regard?

Mr. SCHOENFELD. We have reclassified a number of organizations, but I do not have any statistics on those.

Senator HARTKE. Could you supply those for the record for us? I mean, where you have really taken action?

Mr. SCHOENFELD. We can make an attempt.

Mr. ALEXANDER. We will do our best to get this information for you, sir. This is information——

Senator HARTKE. Do you really think there are any reclassifications—now do not tell me that you have done this if you have not. Let me make a generalized statement.

We feel at this moment that we are pretty much in the dark, and we think you are, too; and we feel we are in a much darker arena than most people understand. As I said in my opening statement, there have been people who have made statements here that the act has been of great detriment to foundations. Others have said it has been a great asset to foundations. Others have said it is in between. But there has been almost a complete void as to factual circumstances. And I think that, in general, that you would have to say that your statement, in answer to our questions, which we had to prod you to answer—but I am not arguing about that—that pretty generally we are still back in the same situation, in answers to our questions, that you left us in much the same position; that we are in no better position, really, to legislate or to evaluate the 1969 legislation than we were 4 years ago.

Is that fair? I mean, if I am being unjust in this accusation—I mean, I am going to tell you quite frankly, we are struggling to get this information.

Mr. SCHOENFELD. Yes, sir. I think that is—if you will permit me——

Senator HARTKE. Yes.

Mr. SCHOENFELD. Because I think you have to look to what has happened. It is fair to say on the one hand that the legislation was passed 4 years ago, but I think we have to look up, as to the time-

table of the regulations, the way the Service has administered this, and the way the foundation community has responded to our regulations. I think until March of 1973, we really did not, ourselves, have a grasp or a grip on the universe of private foundations or how many there were. The key regulations were not final until then.

I do not mean to harp on this fact, but during the period that these regulations were becoming final, you could not take an organization and go out and audit it, and say we are going to reclassify you. As the Commissioner said, we are not going to not work because we do not have these regulations; and we will make the best judgments that are available until they became final.

One problem is that we just did not keep statistics until the regulations reached that point. And this accounts for part of the problem.

Mr. ALEXANDER. Mr. Gibbs.

Mr. GIBBS. Mr. Chairman, could I say something? Because it is something that I am seeing in other areas.

One of the things when I was practicing, I assumed that the Service would see and have answers to a lot of the problems that I was seeing as a practitioner. What I did not realize then that I realize now, serving in the Government, is this: That after legislation is passed or regulations are put out, there is a period of time in which the people that are seeing the impact of the legislation or the regulations and are planning either to terminate the foundation or to adapt the foundation to comply, either "technically" or really with the rules, is that the practitioners and the foundations themselves—and it is only after this lead time, when you get legislation, regulations, and then you get your practitioners and your taxpayers and your foundations working with this, it gets to a point where it comes to the Service and to the Treasury in such a way that you can meaningfully tell what is actually happening with the legislation that you are getting. And if 4 years sounds like a long time to you, all I can say is, I think that is really what it has taken, and I think we are just beginning to get into the areas to find out how people have reacted to and adapted their organizations to the legislation that was passed and is being implemented and has been implemented in the last 4 years.

Senator HARTKE. All right, then, let me come back to specifics.

Section 509(a)(1) provides that organizations described in section 170(b)(1)(A)(vi) are treated as public charities if they meet a test of facts and circumstances of public support.

To what extent is this classification being used by organizations to escape private foundations status? In other words, are these organizations in fact responsible and responsive to the public?

Mr. SCHOENFELD. I think in reply to your questions, we point out that since all of these organizations described in section 509(a)(1) are considered as public charities, we do not, for our internal record keeping purposes, maintain a breakdown of the subclasses of public charities. So, for example, as to how many organizations receive rulings under the facts and circumstances test in section 170(b)(1)(A)(vi), we just would not have that figure available.

Mr. ALEXANDER. Mr. Chairman, I would like to discuss this for a moment with you, if I might.

The new regulations define what it takes to qualify as an organization within the category you describe, the so-called (vi) organizations—organizations which receive a substantial part of their support from direct and indirect contributions from the general public and are not otherwise described in one of the specifics mentioned in the preceding portion of that section. The new regulations define a substantial part to mean 10 percent or more. The old regulations, if I recall them correctly, and I think I do, contained, no minimum percentage whatsoever. Many organizations were quite upset about the introduction of the 10 percent requirement before one could get to a facts and circumstances test, since no such requirement had appeared under wording identical in all material respects to that in the new statute.

Now, if anything, the standards are tight. The questions of possible abuse are by no means eliminated, although with the audit program which we hope to have, are less than they were before.

As a private practitioner when this statute was changed, I was called on by a number of entities that were quite upset about being classified under the new rules as private foundations rather than the category to which they thought they were entitled and to which they considered themselves entitled before. If anything, the implementation of the statutory rules by new regulations, has narrowed the possibilities of abuse in this area. And it is up to us to have a sound and an effective audit program to carry out, to implement, the directions in the statute and in the regulations. But also carry it out in an understanding way, in a stance that reflects our regulatory function rather than our tax collecting function.

Senator HARTKE. A penalty tax has been assessed?

Mr. SCHOENFELD. Some have been, Senator, and I know that from personal knowledge; but we do not keep statistics.

Senator HARTKE. No statistics on penalty taxes, right?

Mr. SCHOENFELD. That is true.

Senator HARTKE. Now, when the act was passed, it prohibited the foundations from entering into transactions with their donors or their directors, right? So-called self-dealing. It required a minimum payout of foundation assets, a 6 percent requirement; prohibited foundations from holding more than 20 percent of the assets of any corporation. That is the excess business holder provision. In other words, there were considered to be abuses which were alleged to be corrected as a result of the 1969 legislation.

We feel, and I would hope that you would feel, it would be very important for us to know just how each one of these various efforts have succeeded, and how can we really tell how they have succeeded in this field unless we know, at least in one field, how much the penalty taxes were assessed and how much of it came from so-called second level tax—that is a tax which is levied if the foundation fails to correct an abuse for which it has already been penalized. In other words, do you not think it is important for Congress to know just how well the foundations are complying with the various provisions which were added by the 1969 act?

In other words, the purpose of the legislation—and I really do not know whether I want to pursue it any further, to tell you the truth, at this moment—I am concerned about how we are going to move without us doing an indepth study ourselves in the committee——

Mr. ALEXANDER. Senator, you are certainly entitled to consider this questioning, and it is a point——

Senator HARTKE. Well, let me just say this, if you are short of personnel and have not been able to do this, I do not know what it would take. We had been hopeful that someplace somebody was going to be able to give us some of this information.

Mr. ALEXANDER. Well, first, let us not abandon hope, because—well I might call on Mr. Schoenfeld to supplement this answer, because if anyone has the information, he has.

Second, what we have here is, I think, some specific information in response to many, but by no means all, of your questions.

So, as I stated earlier, we do not have an absolute vacuum unless we want to construct one.

Third, our purpose, I guess, from the standpoint of the Internal Revenue Service, is to try to administer this law. Our secondary purpose is, of course, to collect data for the purpose of testing whether we are administering the law wisely and soundly; and if we are not, then the administration should be corrected. And you certainly have the right and the authority to correct it, and, for the purpose of collecting the data itself. But that, as we have seen it in the past, perhaps wrongly, has been a secondary purpose in this new field.

Now, I am very sympathetic, and I think the entire Agency is, to the need for good information in this area; and I regret greatly that some of the information in this area is lacking on our part. And I recognize your need, Mr. Chairman, for definitive and full information, which unfortunately we are unable to supply you. We can supply you with full information in some of the areas which you posed questions to us, and I think we have supplied that. In other areas, the information is incomplete. We hope that it will be more complete later, but some of it, as Mr. Schoenfeld has pointed out, cannot be complete.

Mr. Schoenfeld?

Mr. SCHOENFELD. We, too, would like to have more reliable information about the organizations that we are examining, and we referred previously to the TCMP program. This program will include the examination of some 10,500 returns. It will include 3,500 private foundations. These returns will be selected on a scientific basis, and the purpose of this kind of examination will be to elicit information of the type you are referring to; and hopefully we will be able to even explode this information and possibly even get information about the universe of foundations as a whole. But it has been very difficult to get information in the past, and this is our answer to how to get the answers to the questions that you have been raising. And we are starting on this program in August, and it will run for 18 months.

Senator HARTKE. Mr. Alexander, I know that you are aware of the changes that have been made that there have been attempts to use the power of the Internal Revenue Service for partisan advantage, and I believe you have testified before Senator Montoya's subcommittee on this subject, and maybe will be doing so again this week.

Without getting into details, I just want to ask you one or two questions on this subject which touch upon foundations.

First, in a September 21, 1970, memorandum from Tom Charles Huston to H. R. Haldeman, which is reprinted in the Senate Watergate hearings on page 1338, as exhibit No. 42, there is a reference to a special service group.

Can you just tell us for the benefit of the record what this group is or was?

Mr. ALEXANDER. Mr. Chairman, it was. The special service group or special service staff, as it was called before I disbanded it on August 9, last year, was a group set up under a different name, I think it was Activist Organizations Group, as a result of certain hearings conducted in the late 1960's by as I recall, the Senate Permanent Subcommittee on Investigations. It was a group set up with the purpose of seeing whether certain activist organizations of all types, extremists on both ends of the political sector, were indeed meeting their tax responsibilities. I think concerns had been expressed as to whether these organizations were deriving income on which no taxes were being paid, and on other concerns about possible abuses of the tax system.

When I became Commissioner of Internal Revenue on May the 29, I started a study——

Senator HARTKE. What year?

Mr. ALEXANDER. May 29 of last year.

Senator HARTKE. That is 1973?

Mr. ALEXANDER. 1973.

I started a study of this group. As a matter of fact, I had a briefing on this group on May 30, 1 day after I was sworn in, and I found that the work of coping with those who would try to prevent the Internal Revenue Service from going about its business and performing its duty of administering and enforcing the tax laws could better be handled by our regular inspection, internal security and intelligence personnel. I saw no reason for this group, furthermore, I was concerned about the possibility or probability that this group could be considered or could consider itself to be engaged in matters beyond the tax system. By matters beyond the tax system, I mean matters concerned with the political views of particular organizations or particular persons, which views are irrelevant to the tax system. (And) So the group was abolished.

Now, we kept the files of this group intact because the Joint Committee on Internal Revenue Taxation, of which you are a member, was investigating the Internal Revenue Service, and still is, to see whether the Service was misused, whether its procedures were abused by those who might have wanted to misuse its procedures or abuse the Service.

Furthermore, Senator Ervin's committee and other committees have been interested in looking into these matters. We maintain the files. We have abolished the special service staff. We are not interested in political views. They are irrelevant to the tax system except insofar as some political organization may try to claim tax exemption. At that point we do have a statutory duty to inquire as to whether the organization is entitled to exemption, whether it is an "action" organization or whether it is not. Beyond that I saw no purpose in inquiring into any such activist or extremist, whatever one might call them, views of any person or organization, and the special service staff is abolished in reality as well as name.

Senator HARTKE. All right.

In other words, you say that the organization is no longer in existence now, right?

Mr. ALEXANDER. It has not been in existence since——

Senator HARTKE. As a special service group.

Mr. ALEXANDER. That is right, and the organization is not in existence, and the Internal Revenue Service is not in the business, and in my judgment has not been in the business of engaging in selective enforcement based on political considerations.

Senator HARTKE. In your investigation or to your knowledge, was it used for the purposes which were alleged in the memorandum of Mr. Huston for going after groups or individuals whose ideologies were opposed or seemed to be opposed to those of the White House?

Mr. ALEXANDER. I am not aware of the details of Mr. Huston's memorandum. I am aware that such a memorandum exists.

Senator HARTKE. Let me say to you, I will be glad to supply the whole item for you.

Mr. ALEXANDER. I would be glad to reply to you, sir. I would appreciate it, Mr. Chairman, if you would supply that memorandum to me. I think I have a copy of it, but I want to make sure we have the same one. I would be glad to respond to that.

Senator HARTKE. It is not very long. I would be glad to give it to you.

Mr. ALEXANDER. I am interested to hear that Mr. Huston thought that the report which he mentioned was long on words and short on substance Assuming I understand his views of substance, I am pleased to see that he found the memorandum lacking, Mr. Chairman. And, Mr. Chairman, I do not think the processes of the Internal Revenue Service were being abused by any engagement in selective enforcement. We are looking into these practical matters now. They are the subject of several continuing investigations and I think that the facts will be brought out.

Senator HARTKE. Well, let me ask you, on the basis of the information that you have now, was it to your knowledge or your investigation, used for any of the purposes of going after groups or individuals whose ideologies were seen as opposed to the White House?

Mr. ALEXANDER. Mr. Chairman, there is no doubt but that this group did make reports to the field, and certain investigations were made of certain organizations. So there is no doubt that certain investigations were made.

Senator HARTKE. So in substance, what you are saying is that the suggestions of the memorandum were in fact carried out by the special service group.

Mr. ALEXANDER. I am not saying that at all, Mr. Chairman. I am simply saying that——

Senator HARTKE. I do not mean to put words in your mouth, but that is what I took from your answer.

Now, what I am asking you is, again, just really whether or not these special services group did to your knowledge for investigation use the Internal Revenue Service for the purpose of going after groups or individuals whose ideologies were seen as opposed to the White House.

Mr. ALEXANDER. Mr. Chairman, I would regret that my answer to you may not satisfy you. I am going to repeat——

Senator HARTKE. Well, the question of satisfying me——

Mr. ALEXANDER. I am going to repeat several things I just said.

No. 1, I have said that the functions of the special service group is a matter of ongoing investigations.

Senator HARTKE. It is what?

Mr. ALEXANDER. This is a matter of ongoing investigations.

Senator HARTKE. I am not asking about the future. I am just asking you, have you so far to your knowledge and your information found out that the special services group was used for the purpose of going after groups or individuals whose ideologies were seen as opposed to those of the White House.

Mr. ALEXANDER. All right, Mr. Chairman, I am going to tell you that the special service staff did make various reports to the field, and various investigations were made. In answer to your general question, I do not consider that it was so used.

Senator HARTKE. You do not consider it so used?

Mr. ALEXANDER. I do not consider it so used. Other judgments might differ. Other judgments might differ because any organization that is investigated and that happens to have a particular ideological bent may well charge that the investigation was for the purpose of harassing the organization rather than for the purpose of enforcing the tax law, and an organization can so charge. Some are charging that today.

Senator HARTKE. I missed a word there, either one of you, the reporter or you, and I am sorry, my staff did not catch the word that I missed, so I have got to find out either from you or from her.

Could I ask you?

Mr. ALEXANDER. I'll ask her to read back my answer.

The REPORTER.

Senator HARTKE. You do not consider it so used?

Mr. ALEXANDER. I do not consider it so used. Other judgments might differ. Other judgments might differ because any organization that is investigated and that happens to have a particular ideological bent may well charge that the investigation was for the purpose of harassing the organization rather than for the purpose of enforcing the tax law, and an organization can so charge. Some are charging that today.

Mr. ALEXANDER. Mr. Chairman, may I make two points about this. The special service staff, by any name it was called, simply collected information, and collected information from a number of sources, including the Federal Bureau of Investigation. It would disseminate certain information to our field offices, but the field offices would then decide whether they were going to audit an organization or whether they were not going to audit an organization. The special service staff, by whatever name it was called, did not engage in auditing on investigating organizations. It did not engage in taking collection action as to the overdue taxes due from organizations.

Now, let me say that in response to a sentence in this memorandum which I would like to read to you,

what we cannot do in the courtroom by a criminal prosecution to curtail the activities of some experience, IRS could do by administrative action.

It did not do so.

Senator HARTKE. Well, now, by admintrative action, you mean by that in a strict legal sense of taking administrative procedures, or do you mean—would you consider the field—what do you call them, the field people?

Mr. ALEXANDER. The field personnel, the Revenue officers.

Senator HARTKE. I am asking you, and you understand the process, and you correct me now if I am wrong in my assessment in what I said, that you said that the special services group did in fact take some type of action against certain organizations.

Mr. ALEXANDER. No, sir, I did not. I said the special service staff collected information. They collected information with respect to several thousand organizations. It would, in instances where it thought action was warranted, send out information to the field, but it did not take action in its own behalf. It did not take any action as the special service group or for the Internal Revenue Service in any way to audit organizations or individuals, or to take collection action with respect to organizations or individuals. This would be done or not in the judgment of the field people by the field people.

Senator HARTKE. Yes. In order words, you have got to get this situation straight.

As I understand what you are saying is, in your investigation you found out, as a result of your investigation, right?

Mr. ALEXANDER. As a result of our investigation, and by the way, sir, the Joint Committee on Internal Revenue Taxation also investigated the special service staff, and a member of the Joint Committee staff is here.

Senator HARTKE. Yes, I am a member of that committee.

Mr. ALEXANDER. I am aware of that, sir.

Senator HARTKE. Now, as I understand what you have said, though, the special services group did conduct certain investigations and collected——

Mr. SCHOENFELD. No, sir, it did not conduct investigations. It only received and disseminated information.

Senator HARTKE. How did they receive information?

Mr. ALEXANDER. They received information from a number of sources, including the Senate of the United States, which gave a substantial amount of information.

Senator HARTKE. Voluntarily received it. In other words, they did nothing on their own initiative whatsoever, according to information——

Mr. ALEXANDER. They received information, and whether you call that on your own initiative received or by reason someone else's initiative, I think is idle. What I am suggesting——

Senator HARTKE. What I am asking you is, did they—in other words, was there a suggestion made of give me some information? In other words, did they just sit there, did the special services group just sit there?

Mr. ALEXANDER. They did not exactly just sit there.

Mr. SCHOENFELD. They did not conduct audits, sir.

Mr. ALEXANDER. They did not conduct audits, they did not conduct enforcement activities of any kind,-they did not conduct collection activities, they did not conduct investigations. I think there were only eight people in this group.

Mr. SCHOENFELD. And a lot of files.

Senator HARTKE. Let me try it again.

The special services staff—I always thought it was a rather unfortunate choice of words to use, the SSS, by the way, but that is in reference to a prior term in history, especially for such a group—but anyway, they would gather information, right?

Mr. ALEXANDER. They were gathering information, that is correct.

Senator HARTKE. And they would gather it both on the finances and the activities of the organizations, is that correct?

Mr. ALEXANDER. They would gather information as to an organization. The Federal Bureau of Investigation would send them information. They would get information sent to them from Congress and from elsewhere as to organizations.

Senator HARTKE. Now, how did the FBI and the Congress and the Audit, Collection, Intelligence, Alcohol, Tobacco and Firearms Division and so forth, how did they know what it was that the SSS wanted?

Mr. ALEXANDER. Well, for one thing, the Senate Committee on Investigations, being the father of this child, necessarily knew what the child wanted, and I do not know how the special service staff may have communicated with the Federal Bureau of Investigation or who instigated the communication. I can look into that, sir, and supply you information for the record.

Senator HARTKE. You said that they did not request this information. How would you know they did not request this information if you do not know how they got this information?

Mr. ALEXANDER. To the extent that I indicated that no requests were made, I will supply that for the record. I know they did not conduct audits, and I attempted to impart that knowledge.

Senator HARTKE. All right, they did not conduct audits, but gathering the information, as I understand what you are saying is

that you are neither saying that they did or did not request this information.

Mr. ALEXANDER. I am saying that I do not know who instigated the communication between the special service staff and those who provided information to it. Perhaps Mr. Schoenfeld——

Mr. SCHOENFELD. Just like we would receive from you, or since you brought it to our attention, the newspaper article concerning the Nemours Foundation, the special service group brought to the attention of appropriate district officials information activities of some exempt organizations. A decision was made at the local level by Internal Revenue Agents on whether or not to take any action.

Senator HARTKE. Well, let me ask you, though. Are you saying now that they did not request this information? Are we back to that position again, or we do not know?

Mr. ALEXANDER. No, we are not back to that position at all, Mr. Chairman.

We are simply saying that we will attempt, with the permission of the Chair, to find out whether the special service staff instigated inquiries of other organizations, or whether other organizations sent material to the staff, if that would answer the question that you put.

The question that we were discussing was what was done with the information, not how the information was acquired.

[The following was subsequently supplied by IRS:]

Where did the names representing Special Service Staff files originate?

Names were obtained and originated in two general ways:

(a) Material and information were obtained generally without SSS initiative from the FBI, House Committee on Internal Security, Senate Subcommittee on Investigations of the Committee on Government Operations, and the Senate Subcommittee to Investigate the Administration of the Internal Security Laws of the Committee on Judiciary.

FBI reports were received both through routine dissemination (which accounted for the bulk of the names) and upon specific request. Congressional Committee information including names were in the main obtained from published hearings. It is estimated that from 75% to 80% of the total names were obtained without Special Service initiative.

(b) Other sources: Various publications were subscribed to by the Special Service Staff, i.e., Underground Newspapers including tax resistance newspapers. These publications were gleaned for names of individuals and organizations who appeared to have a high propensity to avoid payment of Federal taxes. After additional names were obtained from these sources, the Staff caused a check to be made from the FBI and Congressional Committee publications for any further pertinent data. As warranted, internal file searches were made to determine whether or not the individual or organization had filed appropriate tax returns.

2. How many field referrals were initiated by the Special Service Staff?

Referrals to field for investigation 8/69–8/7/73—250 (Includes Audit and Collection).

Senator HARTKE. Now, as to the collection of this information, am I correct in this statement that what you are saying is that the special service staff did not actually go about itself on investigations?

Is that what you are saying?

Mr. ALEXANDER. This, special service staff, special service group, and the activist, or whatever it was, organization before that did not undertake field audits, field activities, field investigations or any such activity.

Now, that is not saying, sir, that that group did not inquire of other organizations whether they had information which would presumably be of importance to the staff. I do not know how the relationship of submission of information to the staff from these other organizations was instituted or was actually conducted, but I will find that out for you, sir.

Senator HARTKE. Now, as I understand what you are saying, that after they had this information, that they would make certain recommendations to the field offices. Is that right?

Mr. ALEXANDER. I understand that they would submit information to field offices, but I think they—I can get for you, I believe, sir, the number of times that they submitted information. I think that number is small.

Senator HARTKE. Well, let me ask you, am I more nearly correct in saying that just for the purposes of getting the record straight, that they did not submit recommendations about criminal prosecutions? But did they submit recommendations that a certain organization's returns be audited or reviewed?

Mr. SCHOENFELD. To my knowledge, the information was passed on for whatever action the district officials felt was appropriate. It was up to the Revenue Agents in charge of examining these returns to determine the worthwhileness of the information, on the basis of the information received, to take appropriate action.

We in Internal Revenue receive information all the time from a lot of sources. We act on what we think is the most appropriate information to prevent tax abuses.

Senator HARTKE. During this time, was there any information which was collected about these groups? I am speaking now specifically about foundation groups, which was in turn given back to any of the White House staff other than the information concerning the actual revenue or the tax questions itself. Was there any other information given?

Mr. ALEXANDER. Mr. Chairman, I believe that the White House did get certain information as to taxpayers during the period commencing in 1969, just as it did in earlier periods. Now, whether it obtained information with respect to these particular groups is something on which I do not have any personal knowledge.

Do you know?

Mr. SCHOENFELD. I have no such personal knowledge either.

Senator HARTKE. Is such information being submitted to the White House now?

Mr. ALEXANDER. As to what—well, the information being submitted to the White House, to my knowledge—and I think I know about what is going on in the Internal Revenue Service, Mr. Chairman—is in connection with tax checks of potential appointees.

Tax checks of potential appointees have been made regularly, I believe, for at least 20 years, to find out whether someone who is being considered for a Federal appointment has filed returns and is now in trouble or not with the tax system, whether he is current in his tax payments.

That sort of information, it seemed to me, and it seemed to, I would think, at least five of my predecessors, is information to which the appointing official is surely entitled to.

As to other information, Mr. Chairman, section 6103 of the Internal Revenue Code provides that tax returns and tax return information shall be open on order of the President. The President does have access by law to a tax return and tax return information, and that has been the situation as far as I know since section 6103 and its predecessors came into the law.

Now, to complete my answer to your question, I am submitting no tax material to the White House and have not done so since I have been in office.

Senator HARTKE. When was the special services group deactivated or abolished?

Mr. ALEXANDER. August the 9th, 1973, the date I issued a press release announcing my decision.

Senator HARTKE. Was it done by official memorandum?

Mr. ALEXANDER. It was done, yes, it was done officially by a directive which I signed on August 13 and which I wrote.

Senator HARTKE. Could you supply a copy of that for the record, please.

Mr. ALEXANDER. I certainly will, sir.

Senator HARTKE. Thank you.

[The information referred to follows:]

DEPARTMENT OF THE TREASURY,
INTERNAL REVENUE SERVICE,
Washington, D.C.

NEWS RELEASE

WASHINGTON, D.C.—The Special Services Staff within the Internal Revenue Service will be disbanded, Commissioner of Internal Revenue Donald C. Alexander announced today.

"The tasks now being performed by the Staff," Mr. Alexander said, "can be handled efficiently by other components of the Service as a part of their regular enforcement activities."

The decision was reached after a two-month study ordered by Mr. Alexander immediately after he entered office. The study showed that the function performed by the Staff could be carried out by other units of the IRS having responsibilities for enforcement and administration of the tax laws.

The staff was originally formed in 1969 as a result of inquiries made of IRS by the Permanent Subcommittee on Investigations of the Senate Committee on Government Operations. At that time, in the wake of civil disruptions and demonstrations by "extremist" organizations, the Subcommittee raised questions concerning the financial resources available to these organization. There was evidence that some of the organizations which enjoyed tax exempt status were not complying with the tax laws. The assignment of the Staff was to gather information on the sources of funding of these organizations and to check the income tax status of the organizations and their principals.

The data-gathering work of the group is presently confined to tax resistance organizations and those individuals who publicly advocate noncompliance with the tax laws. "The IRS will continue to pay close attention to tax rebels," Mr. Alexander said, "but political or social views, 'extremist' or otherwise, are irrelevant to taxation; the work of the Staff as a separate unit will be phased out."

MANUAL SUPPLEMENT: SPECIAL STAFF SERVICE ACTIVITIES

August 13, 1973.

Section 1. Purpose

The purpose of this Manual Supplement is to abolish the Special Service Staff, Collection Division, National Office.

Section 2. Background

The Special Service Staff was established in July 1969 to serve as a central point for coordinating information relating to organizations or related individuals involved in tax strike, tax register, and tax protester activities, and distributing it to appropriate district offices. A determination has been made that it is no longer necessary to continue this activity.

Section 3. Abolishment of Special Service Staff

The Special Service Staff, Collection Division, Office of Assistant Commissioner (ACTS), is hereby abolished.

Section 4. Effect on Other Documents

IRM 1113.654 is revoked and Exhibit 1113-5 is amended. This "effect" should be noted in pen and ink on the text and Exhibit with a reference to this Supplement.

The following Manual Supplements dated April 12, 1973, are revoked: 51G-93, CR 1(16)G-18, CR 42G-300, CR 5(17)G-25, CR 93G-133, CR (10) 4G-3, and CR (11)6G-70.[1]

DONALD C. ALEXANDER,
Commissioner.

Senator HARTKE. Do you know to what extent the members of the special services staff audited the returns of private foundations or other exempt organizations?

Mr. ALEXANDER. They did not audit any returns, Mr. Chairman.

Senator HARTKE. I have some questions which I do not really know from what you have indicated before, you told me on the effect of the payout requirements, and which it required a pay-out of the minimum of the assets; the problem I present in this is simply the fact that you do not know the market value of the assets, as you have indicated before.

Is that fair?

Mr. SCHOENFELD. On an aggregate basis, Mr. Chairman, we have not been able to tabulate, really, that information until this year. Beginning this year we will be tabulating that information.

Senator HARTKE. And you will be able, then, to make the determination as to whether or not the individual foundations are complying, or just the aggregate?

Mr. SCHOENFELD. Well, that is many steps to make the conclusion that you suggested about compliance. We are just going to be getting the figure initially. There will be other ways we go in order to check compliance with the minimum payout provision.

Mr. ALEXANDER. Mr. Chairman, I would like to discuss one specific of the compliance problem that you have mentioned, because we do have some figures that may be helpful to you, sir.

In 1973 the aggregate tax imposed on section 4940 of the Code, the 4-percent tax, was $76.6 million. Of that aggregate, Mr. Chairman, capital gains incurred by the 10 largest foundations accounted for $17 million of this $76 million total, because those foundations had

[1] Related annotations should be removed, with a reference to this Supplement, from IRM 1(16)41, Physical and Document Security Handbook; IRM 4260; IRM 5100; 100 of IRM 5(17)00, IDRS Handbook; IRM 9370; IRM (10)400; and IRM (11)671, Exempt Organizations Handbook. (At IRM 9370, remove reference to CR 93G-134, shown in error instead of CR 93G-133.)

over $400 million in capital gains. So we do have a showing of two things, one of which is the possibility that the tax produced under section 4940 of the Code for 1973, which looms very large in comparison with the cost of our compliance effort in the exempt organizations area for that year, may not be indicative of the future, because of the large capital gains incurred. And we have another suggestion of compliance. Why were those capital gains incurred when the organization would suffer a 4-percent loss of principal, 4-percent loss of the amount of the gain, Mr. Chairman, which in many cases amounts to almost 4 percent of the total because of the lack of base, if it were not for the organization's duty and its recognition of the duty to comply with one of the provisions you mentioned, the provision regarding excess business holdings in section 4943 of the Code? So we do have some indicators.

Now, what we need to do—and you have brought out our obligation in this respect very clearly this afternoon, Mr. Chairman—is do a better job of the second facet of our work in this area, compiling meaningful statistics which will give this committee a better view of the effect of the 1969 legislation and a road map for changes that the committee may have in mind. We can give this committee, and have given this committee through the letter from the Secretary of the Treasury, a suggestion for one change that the committee might consider, which is the reduction of the 4-percent tax to 2 percent. If, indeed, the tax is in some part a measure of the cost of administering these provisions, then the tax is too great, because the cost has not been there.

Senator HARTKE. Well, part of this is computerized, right? Part of this information is being computerized?

Mr. ALEXANDER. Yes.

Senator HARTKE. Now, we did make a suggestion to you on February 12 that you put eight additional items reported on the 990 PF form be included in that computer inventory. In our opinion, we thought they might be very helpful in getting a better picture of the foundations' assets and investments, as well as to determine the problems that some of the foundations might be having with the 1969 act. On April 12 you indicated that you would give consideration to our request.

Now, can we have any more understanding better than "consideration"?

Mr. SCHOENFELD. There has been a need to gather more information. We have—and I think as our letter explains—we have different sources of information. We have information we can get on a regular recurring basis, and there is information we can get from special, one-time studies. We do have underway a number of special, one-time studies to provide the kind of information that you suggested in your letter.

We have one study that will tell us about the completeness of returns. We have another study that will tell us about the statistics of what these returns show about all private foundations. And we have the TCMP program where, also, we continually take a look at what our master file has and what our master file should have. The reason that something that may not go in the master file is because this

is something that requires continual updating. Sometimes we feel we can provide better information by focusing on a special subject or a special problem or a special area and doing a statistical search in this way.

Right now we think that the information that you asked will be available on some statistical studies that will be completed on the returns that are currently being filed for the 1973 processing year.

Senator HARTKE. In other words, you are saying that the information we requested in those specific questions is going to be available to you from another source?

Mr. SCHOENFELD. Yes, sir, if not from our master file. It ought to be available from other sources.

Senator HARTKE. But that will be only a one-shot operation will it not?

It will not be on a recurring basis?

Mr. SCHOENFELD. If there is a need to gather this information on a recurring basis, if we can justify on a cost-benefit basis, we certainly would put it on a recurring basis.

Senator HARTKE. Let me ask you what would be the cost of including these eight items in a computerized bank?

Mr. SCHOENFELD. That was in my letter, and my copy is nearly illegible.

Mr. ALEXANDER. Mine is completely illegible. You have a better copy than I do.

$30,000 start-up cost and $10,000 annual cost—or it is $50,000 start-up cost? I am unable to read it, Mr. Chairman.

Senator HARTKE. It says $50,000 not $30,000. Let me correct it; $50,000 starting cost and $10,000 in annual costs, and the total budget for auditing is a little over $9 million, almost $10 million.

Is that right?

Mr. ALEXANDER. Mr. Chairman, we are talking about auditing private foundations alone. That $9 million figure is small, because it did not include the October pay raise. So we are talking, Mr. Chairman, about a very small figure in comparison with the aggregate cost of auditing the private foundations.

Senator HARTKE. That is what I am saying. For $50,000 start-up costs and a $10 million budget, and a $10,000 annual cost beyond that. Do you not think that the information would be worthwhile, instead of relying upon these other sources, which at best would be a one-shot operation?

Mr. ALEXANDER. Can we get this information off the tax return?

Mr. SCHOENFELD. Yes. That is where the information comes from.

Mr. ALEXANDER. I think this would be extracted from the tax return.

Recalling your letter to me, Mr. Chairman, I think that the data that you mentioned would be extractable from the tax returns as presently constructed. You see, we have an added cost and one that we share with the foundation community. If we put anything on the tax return that is not essential to be on the tax return. We are constantly bombarded with requests to gather statisical data through tax returns, and we resist that whenever we can.

We resist it because not only does it involve expense to us and, therefore, expense to the public, but it also involves a direct expense and a very great one to the public. The more we have to add to tax returns, the more we add items that are not necessary to the computation of tax liability, the more costs we impose upon the public and the more difficult we make it for the public to comply with their responsibilities.

Now, I think we are talking about information here which can be compiled from our tax returns as now constructed. And the cost that we are talking about is limited to the cost of compilation and recording. The input cost and, as you point out, Mr. Chairman, the relative costs are small.

We examine each item from the standpoint of the benefit and the cost, because we do have a responsibility, which we certainly recognize, to administer the tax system as well as we can, at the least possible cost that we can. There are certain things that we would like very much to do that we cannot do.

Senator HARTKE. The question of the special assistant commissioner of IRS for exempt organizations, in both the House and the Senate pension bills which are now in conference, it is established a special assistant commissioner for tax exempt organizations. And the reasoning, I suppose, was to give more importance to exempt organizations within the IRS. I suppose it is more or less a compromise between the present situation and those who opt for an independent agency for exempt organizations.

On page 7 of your statement to us, you said, "We do not expect major changes in our activities in enforcing the exempt organization provisions of the Internal Revenue Code." That is from the pension bill provisions.

Now, if you do not expect any major changes from the establishment of an assistant commissioner for exempt organizations other than a more unified policy and more unified treatment of exempt organizations, why do you need a special assistant commissioner at all?

Would it not mean just more taxpayers' expense and additional bureaucracy?

Mr. ALEXANDER. Mr. Chairman, I was asked almost the same question at my confirmation hearing, and I said we did not need one. I would repeat that answer if we did not have the new obligations imposed upon Internal Revenue, or to be imposed upon it, in connection with the pension legislation, which make for great new responsibilities which we will undertake to meet effectively to the best of our abilities.

With these responsibilities in the pension area, there comes a necessity for uniform functional guidance, for uniformity of decision about qualification or nonqualification throughout the country. And we think that putting exempt organizations with pension plans, which, after all, are a certain category of exempt organizations, makes sense and should make for greater uniformity, and, I hope, better administration and more responsive administration in the exempt organization area.

So I do not think we needed this office but for enactment of H.R. 2. But I do think we need it if H.R. 2 as enacted. I think it will be helpful in the exempt organizations area in unifying functional work, in bringing together my friends to my left in technical and my friends to my right in compliance, both of whom have functional responsibilities in a field that demands uniform treatment and uniform understanding I think it will be helpful. But for enactment of the pension bill, I do not think it is necessary.

Senator HARTKE. I see.

All right.

On page 7 of the materials which you submitted in response to my questions, you make the statement you get your personnel, your present personnel, from lawyers, recent law school graduates, people with accounting backgrounds, and people—here is the emphasis—people with experience in the field of exempt organizations.

Now, are these people with experience in the field of exempt organizations from the foundations and the grantee organizations themselves, or are they people who have gotten their experience from foundations within the IRS, or just where do they come from?

Mr. ALEXANDER. I would like to call on Mr. Tedesco to respond to that question. He is best qualified.

Mr. TEDESCO. Mr. Chairman, speaking from the technical side of this rather than the compliance side, most of the people that we hire are either from the field or they have worked in exempt organizations.

Senator HARTKE. You mean the field of the IRS?

Mr. TEDESCO. That is right.

Senator HARTKE. All right.

Mr. TEDESCO. Or they are lawyers just out of school or people who have given up practice and things like that. But most of our people in the technical aspect are lawyers, new lawyers, hired.

Senator HARTKE. And have really come from the exempt organizations primarily, or do they represent them?

Mr. TEDESCO. No, this statement does not apply particularly to my branch. It might in the field; I do not know.

Mr. SCHOENFELD. The examiners in the field are usually hired as accountants who begin their work as Revenue agents, and after they have worked for a while, generally in the income tax area, receive specialized training in the exempt organization area.

Senator HARTKE. In the field of rulings which pertain to exempt organizations, you indicated that you had published 22 of 2,351 rulings which have been made since 1969.

Now, what is the benefit of making a rule unless it is published to the extent so foundations will have an idea what the ruling really means and how it will affect them?

Mr. GIBBS. Mr. Chairman, I would like to reply to that by clarifying the statistics which we have given you. You will notice that the statistics are 2,351 ruling requests, not rulings issued, but rulings that had been filed with us for answer, and that during this period of time we have published 22 revenue rulings.

I would like to explain that, because I think that you have somewhat a distorted view of our process, just on the basis of those num-

bers. First of all, an amount of perhaps up to half of the 2,351 are rulings that relate essentially to the same issue. For example, under one of the sections of the Code that was added in 1969, the excise tax section, there is a provision that a foundation is subject to an excise tax on taxable expenditures if the grant does not qualify as a scholarship. And we have had easily over 1,000 of those requests on that one issue alone, and it would be the same issue in every case.

Second, of the ruling requests that are received during the period of time that we are developing the regulations, because we recognize that individual taxpayers must have an answer to their specific question, we will go ahead and issue letter rulings on which that particular taxpayer can rely but other taxpayers cannot.

Now, before that ruling is issued, we will, of course, coordinate with those people in the Treasury who are preparing the regulations. However, we do not publish that ruling until after the final regulations are published, and for several very good reasons.

First, the regulations themselves may answer that question; and, secondly, the ruling that we give on an interim basis—and this is true of all of our rulings—may well be inconsistent with the final position of the Treasury, as indicated by the final regulations.

Senator HARTKE. I understand this procedure very well. But the point of it is that what you are saying is that in those areas in which there is some difference of opinion and in which there is a sincere problem, that if a person makes an application for a ruling, he gets his answer, but that information in the meantime, the rest of them have to take a blind stab at it.

Is that not correct?

Mr. GIBBS. In terms of taking a blind stab at it, they, too, can come and ask us the same questions. As I told you, Senator, having been in private practice, the questions are pretty well defined long before they reach the Service. And just because it could be very well misleading if we should publish those private rulings and taxpayers had the feeling that they could rely on those without coming and asking us for the same ruling, because one taxpayer cannot rely on another taxpayer's private ruling.

Senator HARTKE. I know that rule.

Do you approve of that rule?

Mr. GIBBS. Yes, sir, I do. I certainly do. Because if you did not have it, we would, in effect, eliminate, in my opinion, the letter ruling system. Because if you had to have the levels of review which are given to our regulations and to our revenue rulings for every private ruling we would not be able to issue a private ruling on a timely basis, and, therefore, our letter rulings project and system would simply not be responsive to the needs of the taxpayers.

Senator HARTKE. And the question of scholarships, just a corollary to that, there is this question about scholarships for employees and their families which has not been published.

Is that right?

Mr. GIBBS. That is correct, sir. Well, the final regulations have been published under the provision, and we are, at the present time, processing applications that are received. This is, as I am sure you know,

Mr. Chairman, a very difficult area because of the potential conflict between the provisions in the charitable organizations area of section 49.45 and the provisions in the income tax section under section 117, which involve the question of the taxability of the scholarship to the recipient.

And what the Congress has done has been to import tests in the income tax side into the regulations, or into the statute, on the charitable organizations side. That is to say, a charitable organization which is—a charitable foundation which is making grants in the form of scholarships to employees would only have their program qualify if it also meets the conditions of income taxation under section 117 to recipients.

And I submit to you that puts us in somewhat of a dilemma, because in one sense if you take a look at the law that is developing under section 117, it would indicate that many of these foundations, company foundations, company scholarship foundations, could no longer qualify, although they have qualified in the past. On the other hand, if you disregard those sections, then inevitably you will erode the law that has been established in the 117 area.

We are attempting to resolve this dilemma at the present time and hope to in the near future.

Senator HARTKE. What would be your reaction to a change in the tax code which would permit an organization seeking tax exempt status to get a declaratory judgment on the issue from the Tax Court with the right of appeal to the court of appeals?

Mr. ALEXANDER. Mr. Chairman, we favor the right of an organization seeking tax exempt status, or an organization which has been tax exempt or considered tax exempt and wants to oppose the revocation of tax exempt status, to have an opportunity to go directly to the Tax Court within a short period of time and have that organization's claim for exemption in the first place or continued exemption in the second place heard by a judge as promptly as possible, as easily as possible.

I spoke in January in Atlanta before the state attorneys general in favor of this proposition. I have been in favor of it long before then, and I recently had two chances to reiterate the support of the Internal Revenue Service and the Treasury Department for this proposal. I hope that Congress will act promptly and favorably on it.

Senator HARTKE. Do you believe there should be in the tax code a prescribed method of determining the fair market value of foundation assets, or do you believe that it is better to do this by an administrative procedure?

Mr. ALEXANDER. I think it is better to do it, Mr. Chairman, by sound administrative procedures.

Now, we do have in the tax code a determination, or partial determination, of when or how frequently assets ought to be valued. As I recall, that is section 4942. I think that the determination of fair market value should be provided in the regulations and in a way that is understandable and usable by the foundation community and administerable by the Internal Revenue Service.

Senator HARTKE. How would that be defined?

Are you going to define that by——

Mr. ALEXANDER. Well, fair market value is a term that may defy description, unless one wants to be, one, very long, and two, very arbitrary. The method of determination of fair market value does not defy description, however, but it is a method that may change from time to time, and a method that may make sense today may not make sense next year. It is rather easy to value listed stocks under present circumstances, however, but who can predict the markets in the future. It is rather difficult, quite difficult, to value unlisted stocks and interests in real estate, for example.

And accordingly, if my memory serves me right, we do not require as frequent evaluation or as exact a determination in these more difficult areas as we do in the easier area of listed stocks.

What we need to do here is have an understanding and a melding of our duty to administer the law and carry out what Congress expected of us with the taxpayers' duty to comply with the law and we should adopt reasonable standards that make sense.

Now, I think we have done that, but we do not reach final design, we do not get embedded in stone. And we are certainly open to suggestions as to how to do this job better. We have received several helpful suggestions from the foundation community recently, and we are studying those at this time.

Senator HARTKE. All right.

That is all the questions I have today.

I want to thank you for taking your time and being here with us today.

I may have some more questions for you in writing, also for Assistant Secretary of the Treasury, Mr. Hickman, and I hope we can get a record which will be somewhat helpful to the committee.

These hearings are adjourned, subject to the call of the Chair.

[Whereupon, at 4 p.m., the subcommittee was adjourned, subject to the call of the Chair.]

APPENDIX A

Communications Received by the Committee on Finance Expressing an Interest in These Hearings

REAVIS, POGUE, NEAL & ROSE,
Washington, D.C., May 10, 1974.

Re Private Foundation Hearings.

Senator VANCE HARTKE,
Chairman, Subcommittee on Foundations,
Senate Committee on Finance,
Washington, D.C.

DEAR SENATOR HARTKE: We wish to bring to your attention a problem affecting virtually all organizations which qualify for tax exempt status under Section 501(c)(3) of the Internal Revenue Code of 1954 (the "Code"), i.e., organizations organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary or educational purposes, and particularly thase organizations which are "private foundations" as that term is defined in Section 509 of the Code.

The problem to which we are referring arises as a result of the enactment of the so-called "private foundation" provisions under the Tax Reform Act of 1969 and relates to the manner in which these organizations can determine with a reasonable degree of certainty the fair market value of property contributed to them and the fair market value of property held by them. The determination of fair market value of property is a critical factor in the analysis which a Section 501(c)(3) organization must make in order to first determine whether it is a private foundation and, if so, the extent of its liability for the special excise taxes imposed pursuant to Section 4940 *et. seq.* of the Code.

Under existing law there is no method by which such organizations can establish, with any reasonable degree of certainty, fair market value. The absence of such a statutory provision, we submit, results in substantial administrative problems for these organizations. We therefore urge your Subcommittee to resolve this problem (which was created by legislative action—*i.e.*, the enactment of the Tax Reform Act), by either taking some corrective legislative action (*i.e.* the adoption of a minor administrative provision set forth below) or obtaining assurances from the Internal Revenue Service that they will adopt appropriate administrative procedures to deal with the problem.

The degree to which a Section 501(c)(3) organization is affected by the determination of the fair market value of property contributed to it as well as the fair market value of its other assets can be illustrated by the following discussion of just some of the Code provisions where this is a factor. Section 509(a)(2) of the Code provides, in part, that an organization will not be a private foundation if it normally receives more than one-third of its support in each taxable year from contributions from persons other than "disqualified persons" (as defined in Section 4946 of the Code). Section 4946 in turn defines a "disqualified person" to include a "substantial contributor" to the foundation which under Section 507(d)(2)(A) is defined to mean any person who has contributed more than $5,000 to a private foundation if such amount is more than two percent of the total contributions received by the foundation before the close of the taxable year in which the contribution was made.

As can be seen from the foregoing, the valuation of property contributed to a Section 501(c)(3) organization is critical in determining whether the organization is a private foundation. Obviously, if all contributions were in the form of cash or securities traded on a national exchange, valuation would not pose a substantial problem. However, contributions are made in all forms of property, *e.g.*, stock in unlisted corporations, land, art objects, etc.

This problem is further highlighted by the fact that in determining whether it is a private foundation an established organization must, in effect, make a retroactive determination of fair market value. Section 507(d)(2)(B) provides

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first, that each contribution shall be valued at its fair market value on the date it was received; secondly, that for purposes of applying the two percent-of-total contributions rule, all contributions made to a foundation in existence prior to October 9, 1969 shall be treated as having been received in one year; and finally, that any person who becomes a substantial contributor at any time shall remain such for all subsequent periods.

The valuation question continues to be a critical fact even after an organization is determined to be a private foundation. For example, the status of a person as a substantial contributor (which determination requires a fair farket value determination) in turn affects the permitted holdings of a foundation in the stock of a corporation. Section 4943(c)(2)(A)(ii) provides, in this respect, that the permitted holdings of a private foundation shall be reduced by the percentage of voting stock owned by all disqualified persons, including a substantial contributor. To the extent that a foundation holds stock in excess of the permitted amount it is charged a tax equal to five percen of the value of such excess holdings. Section 4943(a) of the Code.

Another example of this problem is illustrated by Section 4942 of the Code which imposes a tax of fifteen percent on te undistributed income of a private foundation. Pursuant to this provision, a private foundation must distribute the higher of its adjusted net income or the "minimum investment return". Section 4942(d). The minimum investment return, in turn, is determined on the basis of the fair market value of all assets of the foundation in a given taxable year. Section 4942(e) of the Code.

As can be seen from the foregoing, the determination of fair market value is critical to all Section 501(c)(3) organizations. However, neither the present law nor Income Tax Regulations (except for determining the "amount involved" in an otherwise unintended act of "self-dealing"—see Reg. § 53.4941(e)-1(b)(2)(iii)) provide a method by which an organization can establish fair market value with any reasonable degree of certainty that the determination will not be subsequently challenged by the Internal Revenue Service. In this rgard, it is notd that it is the general policy of the Internal Revenue Service not to issue private rulings on basically factual issues.

In view of the obvious importance to an organization to establish fair market value and the penalties which could be imposed in the event that the Internal Revenue Service successfully challenges an organization's good faith determination, we respectfully submit that the Code be amended so as to set forth acceptable means by which an organization can establish fair market value with a reasonable degree of certainty, and thus be assured that it is in full compliance with the Sode provisions enacted by the Tax Reform Act of 1969.

We therefore respectfully submit that the Subcommittee give serious consideration to either (1) amending relevant provisions of the Code so as to make it clear that, absent fraud or other improprieties, an independent appraisal obtained from an unrelated appraisal company would be recognized by the Internal Revenue Service as exidence of the fair market value, or (2) eliciting some assurances from the officials of the Internal Revenue Service that they will adopt some administrative procedure to deal with this problem. Under either of the foregoing proposals and provided the organization made a good faith attempt to obtain a bona fide independent appraisal as to fair market value, that determination would not be disturbed unless it was subsequently determined tht the appraisal was not made in good faith or was not determined on the basis of a generally accepted valuation method.

Whether the foregoing proposals or some other reasonable alternative is acceptable, we trust you will agree that Section 501(c)(3) organizations face a serious problem in this area which is not of their own making, but rather is a product of the Tax Reform Act of 1969. Accordingly, we hope that your Subcommittee will give serious consideration to the resolution of this legislatively-created problem.

If you wish to discuss any aspect of these proposals in further detail, please contact the undersigned or Mr. Lee Scher at 293-2030.

Respectfully submitted,

JAMES T. O'HARA.

YORK BEACH, MAINE, *May 17, 1974.*

Mr. MICHAEL STERN,
Staff Director, Committee on Finance, Dirksen Office Building,
Washington, D.C.

DEAR MR. STERN: I hope the gentlemen on the sub-committee will be sympathetic to the plight of the small museums who as private foundations have to pay the 4% excise tax.

I am affiliated as a volunteer with the Old Gaol Museum Committee in York, Maine, one of three museums in Maine accredited by the American Association of Museums.

We maintain two buildings, the Old Gaol built around 1720, and the Emerson-Wilcox House dating from 1740. Funds are constantly needed for restoration work on the buildings and conservation work on the collections. Our excise tax for 1973 was $946, which meant cutting our strained budget even more.

Since the Old Gaol was opened as a museum in 1900, residents of York and tours of school children have paid no admission fees. The Committee feels that this is an important part of our educational duty, but we may be forced to change this policy and charge towns people.

I beg you to change the laws and eliminate the 4% excise tax on small museum type foundations.

Sincerely,

MARGARET B. ELLIS.

WORCESTER, MASS, *May 18, 1974.*

Mr. MICHAEL STERN,
Staff Director, Committee on Finance, Dirksen Office Building,
Washington, D.C.

DEAR SIR: As a trustee of the Society For The Preservation Of Historic Landmarks In York County (Maine) I write in protest against the assessment of a tax on the income of small previously tax-exempt museums. Under the provisions of the 1969 Tax Reform Act small community-serving non-profit organizations are finding their income returns from modest endowments are being increasingly absorbed not only by the tax levied under this law but especially by the paper-work required in its computation.

I urge some better means be found for controlling abuses of the tax-free privilege of small community-serving museums.

Very sincerely,

NATHANIEL WHEELER.

POWERS & HALL,
Boston, May 31, 1974.

MICHAEL STERN, Esq.,
Staff Director, Committee on Finance, Dirksen Office Building,
Washington, D.C.

DEAR MR. STERN: In connection with the current hearings of the Subcommittee on Foundations, I am enclosing my letter of May 31, 1974 and enclosed memorandum to Commissioner Donald C. Alexander relating to the problem of disposition of excess business holdings under Sec. 4941 of the Internal Revenue Code.

I trust the Committee will feel that the proposals made in the memorandum have merit and will see fit to take action favoring their adoption.

Sincerely yours,

RICHARD F. BARRETT.

Enclosures.

POWERS & HALL,
Boston, May 31, 1974.

Hon. DONALD C. ALEXANDER,
Internal Revenue Service,
Internal Revenue Building,
Washington, D.C.

DEAR MR. ALEXANDER: Enclosed are two copies of a memorandum recommending action by the Internal Revenue Service relating to the administration of Secs. 4941 and 4943 of the Code and the disposition of excess business holdings under the transitional rules of P.L. 91-172, § 101(1)(2)(B).

I know you are aware of the problem in this limited area facing a limited number of taxpayers and private foundations, and the objective of the regulations under Sec. 4941 to provide a feasible solution to the problem. The action recommended in the enclosed memorandum is limited and simple, and merely provides several methods of briefly clarifying the regulations so as to permit them to be employed to achieve their objective.

No aspect of the action recommended involves an advance determination of valuation or any change in the normal timing for determination of value by the Service and imposition of the Sec. 4941 initial tax. The proposed action eliminates rather than adds complication to the achievement of the regulations' objective.

I think it is also worth noting that providing a feasible method to permit taxpayers to proceed in good faith to eliminate excess business holdings avoids a potential burden on the Service of substantial size and duration in litigating market value and exposure to large penalties and reversal of transactions.

I am pleased to advise you that the following endorse the enclosed memorandum and recommended action and have asked me to so advise you and recommend to you on their behalf your approval and favorable action:

Mrs. Marion R. Fremont-Smith
Choate, Hall & Stewart
Boston, Mass.

Kenneth W. Bergen, Esq.
Bingham, Dana & Gould
Boston, Mass.

Norman A. Sugarman, Esq. Robert S. Bromberg, Esq.
Baker, Hostetler & Patterson
Cleveland, Ohio

James T. O'Hara, Esq.
Reavis, Pogue, Neal & Rose
Washington, D.C.

Theodore A. Kurz, Esq.
Debevoise, Plimpton, Lyons & Gates
New York, New York

The transitional rules expire December 31, 1974, and I trust that it will be possible to give consideration promptly to our recommended action. I will plan to telephone you shortly to discuss our proposals with you and to be of any further assistance in this matter that I can be.

Copies of the memorandum and my letter to you are being sent to Michael Stern, Staff Director, Committee on Finance, Senate Office Building, Washington, D.C., in connection with the current hearings of the Subcommittee on Foundations.

Respectfully,

RICHARD F. BARRETT.

Enclosures.

MEMORANDUM

The dilemma presented to taxpayers by Secs. 4941 and 4943 enacted by the 1969 Act is well-recognized. On the one hand, by Sec. 4943 Congress required private foundations to dispose of excess business holdings stock, and on the other hand by Sec. 4941 a most severe penalty was imposed if the disposition was to the only available, realistic market in most cases, i.e., one or more disqualified persons.

Congress recognized the desirability of promoting the disposition and assisting taxpayers in accomplishing it, by amending Sec. 537 to approve redemptions of the stock under Sec. 531 and enacting P.L. 91-172, § 101(1)(2) to provide a transitional period through December 31, 1974 in which disposition might be made to a disqualified person at fair market value without Sec. 4941 penalty.

The dilemma for most taxpayers still persisted, however, since the fair market value of the stock of family, closely-held corporations is inherently uncertain and incapable of being established with precision in advance of review by the Internal Revenue Service. Accordingly, the disqualified person purchasing from the foundation was faced with the clear risk of a Sec. 4941

penalty on the full fair market value as ultimately determined, for each of three years pending audit, plus reversal of the transaction. This could mean in existing cases penalties in the millions accompanied by complete abortion of the transaction.

The problem as condensed above is presented in more detail in a letter of the writer to Lee H. Henkel, Jr., Chief Counsel, dated June 12, 1972, a copy of which is attached. It is also discussed in the leading article on the subject in 31 Annual N.Y.U. Institute 1311 by Theodore A. Kurz, Debevoise, Plimpton, Lyons & Gates, New York, formerly Treasury Department Tax Legislative Counsel attorney at the time regulations dealing with the problem were under consideration.

Recognition of the problem and the need for a solution by the Treasury and the Commisisoner's office resulted in the issuance of regulations adopted in final form April 16, 1973, incorporating provisions that a "good faith effort" to determine fair market value would confine the application of the penalty to the excess of the fair market value of the stock transferred over the amount received by the foundation, and eliminating reversal of the transaction if such excess were paid. Unfortunately, the definition of good faith effort makes it impossible for a taxpayer to proceed with assurance of compliance with the definition, and clarification of the definition in the manner described below is needed to make the regulations usable and achieve the desired end of permitting taxpayers to proceed in good faith to eliminate excess business holdings.

The specific clarification required is with respect to (a) the requirement that the person making the valuation is not in a position by stock ownership "or otherwise" to derive an "economic benefit" from the value utilized—the phrases "or otherwise" and "economic benefit" are broad generalizations not capable of interpretation by the taxpayer with the advance precision and assurance necessary to proceed with safety; (b) the requirement that "a generally accepted method for valuing" comparable stock be used again, as under (a) above, the taxpayer cannot in most cases proceed with any certainty of compliance since the valuation of closely-held stock by consensus is a notoriously imprecise and speculative process without any established method one can depend upon the acceptance of by the Internal Revenue Service; (c) the provision that successful compliance by the taxpayer with the regulations will, however, only "ordinarily" establish the required good faith effort.

The methods recommended for clarifying the regulations are as follows.

1. With respect to Reg. 53.4941(e)-1(b)(2)(iii) (a) and (b) dealing with "good faith effort", public ruling by Revenue Procedure, regulations amendment or other available method that

(a) An independent bank, investment broker, brokerage firm or other appraising organization, with no direct or indirect stock ownership in either a fiduciary or non-fiduciary capacity in the private foundation or the disqualified person, shall not be deemed to be in a position, whether by stock ownership or otherwise, to derive an economic benefit from the value utilized solely by reason of prior or current arms'-length business dealings with the private foundation or the disqualified person in the nature of customary banking, creditor, investment, brokerage, advisory services or other normal operations of the appraisal organization, or solely by reason of any such dealings taking place or anticipated to take place subsequent to the valuation.

(b) The appraising organization utilizes a generally accepted method for valuing comparable property, stock, or securities as required for a good faith effort, if in making the valuation, it applies, for example, in the case of stock, such of the valuation principles set forth in Rev. Rul. 59-60, or, in the case of securities or other property, whatever factors customarily used by it in making similar valuations, as in its judgment the appraising organization considers appropriate and applicable in making the particular valuation.

2. Adoption of a publicly announced policy of issuing advance rulings to taxpayers as to whether as required for "good faith effort" the person making the valuation, by reason of compliance with the requirements set forth in paragraphs (a) and (b) of method 1 above, is in a position to derive no economic benefit from the value determined and has utilized a generally

accepted method for valuing the property, stock or securities involved. The ruling would make *no determination or agreement as to the correct fair market value*, which would remain to be determined in the usual course of procedure.

3. Public ruling by Revenue Procedure, regulations amendment or other available method that fair market value has for purposes of self-dealing been paid if there is (a) a binding obligation that the purchaser will pay at least the fair market value as finally determined; (b) payment of the amount of underpayment, plus interest at the applicable percentage set forth in Sec. 4942(e)(3), within a limited period after final determination of value, such as 90 days, and (c) an attachment to the foundation's annual information return for the year in which the transaction occurs, setting forth (i) the relevent information with respect to the transaction including a description of the property, the price and method of payment, the appraiser employed, the method of valuation utilized and other appropriate detail; and (ii) a representation that both the purchaser and seller have agreed to be bound by the terms of (a) and (b) above.

Methods 1 and 3 above would permit the taxpayer to proceed promptly without a ruling, and would eliminate the need for the consideration and issuance of an advance ruling by the Service. Method 2 simply follows the tradition of advance rulings to provide taxpayers with assurance of result in major tax transactions. These methods eliminate the uncertainty of the present regulations and permit said regulations to achieve the objective for which they were intended, but which in their present form they do not fully achieve.

At the time that action such as is recommended is taken, further action is recommended to make clear that the restriction of self-dealing is eliminated with respect to Sec. 537 if the good faith effort requirement is met.

JUNE 12, 1972.

LEE H. HENKEL, Jr.,
Chief Counsel, Internal Revenue Service, Internal Revenue Building, Washington, D.C.

DEAR MR. HENKEL: Sections 4943 and 4941 of the Internal Revenue Code present a most difficult situation to certain private foundations owning excess business holdings. The problem is one I believe you are familiar with. I have had extended discussions on the subject with the office of the Tax Legislative Counsel, and Mr. John Chapoton has suggested I furnish you with my views and recommendations.

Section 4943 requires the private foundation in order to avoid penalty to dispose of its excess business holdings. These holdings in the typical situation are necessarily by the definition of excess business holdings not marketable, traded ecurities, but stock in a closely-held, family-type corporation without an established fair market value. If a substantial amount of stock is involved, the only realistic market and source of funds is usually the issuing corporation, which, again in the typical case, is a disqualified person. Sale of the nonmarketable stock to a person outside the disqualified persons group, if feasible at all, is in all likelihood available only at a bargain price in conflict with the purposes and interests of the foundation and its beneficiaries.

The net thrust of Section 4941 is, accordingly, to require the typical private foundation with excess business holdings to dispose of such holdings to a disqualified person if the disposition is to be realistic and representative of the true value of the stock held.

Section 4941 confronts the foundation with the rule and penalty of self-dealing involved in a transaction by the foundation with the disqualified person. The burden and penalty imposed on the parties can be most severe, with a potentially absurd result that could be amusing if it were not so punitive. Under Section 4941, if the price at which the stock is sold is not equal to or in excess of fair market value, a penalty is imposed on the self-dealing disqualified person. The penalty is at the rate of 5% on the full fair market value of the stock sold, not merely on the deficiency of the sales price from fair market value. Further, the tax is imposed for each taxable year, starting with the year of the transaction, until the transaction is corrected. The purchaser could therefore sit with the uncertainty awaiting audit and a determination for three years. My primary foundation client in this matter holds closely-held,

non-marketable excess business holdings of uncertain fair market value in the area of $5,000,000 to $7,000,000. Assuming a sale at $6,500,000 and a determination of $7,000,000, a penalty of $350,000 for each of three years could be imposed totalling $1,050,000.

The inequity in this is apparent. The ultimate absurdity, however, is the requirement that the transaction be "corrected" by a complete reversal of it, by return of the stock and the purchase price. The objective of Section 4943 of disentaglement of the foundation from the disqualified person has been frustrated. The frustration of the purchaser who failed to evaluate precisely a stock of undetermined value at the cost of a $1,050,000 penalty requires no comment.

We have in the foregoing the potential situation of Section 4943 imposing an obligation for action which Section 4941 exposes to serious risk of penalty. The inequity and undesirability of this appears clear. It is recommended that regulatory, ruling or other administrative action be taken to relieve the situation and prevent the potential result which is clearly unintended. I suggest that such action could be of the following nature:

1. Provision that determination of fair market value in good faith will relieve the disqualified person of penalty, even though a higher value is determined to be fair market value.

2. In the alternative, imposition of the penalty upon only the deficiency of sales price from full market value as determined.

3. In either case, correction of the transaction by further payment by the disqualified person of the deficiency, leaving the transaction a consummated act.

I trust you will feel there is merit in my interpretation of the problem and possible curative action. If I can in any way be of any assistance in your consideration and dealing with the problem, please be sure to call upon me.

Respectfully,

RICHARD F. BARRETT.

OTTERMAN AND ALLEN,
March 8, 1974.

Re 4% excise tax on tax exempt institutions.

SUBCOMMITTEE ON PRIVATE FOUNDATIONS,
U.S. Senate,
Washington, D.C.

GENTLEMEN: Our Senator, George D. Aiken has suggested that toward the end of March, he understood your committee would be taking up the question of the 4% excise tax.

Senator Aiken has been very sympathetic to our problem and has a great deal of material on it which I believe he will be happy to supply to your committee.

I have been treasurer and a member of the Scholarship Award Committee for the Chelsea High School Scholarship Fund since it was originated in 1959.

Chelsea, Vermont is a town with a population of less than 1,000 and has a very small high school from which I graduated in 1930 in a class of nine.

The Chelsea High School Alumni Association meets each year and is quite an active organization. It became concerned about graduating seniors and from voluntary contributions, has built up a scholarship fund with assets of a little over $10,000.00. The $500.00 approximate income each year is awarded to a deserving senior or seniors of the graduating class to encourage that person to acquire further education.

The award committee is composed of the president and secretary of the Alumni Association, the principal of the high school and two other persons who need not be alumni, who are elected at the annual meeting of the association.

After a great deal of red tape, and supplying untold numbers of documents and applications, we received from the Internal Revenue Service, July 28, 1969, a form L–178 stating that Chelsea High School Scholarship Fund, Id. #03–6008039, were exempt from Federal Income Tax as an organization described in Section 501(c)(3) of the Internal Revenue Code. This document stated in part, "You are not required to file Federal Income Tax Returns so long as you retain an exempt status". We were subsequently advised, however, that we were

rquired to file annually, returns for an organization exempt from income tax on form 990 and we have done so each year.

We have now been advised that we not only have to file a return, but we have to pay tax on our income and we also have to publish a statement in the local paper annually, that our annual report is available for inspection by any person interested and that a copy will be mailed free of charge to such persons as request the same.

It seems ridiculous to us that a small outfit, such as ours, trying to do some good, in a very small way, should be humiliated and harrassed by all of the paper work required to file this form 990 and to pay some six or eight dollars a year for advertising in a paper and paying the federal government some twenty odd dollars tax.

Our returns have been audited by Andover, Massachusetts, Burlington, Vermont, Washington, D.C., Cornwells Heights, Pa. and heaven knows what other source and we have been required to file forms, answer telephone calls and answer all of these various addresses.

Isn't there something your committee can do to help us and other organizations in a similar category.

We subscribe to three local papers and I have never seen any advertisement in any of them similar to the ones we are required to make, although I know it is a part of the law.

We hand you herewith a copy of our last annual statement and will be happy to supply you with copies of any of the multitude of forms which we have in our files.

I don't know whether the committee is fortunate or unfortunate to have someone who feels that he can devote as much time to the bookkeeping and accounting as there is in this very simple affair, but I have contemplated resigning many times because of the attitude of the I.R.S. and the stupidity of the law under which they are required to operate.

Sincerely yours,

G. ALLEN.

STATEMENT OF WILLIAM L. GRALA, VICE PRESIDENT, SMITHKLINE CORPORATION,[1] AND EXECUTIVE SECRETARY OF THE C. MAHLON KLINE MEMORIAL FOUNDATION

I welcome this opportunity to bring to your attention a matter of concern to SmithKline Corporation, which is a contributor to and the founder of the C. Mahlon Kline Memorial Foundation. The Foundation has also received contributions from the estate of C. Mahlon Kline and receives occasional individual, small gifts, primarily from employees of SmithKline Corporation in memory of co-workers.

SmithKline Corporation is a diversified corporation whose principal business is the manufacture of pharmaceutical products. We have approximately 18,000 employees and about 17,000 shareholders. Our products are marketed throughout the world, and we have annual sales around $450 million.

The C. Mahlon Kline Memorial Foundation was established in 1967 to perpetuate the memory of the late Mr. Kline, our onetime Board Chairman, who was a distinguished businessman and humanitarian and who was deeply interested in SmithKline employees and their families. At the end of 1973, the Foundation had a fund principal of about $470,000. It is, therefore, a small foundation.

This foundation is exempt from Federal Income Tax under Section 501(c)(3) of the Internal Revenue Code of 1954. It has been determined by the IRS to be a private foundation.

Since its inception, the Foundation has provided educational assistance in the form of scholarships for the college and graduate education of children of disabled or deceased employees of SmithKline Corporation and its subsidiaries. Thus far, 23 children of disabled or deceased employees have been helped through this program, 16 of whom are still attending undergraduate or graduate schools.

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[1] 1500 Spring Garden Street, Philadelphia, Pa.

Since the Foundation was established in 1967, a total of $38,825 has been contributed for these purposes. In 1973, the Foundation made grants for scholarships in the amount of $13,374. Grants cover one half of the grant recipient's tuition, but in no case are they less than $500. This scholarship program recently received a favorable determination letter from the Exempt Organizations Branch of the IRS; it will remain in effect providing the Foundation adheres to certain provisions.

The one provision in this determination letter that we feel is unfair restricts the Foundation in the number of scholarships it can award. We have been informed that the percentage of grants awarded by the Foundation cannot exceed 25% of the number of eligible applications received. In other words, if the Foundation receives only three scholarship applications in any one year, no child, however needy and deserving he or she may be, can receive scholarship consideration. It should be noted that several years ago IRS issued a favorable determination for the Foundation's program with no such restriction, and we have been operating in accordance with that approval since that time.

This limitation of 25% is of particular concern to us because the Foundation receives on the average less than four applications each year. This year, for example, we have but one applicant, and since awards are made only to the children of *disabled* or *deceased* employees of SmithKline Corporation and its subsidiaries, it is unlikely that numerous applications for aid will be received in any one year, because unfortunate cases of need of this kind do not occur in large numbers. It is illogical, in our opinion, that a single deserving applicant should be turned down for scholarship aid because a sufficient number of other persons have not applied.

I do not believe it was the intention of Congress when it enacted the Tax Reform Act of 1969 (PL91-72) to limit the number of scholarships that can be awarded by the C. Mahon Kline Memorial Foundation or other foundations having scholarship programs. This situation is particularly serious at present, because State and Federal governments cannot begin to meet these important scholarship needs due to other pressing priorities. It is therefore up to private sources of funding to help fill the gap; and we cannot do so, to the extent our small resources permit, as the result of the recently received determination letter from the IRS.

It should be noted further that this policy has neither support in the form of regulations to the Internal Revenue Code nor in the form of a published IRS ruling. As such, it has not been open to public hearings that would permit organizations with scholarship programs an opportunity to express their views.

I am appending to this statement a copy of the 1973 Annual Report of the Foundation and literature on the program that we give to our employees.[1]

We will appreciate consideration of the points made in this statement by members of the Subcommittee on Foundations of the Senate Finance Committee.

MARK SKINNER LIBRARY,
Manchester Center, Vt., May 7, 1974.

Mr. MICHAEL STERN,
Staff Director, Committee on Finance,
Dirksen Office Building, Washington, D.C.

DEAR MR. STERN: The Mark Skinner Library, Manchester, Vermont, has been re-classified by IRS as an Operating Private Foundation under a law passed by Congress in 1969 and made subject to an excise tax on all of its income at 4% without any allowance for necessary expenses of operation such as salaries, wages, heat, lights, books, insurance, general maintenance etc. etc.

Our existence as a library serving the public interest without public support is constantly in jeopardy. The Mark Skinner Library does not have adequate income to pay the proper costs of operations. Supplementary cash contributions, food and book sales, have been and still are necessary in order to

[1] The annual report was made a part of the official files of the Committee.

supply funds with which to pay bills of operation. We have functioned as an endowed organization, authorized by the Vermont Legislature for more than 75 years.

In order to function in the public interest, relief by exemption from this burdensome and unjust tax is imperative. This so-called excise tax is undeniably more devastating than an income tax would be from which we are already exempt.

Please submit these written statements at the scheduled hearings on May 13 and May 14 and all subsequent hearings.

SUMMARY OF PRINCIPAL POINTS

Mark Skinner Library, an educational organization, originally classified Income Tax free.

Tax Reform Act of 1969 Reclassification of Mark Skinner Library as an Operating Private Foundation, subject to Excise Tax 4% without any deduction for operating expenses.

Mark Skinner Library, an endowed organization chartered under Vermont Legislature laws more than 75 years ago. A library serving the public interest, without public support, constantly in jeopardy due to inadequate income to pay proper operational costs.

In order to function it is imperative Mark Skinner Library be classified exempt from the burdensome and unjust excise tax.

Sincerely yours,

EARLE E. STORRS, *Treasurer.*

THE BELLE PEABODY BROWN FOUNDATION,
Tilton, N.H., May 21, 1974.

Hon. NORRIS COTTON,
U. S. Senate,
Washington, D.C.

DEAR SENATOR COTTON: It has just come to my attention that Senator Vance Hartke's subcommittee on foundations held a hearing on the way the Tax Reform Act of 1969 has affected the ability of foundations to serve grantees.

I would like to impose on the committee's valuable time with the following thoughts, and especially how it affects at least one small charitable foundation here in New Hampshire. I am sure there must be many others with similar problems.

I don't wish to bother you with a lengthy story, but a brief recap of how this Foundation came into being might help. In 1957 Mr. Arthur S. Brown, President and only stockholder of the Arthur S. Brown Manufacturing Company, died without kith or kin. He left his entire holdings to the above foundation with the primary stipulations that the company employing 150 to 200 people be kept in existence (it fills a small but very vital role in industry) so they and their families would have a work place. In addition, it was his desire to help financially needy children, particularly crippled children, wishing to go to college; and other worthwhile charitable endeavors on a local basis (such as hospital expansion, YMCA, Community Funds, etc.). For many years now the Trustees of the above Foundation have been able to carry out these objects, and the Foundation has always had an exempt status, passing all IRS examinations without difficulty.

I am enclosing a copy of a letter from the IRS, dated 8/13/73, refusing our being classified as a "private operating foundation." Also enclosed is our protest to same, and it might be added that this case is still open and being appealed. Two situations come to the fore here:

1. "Substantial Involvement" in the garantee or grantee organization becomes a stumbling block. We do follow the some 30 young people who have education grants, requiring a review of their marks and endeavors each semester, before allowing them assistance in continuing in the program. However, when we give some $15,000.00 to a hospital for expansion, for instance, we are not and cannot run a hospital. This then is classified as an "un-qualified contribution" to our detriment.

2. It is suggested that we might qualify as a Sec. 509 (a) (3) (A), a "supporting organization", giving our charitable funds to another Private Operating Foundation (such as the N. H. Charitable Foundation) who would do exactly as we have done these many years. This then inserts, in our opinion, an unnecessary third party, lessing the final amount contributed to the end grantee, as there would be expenses, etc. deducted therefrom.

Because of the above, our being classified as a "private foundation", possible taxes could "wipe out" this small foundation in one year. We are not opposed to the 4% tax on income, per se. The problem comes in the penalty section of the law dealing with the "minimum investment" feature. Briefly, if the 6% imaginary return on current market basis as put forth under this act, the then 6% imaginary income taxed at 4% would become a confiscatory amount, and one which this foundation would be unable to meet. It does not seem logical that Congress intended that 150 people would be denied the opportunity to work, a vital industry would be put out of business, 30-some young people would not have the opportunity to further their education, and so on.

The response from the IRS, so far, to this situation is that where they have not raised the issue yet, we need not worry. They have determined, and we have agreed, that we are subject to the 4% income tax. Having dealt in tax matters for some 20 years before coming to Tilton, my experience to questions as noted in this paragraph are far from satisfactory. This question will inevitably be raised by some agent in his normal activity. In such a situation, if a one year's tax deficit is assessed, the chaos of a three year assessment (normal reviews in audits—two or three years at a time) would be overwhelming.

Your taking time to read this far is appreciated. I have tried to be brief, but haven't covered some of the other features which are troublesome—this one being the most critical. If we can provide any further information or assistance, we would be most pleased to so do.

Very truly yours,

THE BELLE PEABODY BROWN FOUNDATION,
RALPH E. GIBBS, *Chairman.*

BOSTON DISTRICT DIRECTOR,
INTERNAL REVENUE SERVICE,
August 13, 1973.

BELLE PEABODY BROWN FOUNDATION,
Tilton, New Hampshire.

GENTLEMEN: We have considered your form 4653 (Notification Concerning Foundation Status) dated 2/12/73, on which you claimed to be a private operating foundation as defined by section 4942(j)(3) of the Internal Revenue Code.

The foundation was established May 10, 1949 under the laws of the State of New Hampshire. Exempt status was granted by the Internal Revenue Service on March 5, 1951 under section 501(c)(3) of the Code.

The purpose of the foundation is made up of two parts, the first is to contribute to worthy charitable and educational organizations in the State of New Hampshire, secondly to help needy and deserving persons to further their education in schools, colleges and graduate schools.

The definition of an operating foundation is that the foundation makes qualifying distributions directly for the active conduct of activities constituting its charitable purpose.

Internal Revenue Regulations section 53.4942(b)-2(b)(3) specifically excludes grants to other organizations and scholarships from the definition of qualifying distributions.

On the basis of the above information it our conclusion that your organization does not meet the definition of an operating foundation, and is therefore classified as a private non-operating foundation under section 509 of the Internal Revenue Code.

Your qualification for exemption from Federal income tax under section 501(c)(3) is not affected by this determination.

If you do not agree with this proposed action, you may request a District Conference to discuss this further.

If you do not desire a District Conference, you may request referral of this matter directly to the National Office.

Your request for either a District Conference or referral to the National Office must be accompanied by a written protest setting forth the facts, law and arguments in support of your position and should be prepared in accordance with the enclosed instruction, Publication No. 716.

If you request referral to the National Office, your protest should also include a statement on whether or not you desire a conference at the National Office in the event their decision is adverse to your position.

If we do not hear from you within 30 days this determination will become final.

Very truly yours,

WILLIAM E. WILLIAMS,
District Director.

Enclosure: Publication No. 716.

PROTEST

A. Belle Peabody Brown Foundation, 283 Main Street, Tilton, New Hampshire 03276.

B. Form: Letter dated August 13, 1973 AU:EO:30D, Rm E205.

C. Taxable Year: 1973, et seq.

D. A District Conference is hereby requested.

E. The Taxpayer takes exception to the following denial of private operating foundation as contained in said letter.

Internal Revenue Regulations section 53.4942(b)-2(b)(3) specifically excludes grants to other organizations and scholarships from the definition of qualifying distributions.

On the basis of the above information it is our conclusion that your organization does not meet the definition of an operating foundation, and is therefore classified as a private non-operating foundation under section 509 of the Internal Revenue Code.

F. The Taxpayer submits the following statement of facts in support of its position that it qualifies as a private operating foundation:

1. The Belle Peabody Brown Foundation is a voluntary corporation established May 10, 1949, under the voluntary corporation laws of the State of New Hampshire.

2. The Belle Peabody Brown Foundation received exempt status under Section 501(c)(3) of the Internal Revenue Code by exemption letter dated March 5, 1951.

3. The purposes of the foundation are two-fold:

(a) To contribute to worthy charitable and educational organizations in the State of New Hampshire, and

(b) To help needy and deserving persons to further their education in organizations such as schools, colleges, and graduate schools. (Articles of Agreement, Article III)

4. The Taxpayer has retained yearly an Executive Secretary and Treasurer and that pursuant to his powers, duties, and responsibilities he is required:

(a) As Executive Secretary "to screen the new applicants in line with the funds available and . . . make payments of grants upon approval by other Trustees. (Trustees' Meeting, June 6, 1967)

(b) As Treasurer, to handle the financial transactions pursuant to legitimate purposes of the corporation. (Articles of Agreement, Article VIII)

5. That the Taxpayer has demonstrated a continuing involvement in the programs receiving grants which further the foundation's work, for example:

(a) Evaluation of Tilton-Northfield High School Band Pilot Program. (Winnisquam Regional High School) (Chairman's Report, 1971)

(b) Program of assistance to local medical institutions on the local level. (Chairman's Report, 1971)

(c) Contributions to Winnisquam Regional High School's music department in order to purchase musical instruments for indigent students. Evaluation of the program and subsequent review by Board of Trustees. (Chairman's Report, 1972)

G. The Taxpayer relies on Sections 4942(j)(3); 509(a)(3)(A); 170(b)(1)(A)(i)—(vi) and revenue regulations 53.4942(b)—1(b)(2), 53.4942(b)—1(b)(2)(ii)(A,B).

1. Paragraph 4942(j)(3) of the Internal Revenue Code provides special private operating foundation status to any organization which makes qualifying distributions directly for the conduct of activities constituting the purpose or function for which it is organized.

2. The Taxpayer has actively throughout its existence involved itself with the conduct of special activities or educational activities through scholarship grants, by active participation in, evaluation of and monitoring of programs it benefits.

3. Internal Revenue Regulation Section 53.4942(b)—1(b)(2) does not apply to the Belle Peabody Foundation for the following reasons:

(a) The prohibition applies only in the event that the Taxpayer doesn't retain significant involvement in the active programs in support of which grant scholarships or tuition payments are made or awarded.

(b) The foundation does in fact maintain significant involvement as defined by 53.4942(b)—1(b)(2)(ii)(A,B) and will provide evidence of such significant involvement at the District Conference:

(i) The Taxpayer has retained a salaried employee whose responsibility is to supervise and direct activities of the Taxpayer in achieving its exempt purposes.

(ii) The Foundation has developed expertise in direction of funds, monitoring of programs, and other activities in the community necessary to achieve its charitable goals.

4. In the event that the Taxpayer is denied operating foundation status under Section 4942(j)(3) in the alternative the Taxpayer asserts that it should be classified as a public charity under 509(a)(3)(A).

5. The Taxpayer alleges that the intent of the law was to exempt organizations like the Taxpayer from being classified as private foundations in as much as the grants made by the Taxpayer are made to other organizations such as schools, hospitals, etc.

6. 509(a)(3)(A) provides that an organization which is "organized and at all times thereafter is operated exclusively for the benefit of and to perform the function of or to carry out the purposes of one or more specified organizations defined in Paragraphs 1 and 2 which are to be excluded from the definition of private foundations."

7. The Taxpayer in fact benefits, by way of scholarship grants, only those individuals who participate in educational institutions which would qualify for exampt status under the definitions as set forth in Section 170(b)(1)(A)(i)—(vi);

In that pursuant to its articles of agreement, grants made to individuals are made only to educational institutions for educational purposes exclusively. (Articles of Agreement, Article III).

H. This Protest was prepared and filed by Robert H. Hurd of Nighswander, Lord, Martin & Killkelly, One Mill Plaza, Laconia, N.H., in the absence of Arthur H. Nighswander, Attorney for the Belle Peabody Brown Foundation upon information furnished by the Taxpayer.

NIGHSWANDER, LORD, MARTIN & KILLKELLEY,

By _____

ROBERT H. HURD.

Under the penalties of perjury, I declare that the statements of facts presented in this Protest and in any accompanying schedules and statements have been examined by me and to the best of my knowledge and belief and on behalf of the corporation, are true, correct, and complete.

BELLE PEABODY BROWN FOUNDATION,

MILLER & CHEVALIER,
Washington, D.C., June 4, 1974.

Hon. VANCE HARTKE,
Chairman, Subcommittee on Private Foundations, Committee on Finance, U.S. Senate, Washington, D.C.

DEAR SENATOR HARTKE: The Havens Relief Fund Society is a charity organized in New York in 1878 to make grants to indigent persons suffering severe financial need. For nearly 100 years it has performed the most traditional of the charitable functions—direct relief of the poor. It is exempt from tax under § 501(c)(3) and is a private foundation

As a private foundation, § 6056(b)(7) requires the Society, among other things, to list in its "annual report" under that section all grants, showing the amount, name and address of recipient, and purpose of each grant. This report is publicly available. The requirement that names and addresses of recipients of grants be listed has severely inhibited the Society's traditional work. The Society's charitable grants often involve personal needs of the recipient, such as medical treatment. Disclosure in these circumstances may involve a serious invasion of personal privacy of the individual. The purpose of § 6056(b)(7) would not seem to extend to disclosure of this information. See H.R. Rep. 91-782, 91st Cong., 1st Sess., (1969) at pp. 280-287 and compare Sen. Rep. No. 91-552, 91st Cong., 1st Sess. (1969) at pp. 47-48, 49-51, 52-53.

We urge that § 6065(b)(7) be amended to exclude grants to indigent or needy persons not exceeding $1000 to any person in any year by a foundation organized and operated exclusively for the purpose of making such grants. Draft statutory language and a more complete explanation are enclosed.

Please include these materials in the record of your current hearings on private foundations and give me the opportunity to discuss this matter with appropriate persons on the Committee staff.

Sincerely,

JOHN S. NOLAND.

Enclosure.

MEMORANDUM IN SUPPORT OF PROPOSED LEGISLATION AMENDING SECTION 6056 OF THE INTERNAL REVENUE CODE OF 1954

Under present law private foundations having at least $5,000 of assets must file an annual report with the Internal Revenue Service. The annual report is available for inspection by the public. In addition copies of the annual report must be furnished to the Attorney General of any state having jurisdiction over the exempt organizations and must be made available for inspection at the principal office of the foundation by any citizen upon request made within 180 days after the publication of notice of its availability in a newspaper having a general circulation in the county in which the principal office of the foundation is located.

The information which must be set forth in the annual report includes financial statements, a list of the names and addresses of the foundation manager, and a list of persons who are substantial contributors. It also includes an itemized list of all grants and contributions made or approved during the year, showing the amount of each grant or contribution, the name and address of the recipient, the purpose thereof, and other details.

Some charitable organizations which make grants to indigent or needy persons on an individual basis have encountered difficulties with respect to the last requirement. Often grants of this type involve personal needs of the recipients, such as expenses connected with medical treatment, where disclosure might constitute an invasion of privacy, or where the necessity of disclosure might deter acceptance of the grant by a potential recipient.

Disclosure and publicity of grants of a personal nature does not appear to have been considered or contemplated when the requirement for annual reports was added to the Internal Revenue Code by the Tax Reform Act of 1969. The proposed amendment would eliminate the necessity for reporting and public disclosure in limited cases involving charitable grants to needy or indigent persons; it would permit private foundations to treat such information as confidential.

A precedent for maintaining anonimity exists in the disclosure requirements regarding substantial contributors. A Senate amendment to the Tax Reform Bill of 1969 elminated the necessity of disclosing the names and addresses of substantial contributors of exempt organizations other than private foundations, although such information must still be disclosed on the information return filed with the Internal Revenue Service.

The proposed amendment does not affect the requirement for disclosure and publicity of the names and addresses of recipients of grants for travel, study or other similar purposes.

The proposed amendment would be effective with respect to annual reports filed for taxable years beginning after December 31, 1973, except that for the purpose of public inspection of annual reports at the office of the Secretary or at the principal office of the private foundation under Sections 6104(b) and (d) it would apply with respect to annual reports filed for taxable years beginning after December 31, 1969.

PROPOSED AMENDMENTS TO SECTION 6056 OF THE INTERNAL REVENUE CODE OF 1954

SEC. 1. (a) Section 6056(b)(7) (relating to information which must be set forth in the annual report of a private foundation) is amended by striking out "contribution." at the end thereof and inserting in lieu thereof the following:

"contribution, except that in the case of a private foundation organized and operated exclusively for the purpose of making charitable gifts or grants to indigent or needy persons, the name and address of any recipient of one or more garnts which do not exceed $1,000 during the year may be treated as confidential and need not be listed."

(b) *Effective Date.*—The Amendment made by subsection (a) shall apply with respect to annual reports filed for taxable years beginning after December 31, 1973, except that for the purpose of public inspection of annual reports under Sections 6104(b) and (d) the amendment made by subsection (a) shall apply with respect to taxable years beginning after December 31, 1969.

STATEMENT OF JOAN IRVINE SMITH, RE THE JAMES IRVINE FOUNDATION

A Special Shareholders Meeting of the Irvine Company was called by Mrs. Joan Irvine Smith, who is the largest individual stockholder in this corporation, with her holding of twenty two percent of the outstanding stock.

The principal purpose of the meeting was to consider and adopt a Resolution which would provide for the payment of a substantial Special Dividend to the stockholders for the fiscal year 1973–1974. Preceding the Special Shareholders Meeting, which was called for 10 O'Clock A.M., on May 13, 1974, there was a meeting of the Planning and Policy Committee of the Irvine Company, consisting of the Directors of this corporation, at 8:30 A.M. on the same date. The purpose for the meeting of the Planning and Policy Committee was also to consider the payment of the Special Dividend. At this meeting L. E. Eberling, Senior Vice President and Treasurer of the Irvine Company, submitted a statement which had been prepared by him and entitled "Dividend Recommendations". The introductory statement by Mr. Eberling, in said statement, is as follows:

"We (management of the Irvine Company, which is selected by the James Irvine Foundation, which also selects and appoints the majority Directors of the Irvine Company) have concluded that the current policy of paying 45%–55% of the net income as dividends, and retaining the balance of earnings for reinvestment would best optimize the interests of the shareholders (the charitable beneficiaries of the Irvine Foundation owned 54% of the Irvine stock held by said Foundation, as Trustee) and the corporation. Therefore, we recommend a continuation of the current dividend policies previously adopted by the Board of Directors." At this meeting of the Planning and Policy Committee.

Mrs. Smith reviewed the Resolution which she would prepose at the Special Shareholders Meeting, which would immediately follow said meeting of the Planning and Policy Committee. Mrs. Smith's Resolution, if adopted, would provide for the payment of a substantial increase in the dividend policy of

the Irvine Company, and particularly an increased Special Dividend to be declared at the meeting of the Board of Directors of the Irvine Company on June 11, 1974.

Mr. Raymond L. Watson, the President of the Irvine Company, since his selection by the Irvine Foundation following the death of William R. Mason in July, 1973, and Mr. Eberling vigorously opposed Mrs. Smith's indicated Resolution, and no action was taken by the Committee. The Eberling Report contained the following paragraph:

"Recently our credit line banks have expressed concern that the Irvine Foundation would bring pressure on the Company to increase its dividend pay-out ratio substantially (possibly 100%) *in order that the Foundation may meet its obligations under the Tax Reform Act of 1969. We have assured the banks that the Foundation would resolve their problem without compromising the financial responsibilities and position of the Company.*"

There is no validity whatever to the foregoing quoted statement, as coming from the banks, who make both short term and long term loans to the Irvine Company, and for which they receive substantial interest payments and this reference to said banks was undoubtedly inspired by the Irvine Foundation. So far as the banks are concerned, who make loans to the Irvine Company, they are quite satisfied with their security, based upon the ownership, by the Irvine Company, of eighty thousand acres of clear and unencumbered land in Orange County, California, which has an approximate value of One Billion Dollars. The only way that the Irvine Foundation can resolve the minimum investment return requirements of Section 4942 of the Tax Reform Act of 1969 (which it has fraudulently evaded during the years 1972, 1973 and 1974) is either to sell its Irvine stock and invest the proceeds from such sale in other securities that yield sufficient interest or dividend income to enable the Foundation to comply with Section 4942, or to substantially increase the dividends of the Irvine Company, which said Foundation has the capability to do.

Under the present dividend policy of the Irvine Company, which is set by the Irvine Foundation majority Directors of the Irvine Company, the charitable beneficiaries of the Foundation are only receiving a little more than a two percent dividend return on the Foundation's appraisal for its Irvine stock at approximately One Hundred Million Dollars. It therefore appears conclusively that the Directors of the James Irvine Foundation do not intend to comply with the pay-out requirements of Section 4942, either through the sale of its Irvine Stock, or by requiring the Board of Directors of the Irvine Company, under the control of the Irvine Foundation, to increase its dividend policy.

The above mentioned "Dividend Recommendations" statement of Mr. Eberling was prepared and intended to be used by the James Irvine Foundation Directors and the Foundation management of the Irvine Company to defeat Mrs. Smith's Resolution. The Special Shareholders Meeting was attended by John V. Newman, who is a Director and Vice President of the Irvine Foundation, and also is appointed by the Foundation as Chairman of the Board of Directors of the Irvine Company, and who held a proxy from the Irvine Foundation to vote its holdings of 4,590,000 shares of Irvine stock with the exception of one share thereof, which was voted by proxy holder, Howard J. Privett, who is the attorney for the Irvine Foundation, at said Special Shareholders Meeting.

At this Meeting Mrs. Smith introduced her Resolution to increase the Special Dividend to be declared at the meeting of the Board of Directors of the Irvine Company on June 11, 1974, from six cents per share, which had been recommended by both Mr. Watson and Mr. Eberling, to fifty-one cents per share. A copy of this Resolution is attached hereto at this point:

Whereas, the corporation has established a policy that special dividends, if considered warranted, shall be declared at the June meeting of the Board of Directors; and

Whereas, the net income for the fiscal year, 1973–1974, is the sum of approx. $9,800,000.00, and the retained earnings of The Irvine Company for the fiscal year ending April 30, 1974, is the sum of approx. $49,171,000., and

Whereas, the majority stockholder of The Irvine Company, to wit, The James Irvine Foundation, is the Trustee for the charitable beneficiaries of the Trust

Fund that was established by James Irvine in that certain Indenture of Trust dated February 24, 1937, and in the Articles of Incorporation of The James Irvine Foundation, a charitable corporation; and

Whereas, the Tax Reform Act of 1969 provides therein and in the regulations issued thereunder, that after December 30, 1969, the date the Act was signed, that The James Irvine Foundation, as a private foundation, is restricted from making investments either directly or by The Irvine Company, which is controlled by The James Irvine Foundation, as Trustee, in nonproductive or low yielding assets, and to so manage the business affairs of The Irvine Company as to produce sufficient net income that will currently increase the flow of dividend funds to the charitable beneficiaries of The James Irvine Foundation, to wit, the People of the State of California; and

Whereas, The James Irvine Foundation is required under the Tax Reform Act of 1969, and the regulations issued thereunder, to distribute to its charitable beneficiaries during the taxable year, 1973–1974, that sum of money which amounts to 4⅝% of the market value of its Irvine stock; and

Whereas, the latest sale of any stock in The Irvine Company occurred in November, 1968, through the sale by the Macco Corporation of 135,000 shares of Irvine stock to The Irvine Company at the price of $25.00 per share and which sale established a fair market value as of that time for the 8,415,000 shares of Irvine stock outstanding at $210,375,000.00, and which said market value, for the purpose of this resolution and until the current fair market value of Irvine stock is established by the Internal Revenue Service through an appraisal which is now being made of the underlying assets of The Irvine Company and which it is estimated will be concluded on or about August 1, 1974; and

Whereas, 4⅝% of $210,375,000.00 is $9,193,387.00, which sum of money represents the total dividend which should be paid by The Irvine Company to its stockholders for the fiscal year, 1973–1974, in order to enable The James Irvine Foundation to comply with the minimum investment return and distribution to its charitable beneficiaries as required by Section 4942 of the Tax Reform Act of 1969, for the fiscal year, 1973–1974; and

Whereas, the 1974–1975 operating and capital budget of The Irvine Company, which was aproved, in the absence of Director Joan Irvine Smith, by the Board of Directors of The Irvine Company on April 9, 1974, discloses that the Board of Directors of The Irvine Company intends to only pay a total dividend to the stockholders of The Irvine Company of 58¢ per share, aggregating the sum of $4,880,700.00 for the fiscal year, 1973–1974, which is computed on the basis of dividends paid of 12¢ per share in the September and December quarters for the year, 1973, and 15¢ per share for the March and June quarters in the year, 1974, and a special dividend of 4¢ per share to be declared at the June 11, 1974 meeting of the Board of Directors; and

Whereas, the payment of said sum of $4,880,700.00 if paid and then deducted from the sum of $9,193,387.00 leaves the sum of $4,312,687.00 to be declared and paid to the stockholders of The Irvine Company at the regular meeting of the Board of Directors of The Irvine Company on June 11, 1974, as a special dvidend for the fiscal year, 1973–1974;

Now, Therefore, be it Resolved that it is the consensus of the shareholders present at the Special Shareholders' Meeting on May 13, 1974, that the directors of The Irvine Company at the meeting of the Board of Directors on June 11, 1974, shall declare a special dividend for the fiscal year, 1973–1974, of 15¢ per share on the 8,415,000 shares of stock outstanding, aggregating $4,312,687.00, payable on June 12, 1974, to the stockholders of record as of the close of business on June 11, 1974, in addition to the sum of $4,880,700.00, or a total regular and special dividend for the fiscal year, 1973–1974, of $9,193,387.00.

In reply to Mrs. Smith's Resolution above mention, Mr. Watson, as President of the Irvine Company, summed up the opposition of the Irvine Foundation controlled management of the Irvine Company, by approving Mr. Eberling's "Dividend Recommendations". When the time came to vote on Mrs. Smith's Resolution, proxyholder Privett, as the attorney for the Irvine Foundation, stood up and stated that the James Irvine Foundation was opposed to the adoption of Mrs. Smith's Resolution and both Mr. Privett and Mr. Newman

voted against its adoption, and so did all of the other minority stockholders of the Irvine Company, with the exception of Mrs. Smith and her mother, Mrs. Clarke, who voted "Yes", and Linda Gaede and her husband, M. Keith Gaede, who abstained.

As evidence of the fraud which has been practiced by the Irvine Foundation Directors in their evasion of the pay-out requirements of Section 4942 for the years 1972-1074 inclusive, it is appropriate here to disclose why the minority stockholders of the Irvine Company, who voted "No" on Mrs. Smith's Resolution, and their reasons for doing so. These minority stockholders are: Jay Eye Corporation, 450,000 votes. This corporation holds the stock of Mrs. Katherine L. Wheeler, who is a Director of the James Irvine Foundation, and through her connection with the Foundation has had her husband, Charles S. Wheeler elected as a Director of the Irvine Company, over a period of many years and also to be elected as Secretary of the Irvine Company, at a salary of $25,000.00 per year, and President of the Flying D Ranch Corporation, which is a wholly owned subsidiary of the Irvine Company, and owns a 100,000 acre cattle ranch in the State of Montana.

The other minority stockholders who voted "No" are, to wit: William T. White III, Melinda Royer White, Custodian, wife of William T. White III, Tico and Co., Gloria W. Bryant, sister of William T. White, III, White Co. Enterprises, Melinda A. White, Thornton White, Jr., and William C. Friel, Trustees, Remra & Co., which is a nominee of the Security Pacific National Bank, and Truco, also a nominee for this bank are under the direct control of William T. White, III, who is a Co-Executor and Co-Trustee with said bank for trust and probate estates that own shares of the Irvine stock, which are held by both of the above named nominees. William T. White III, and his relatives, associates and controlled banks have been well taken care of by the James Irvine Foundation, for their support in everything that the Foundation directs Mr. White to vote for or against in connection with the management of the Irvine Company.

On April 9, 1974, Charles S. Wheeler resigned as a Director of the Irvine Company, but continued as Secretary, and by agreement with the Directors of the Irvine Foundation, Mr. White was elected to the Board of Directors of said corporation. Mr. White and his mother's estate, Gloria Wood Irvine, deceased, and several of Mr. White's relatives and associates were recipients, in January, 1973, of the sum of $1,025,000.00 from the Irvine Company, under the direction of the Irvine controlled majority Directors of the Irvine Company, and which said large sum of money purportedly constituted the purchase price by the Irvine Company of certain worthless assets of the Orange County International Raceway Corporation, in which William T. White III, and his relatives and asociates were stockholders, consisting of a grandstand, and race track feilities which had no value whatever to the Irvine Company. The payment of this large sum of money to William T. White, and his relatives, and his mother's estate, and his associates, as stockholders in the Raceway Corporation, and also to the creditors of this Raceway Corporation bailed these parties out of their losses which they had incurred in the operation of their drag race venture. Mr. White, also with the benediction of the James Irvine Foundation, has entered into certain leases and/or agreements with the Irvine Industrial Complex, which is a wholly owned subsidiary of the Irvine Company, and of which Mr. White is also a Director, and these transactions have been financially profitable to Mr. White. Mr. White is also a disqualified person, under Section 4946 of the Tax Reform Act of 1969.

The Assistance League of Santa Ana, which is the remaining minority stockholder of the Irvine Company, with its holding of 58,500 shares of Irvine stock, received this stock as a gift from Mrs. James Irvine, deceased, who also is the grandmother of William T. White III, and this organization also votes at all stockholders meetings of the Irvine Company, in accordance with the instructions received from Mr. White. This organization also receives donations from the James Irvine Foundation.

The dividend policy of the Irvine Company, as dictated by the James Irvine Foundation, for the next five years, and which is outlined by Mr. Eberling, in his "Dividend Recommendations" hereinabove mentioned, is programmed by the Irvine Foundation for the purpose of reducing the appraised value of the

underlying assets of the Irvine Company that the Internal Revenue Service is now conducting under contract with the appraisal firm of Marshall & Stevens. The appraisal of approximately One Hundred Million Dollars, which the Irvine Foundation places on its 4,590,000 shares of Irvine stock is based solely on the earning and dividend record of the Irvine Company, under the control of the Irvine Foundation, as a going concern, and the James Irvine Foundation is therefore projecting the low earning and dividend program of the Irvine Company for the next five years so that the appraisal of the Internal Revenue Service will hopefully be no more than the Foundation appraisal of approximately One Hundred Million Dollars. It therefore should be disclosed that the evaluation of the underlying assets of the Irvine Company, as of June 5, 1973, and as appraised by the Assessor of Orange County, California, where the Irvine Ranch is located is $490,000,000.00 for the year 1972–1973. The appraisal of the Irvine Foundation for the assets of the Irvine Company was only $189,000,000.00.

The 1974–1975 Operating and Capital Budget of the Irvine Company discloses that the real estate taxes on the Orange County property of the Irvine Company are currently $12,157,800.00. This current real estate tax figure discloses that on the two percent basis referred to and approved by the Washington, D.C. Attorneys for the James Irvine Foundation of $490,000,000.00 gives a fair market appraised value to the Orange County land of the Irvine Company of approximately $600,000,000.00, and based on this evaluation, the James Irvine Foundation should be required to distribute to its charitable beneficiaries 4⅛% of 5⅔% of this amount for the year 1972, and 4⅜% of 5⅔% of said amount for the years 1973 and 1974.

The James Irvine Foundation is deliberately and fraudulently violating Section 4942 of the Tax Reform Act by controlling, through its management, and the majority Directors of the Irvine Company, the amount of net earnings and dividends which are received and paid by the Irvine Company. Both the net earnings and the dividends of the Irvine Company should be at least four times the amount which are currently received and paid by this corporation under the control of the Irvine Foundation which has the capability of requiring the Board of Directors of the Irvine Company to increase its net earnings and dividends by directing the Foundation controlled Directors of the Irvine Company to discontinue its investment properties program in constructing office buildings, multi-family buildings, and industrial buildings which will not produce any net income for many years in the future. Furthermore, the cost of these investment properties which now amounts to approximately Inc Hundred Million Dollars is covered by mortgages for the full cost thereof, and the interest expense on said mortgaged investment properties, as disclosed by the 1974–1975 Irvine Company Budget is currently $8,600,000.00, and will be approximately $10,000,000.00 by the end of 1974.

The Irvine Company, under the control of the James Irvine Foundation, is a bureaucratic and monopolistic corporation that refuses to sell any of its land in Orange County, to investors for development by said investors, except in the Irvine Industrial Complex area, and to a select few friends in the Newport Commercial Center area, and said Foundation is determined that the balance of the Irvine Ranch acreage will solely be developed by the Irvine Company over the period of the next fifty to one hundred years.

It is a blatant fraud for the Directors of the Irvine Foundation not to distribute to its charitable beneficiaries, the amount of money which said are entitled to receive under Section 4942 of the Tax Reform Act when this could be easily done through the sale annually of a few hundred acres of land out of the eighty thousand acres owned by the Irvine Company to outside investors; and this should have been done in the years 1972–1973 and 1974 and the net proceeds received therefrom should have been paid as dividends and the share of the Irvine Foundation in said dividends should have been distributed to the charitable beneficiaries of the Irvine Foundation.

Under the Eberling—Irvine Foundation five year earnings and dividend formula for the fiscal years 1974–1979, both earnings and dividends will be fraudulently restricted by the Foundation Directors with their control over the management and Directors of the Irvine Company so that the beneficiaries of the Irvine Trust Fund will be defrauded out of millions of dollars. The an-

nounced program and formula which is contained in Eberling's "Recommended Dividends" Memorandum of May 13, 1974, is as follows:

	Net earnings per share	Dividends per share
1974–75	$1.28	0.64
Total	10,816,300	$5,722,200
1975–76	1.54	.77
Total	12,984,500	6,142,900
1976–77	1.90	.95
Total	16,060,000	7,657,700
1977–78	2.08	1.04
Total	17,502,000	8,583,300
1978–79	2.30	1.15
Total	19,424,000	9,424,900

The above dividend payments for the fiscal years 1974–1979 are based on the Eberling—Irvine Foundation fictitious value of Irvine Company stock at $23.50 per share, which gives a total value to the 8,415,000 shares of Irvine stock outstanding of $197,420,000.00. On the fictitious evaluation of the Irvine stock held by the Irvine Foundation as its principal asset, the dividend yield is as follows: 1974–1975, 2.7%; 1975–1976, 3.3%; 1976–1977, 4%; 1977–1978, 4.4%; 1978–1979, 4.9%.

For the year 1972–1973 the James Irvine Foundation was mandated, by Section 4942 of the Tax Reform Act, to distribute to its beneficiaries at least 4⅞ percent of its Irvine stock, appraised value, to wit: approximately One Hundred Million Dollars, and not only 2.52%, as provided in the Eberling—Irvine Foundation five year formula. By 1976 the Irvine Foundation, under Section 4942, is required to distribute to its beneficiaries not less than 6% of the fair market value of its stock which long before this year will have been officially appraised by the Internal Revenue Service, at a much higher figure than the One Hundred Million Dollars appraisal of the Irvine Company. On the basis of the appraisal of the Assessor of Orange County in 1973 of Six Hundred Million Dollars, as hereinabove mentioned, the current amount of money which the beneficiaries of the Irvine Foundation are entitled to receive is approximately Fourteen Million Dollars.

Not only does the Eberling-Irvine Foundation Five Year Dividend Program perpetrate a fraud on the beneficiaries of the Irvine Foundation, but the management performance, by the Irvine Foundation of the Irvine Company since N. Loyall McLaren, President of the Foundation and Chairman of the Board of Directors of the Irvine Company personally directed the management operations of the Irvine Company, discloses not only fraud connected with such management, but a scandalous and incompetent breach of the fiduciary duty of the Directors of the Irvine Foundation to the beneficiaries of the Irvine Foundation Trust Fund.

For the fiscal year 1966–1967, when Mr. McLaren selected William R. Mason as President of the Irvine Company, the total net income was $8,718,000.00, and approximately Six and One Half Million Dollars of this amount came from the liquidation of capital assets and principally from damages received by the Irvine Company by the condemnation of its land for the Santa Anan Freeway. The total dividend paid from this net income was only the sum of $1,539,000.00, which amounted to 18¢ per share, and only 17.6% of the net income. The dividens which went into the Irvine Trust Found for distribution to the Foundation beneficiaries, amounted to slightly over the sum of $800,000.00, which represented 54% of the total dividend of $1,539,000.00.

There is attached hereto a Consolidated Statement of Net Income and dividends paid during the fiscal years 1966–1967 to 1973–1974.

The Eberling-Irvine Foundation earnings and dividend formula as already mentioned, grossly restricts the net earnings and dividend payments of the Irvine Company by the Investment Properties Program, which not only diverts 50% of the net income of the Irvine Company for this program, but also diverts net income which should go into dividends because of the interest which is paid on the money borrowed to cover the 100% cost of the investment

properties operation, consisting of the construction of multi-family buildings, office buildings, industrial buildings and recreational facilities buildings, such as marinas. The cost of this investment properties program for the year 1974–1975 is $42,972,000.00; 1975–1976, $36,700,000.00; 1976–1977, $47,505,000.00; 1977–1978, $69,781,000.00; 1978–1979, $31,220,000.00, total $228,178,000.00.

Interest at 10%, which is less than the current rate of 12%, at least approximately $30,000,000.00, which added to the present interest that is being paid on the investment properties already constructed of approximately $10,000,000.00, amounts to a total interest payment during the next five years of approximately $40,000,000.00, and also during this period real estate taxes on the undeveloped land of the Irvine Company in Orange County, as well as the investment properties improvements, will undoubtedly be up to $20,000,000.00 per annum.

The Consolidated Statement of Net Income and dividends paid during the fiscal years 1966–1967 to 1973–1974 and the forecasted schedule for the construction of investment properties for the years ending April 30, 1975–1979 are attached.

THE IRVINE COMPANY, CONSOLIDATED STATEMENT OF NET INCOME AND DIVIDENDS PAID FOR THE YEARS ENDING APR. 30, 1967-73

[In thousands of dollars]

	Net income		Dividends			
	Total	Per share	Total	Per share	Percent of net income	Net income reinvested
1966-67	$8,718	$1.02	$1,539	$0.18	17.6	$1,179
1967-68	2,989	.35	1,902	.22	63.8	1,087
1968-69	5,496	.65	2,356	.28	42.8	3,140
1969-70	6,486	.77	3,198	.38	49.3	3,288
1970-71	6,297	.75	3,366	.40	53.4	2,931
1971-72	7,637	.91	3,871	.46	50.6	3,766
1972-73	9,102	1.08	4,544	.54	49.9	4,558
1973-74[1]	9,800	1.16	4,965	.59	51	4,835

[1] Forecasted May 9, 1974.

My attorney, Lyndol L. Young, in talking with Mr. Raymond L. Watson, the Irvine Foundation controlled Director and President of the Irvine Company recently, Mr. Young stated to Mr. Watson that it was the responsibility not only of himself, but also Newman, Lund, Allen, White and Wheeler, as Foundation appointed Directors of the Irvine Company, to comply with the 1969 Tax Reform Act in connection with the payment of dividends by the Irvine Company to the charitable income beneficiaries of the James Irvine Foundation, as well as the other stockholders. Mr. Watson stated that he did not recognize any such responsibility, either as a Foundation Director or President of the Irvine Company, and that he did not agree with Mr. Young that any of the other Irvine Foundation Directors, to wit: Newman, Lund, Allen and Wheeler, had any such responsibility, and that his and their only duty was to manage the Irvine Company in the same manner that it would be operated as a private enterprise corporation, regardless of the fact that the charitable beneficiaries of the Irvine Foundation controlled the Irvine Company through their 54% stock holding in the Irvine Company. Mr. Watson also took the position that it was not the responsibility and the duty of himself, and the other Irvine Foundation Directors and officers of the Irvine Company to see to it that maximum dividends were paid from the net income operations of the Irvine Company. Mr. Watson further stated that at least 50% of the net income of the Irvine Company, including the liquidation of capital assets, should be diverted from dividend distribution by using the same for investments in the construction of commercial multi-family and industry properties, even though such investments will not yield any net income for many years in the future.

THE IRVINE COMPANY AND SUBSIDIARIES FORECASTED SCHEDULE OF CASH PROVIDED FOR THE YEARS ENDING APRIL 30, 1975-79

[At March 22, 1974]

Long-term borrowing	Estimated funding date	1974-75	1975-76	1976-77	1977-78	1978-79
The Irvine Co.:						
Office building No. 4	Aug. 30, 1974	[1] $12,500,000				
Promontory Point, phase I	do	[2] 7,500,000				
Block 100 office buildings	Dec. 31, 1974	1,100,000				
Campus Valley Center	do	2,000,000				
Parkwood Apartments	do	4,350,000				
Promontory Point, phase II	Feb. 28, 1975	[2] 9,500,000				
Deerfield Apartments	May 1, 1975		$3,000,000			
Parkview Center	June 30, 1975		1,750,000			
Rancho San Joaquin Apartments, IA	Aug. 1, 1975		4,550,000			
Turtle Rock Apartments, I	do		5,600,000			
University Golf Club	do		1,400,000			
Main and Jamboree Center	Nov. 1, 1975		1,860,000			
Block 400 office buildings	do		3,375,000			
Big Canyon Apartments, 10A	Feb. 1, 1976		3,650,000			
Fashion Island expansion	May 1, 1976			$1,300,000		
Culver-Moulton Center	do			1,000,000		
Ford and MacArthur Center	do			2,250,000		
Jamboree and Walnut Center	do			579,000		
Block 100 office buildings	do			2,650,000		
Skypark Office buildings	do			3,100,000		
Woodbridge Apartment, Culver South	do			4,200,000		
Woodbridge Apartment, Culver North	do			3,300,000		
Newporter Apartments	do			2,400,000		
Woodbridge Apartments No. Lake A	Aug. 1, 1976			3,000,000		
Woodbridge Center	Nov. 1, 9176			2,780,000		
Turtle Rock Bowl	do			2,258,000		
Industrial Complex East	do			638,000		
Parking structure "C"	do			7,800,000		
Big Canyon Apartments, 10B Canyon	Feb. 1, 1977			4,500,000		
Town Center Apartments, III	do			1,250,000		
Irvine Regional Center	May 1, 1977				$27,321,000	
Newport Village Center	do				3,843,000	

Block "O" office buildings	do				4,961,000	
Rancho San Joaquin Apartments, II	do				4,200,000	
Quail Hill Apartments, I	do				3,650,000	
Bonita Canyon Apartments, I	do				3,400,000	
Town Center VI	do				1,250,000	
Woodridge Apartments, Cor E-A	do				1,050,000	
Rancho San Joaquin Apartments, I-b	do				3,200,000	
New Culver Center	Nov. 1, 1977				2,400,000	
Irvine Center office buildings	do				2,800,000	
Redhill office buildings	Feb. 1, 1978				6,956,000	
University Town Center	May 1, 1978					$5,000,000
New Culver Apartments, A	do					2,580,000
Turtle Rock Apartments, IIIa	do					3,870,000
New Culver Apartments, B	do					2,310,000
Woodbridge Apartments, No. Lake b	do					2,980,000
Woodbridge Apartments, Jeff. So. A	do					3,000,000
Town Center Apartments, IX	do					1,250,000
Woodbridge Apartments, Cor. E-B	do					1,800,000
Bonita Canyon Apartments, II	do					3,430,000
Total		36,950,000	25,185,000	43,005,000	65,031,000	26,220,000
Irvine industrial complex:						
Inventory buildings No. 13, 17, 18, 19	Dec. 31, 9174	3,190,000				
Inventory buildings No. 21, 26, 27, 28	May 1, 1975		2,330,000			
Build to suit buildings	Feb. 1, 1975	680,000				
Future buildings for lease	Nov. 1, 1974		4,250,000	4,500,000	4,750,000	5,000,000
Koll/Irvine, phase II	Dec. 31, 9174	2,152,000				
Kool/Irvine, phase III	May 30, 1975		2,455,000			
Koll/Irvine, phase IV	Dec. 31, 1975		2,480,000			
Total		6,022,000	11,515,000	4,500,000	4,750,000	5,000,000
Consolidated total		42,972,000	36,700,000	47,505,000	69,781,000	31,220,000

Existing commitments at March 22, 1974:
[1] Irvine Tower No. 4, 30 year term at 8.05 percent.
[2] Promontory Point Apartments, 30 year term at 8.375 percent

NOTES

Loans on office buildings, shopping centers and apartments are forecasted as 30 year loans at 8½- percent.
Loans on industrial inventory buildings are forecasted as 25 year loans as 8½- percent.

Attached to this statement is a copy of a letter dated March 22, 1974, and addressed to each of the Directors of the James Irvine Foundation, which supplements this statement with further factual matters that disclose the negligent and fraudulent management of the Irvine Trust Fund, by the Directors of the James Irvine Foundation and their attorneys.

In order to avoid the chance of repetition with the many incidents of non-compliance which are set forth in the above mentioned letter of Mr. Young to the directors of The James Irvine Foundation, there is only one further act of non-compliance which will be mentioned in this statement. There was brought to the attention of the Committee on Ways and Means at the hearing on April 10, 1973, several self-dealing practices connected with the interlocking directorship of The James Irvine Foundation and The Irvine Company, and Mr. Privett, in his testimony, denied the same. However, the following self-dealing practice is a matter of record and cannot be denied by Mr. Privett. At the annual meeting of The Irvine Company in June, 1973, N. Loyall McLaren, at his request, was not re-elected as a member of the Board of Directors of The Irvine Company. At the directors' meeting, following the shareholders' meeting, the directors at this meeting elected John V. Newman, a director of The Irvine Company for several years, to take the place of Mr. McLaren, as Chairman of the Board. Mr. McLaren had been Chairman of the Board of Directors of The Irvine Company since 1960, and also was President and still is President of The James Irvine Foundation as well as a director of the Foundation. As Chairman of the Board of The Irvine Company, Mr. McLaren's sole duty was to preside at the meetings of the Board and for this perfunctory service he received a salary of from $20,000.00 to $25,000.00 per year during his 12 years as Chairman of the Board. Mr. Newman, who is a vice president and a director of the Foundation, receives a salary of $20,000.00 per year for his perfunctory service as Chairman of the Board of Directors of The Irvine Company. Following the annual meeting of the shareholders in June, 1973, the Employees' Compensation Benefits Committee of the Board of Directors of The Irvine Company held a meeting on August 13, 1973, and, although not a member of this Committee, John V. New, Chairman of the Board, Raymond L. Watson, President of The Irvine Company, L. E. Eberling, Vice President of The Irvine Company were present. At this meeting Mr. Newman requested that the Committee adopt a resolution which recommended to the Board of Directors of The Irvine Company that said corporation, commencing June 20, 1973, pay to N. Loyall McLaren, in consideration of the services heretofore rendered to The Irvine Company (for which he received a salary of from $20,000.00 to $25,000.00 per year during his 12 years of service) the sum of $500.00 per month for the balance of his life, and if he is survived by his wife, Mary McLaren, to pay her, commencing on the date of his death, the sum of $250.00 per month for the balance of her life. There is no authorized retirement or pension provision of The Irvine Company to support this self-dealing payment to McLaren and his wife for the balance of their respective lives, and the same constitutes a self-dealing transaction which is sponsored by the directors of the Foundation.

At the meeting of the Board of Directors of The Irvine Company in September, 1973, which was not attended by Mrs. Smith, a resolution was adopted by the foundation-controlled directors which approved this self-dealing pension, and payments of $500.00 per month have been made to Mr. McLaren ever since June 20, 1973.

To demonstrate to the members of the Subcommittee on Foundations the deliberate non-compliance by the Directors of The James Irvine Foundation with the Tax Reform Act of 1969, the following material constitutes Xerox copies from the Annual Reports of The James Irvine Foundation for the years ended March 31, 1971, 1972 and 1973. When these Annual Reports are compared with the reports of other major foundations for the same period, as hereinafter set forth, there can be no question but what the directors of The James Irvine Foundation have shown the same inept and incompetent management of the affairs of the Foundation as they have with the management of The Irvine Company.

In the Report of The James Irvine Foundation as of March 31, 1972, the Committee will note on page 10 thereof the reference to the appraisal by Morgan Stanley & Company of the 4,590,000 shares of the Irvine stock held by the Foundation, as Trustee, to have a fair market value of $22.50 per share, which gives the Foundation's holdings a total appraised value of $103,275,000.00.

PRESIDENT'S MESSAGE, MARCH 31, 1971

The past fiscal year, our first full year of operation under the Tax Reform Act of 1969, was a period of transition in which we examined and made adjustments in our grant program and procedures to ensure full compliance with the letter and spirit of the new legislation. This process necessarily will continue for many months. To date the Treasury regulations necessary for interpretation and implementation of many provisions of the Act have not been adopted. However, on the basis of our past year's experience and the proposed regulations that have been issued by the Treasury, we are pleased to reaffirm our belief that the new legislation will permit the effective continuation and growth of the programs of this Foundation.

While it would be premature for us to attempt to assess the overall effect of the Act on the American tradition of private giving to serve public needs, we are deeply concerned about the immediate impact and long term threat posed by the 4% tax on the income of private foundations. This tax reduced the amount we were able to distribute in the fiscal year just ended by more than $100,000. The total reduction in 1970 grants by all foundations as a result of the tax has been estimated at about 35 million dollars. This appears to us to be an excessive inroad into the private resources available to meet the mounting needs of charitable and educational institutions the activities of which are essential to the maintenance and betterment of the quality of American life. The indicated purpose of the tax is to cover the cost of auditing the activities of foundations. We are informed this has been accomplished for little more than half of the estimated current revenue from the tax. We are hopeful that early Congresisonal consideration will be given to an appropriate reduction in the rate of this tax to avoid a continuing erosion of private foundation funds available to support charitable and educational undertakings.

The past year produced a record number of requests for financial assistance. The projects proposed by the applications had funding requirements in excess of 25 million dollars. As apepars on the following pages of this report, the Foundation allocated all of its income, approximately 2.7 million dollars, to assist in the accomplishment of a substantial number of these projects. As in the past, grants were concentrated in three areas of basic public need—higher education, youth services and medical care. Approximately 94% of the grants in the past year were devoted to specific projects within these broad areas of need. They included programs to combat drug use and abuse among the young; the establishment of new facilities to aid in the prevention of delinquency among young people in low income areas; support for California's private colleges and universities in the form of new facilities and student aid; and new medical and health care facilities.

The pressures of growing public needs, inflation and governmental economies over the past year have placed most charitable and educational organizations under unprecedented strain. We and our colleagues in other foundations must continue to expand our efforts to relieve these pressures. In addition, as the Tax Reform Act is interpreted and implemented by regulations in the coming year, we must continue to assess the adequacy of the new law to preserve the essential role of private philanthropy in American life.

N. LOYALL MCLAREN, *President.*

FINANCIAL STATEMENTS

Statement of Assets and Liabilities as of Mar. 31, 1971

Assets:	
Cash, principally savings accounts and time deposits	$2, 223, 447. 42
Property, real and personal property net of depreciation ($41,238.36)	104, 666. 29
Investments:	
The Irvine Co. common stock at nominal value, see note	2. 00
Corporate stocks, bonds and U.S. Government obligations (at cost, quoted market value $5,733,508.50)	5, 685, 418. 50
Other assets:	
Accrued interest purchased	4, 925. 00
Trust deed notes receivable	2, 079, 339. 77
Total	10, 197, 798. 98
Liabilities:	
Deferred gain on installment sales	328, 220. 66
Corpus	7, 640, 470. 01
Undistributed income:	
Allocated as of Mar. 31, 1971	1, 820, 439. 54
Unallocated	408, 668. 77
Total	10, 197, 798. 98

NOTE.—The Foundation holds 4,950,000 share of The Irvine Co. common stock which it received in trust from the late James Irvine. The shares held by the Foundation represent 54.5 percent of the total shares outstanding. The stock is not listed or traded and no current market value is available.

Statement of Income and Undistributed Income For the Year Ended Mar. 31, 1971

Income:	
Dividends	$1, 992, 099. 26
Interest	450, 821. 23
Rental income, net	14, 026. 00
Total income	2, 456, 946. 49
Expense:	
Attributable to gross income	35, 882. 87
For exempt purposes	106, 357. 84
Total expense	142, 240. 71
Net income for the year	2, 314, 705. 78
Charitable contributions	1, 711, 342. 51
Excess of income	603, 363. 27
Undistributed income, beginning (Adjusted for prior year's depreciation)	1, 625, 745. 04
Undistributed income, ending:	
Allocated as of Mar. 31, 1971	1, 820, 439. 54
Unallocated	408, 668. 77
Total	2, 229, 108. 31

PRESIDENT'S MESSAGE, MARCH 31, 1972

At the close of the past fiscal year The James Irvine Foundation marked its 35th year of service to "the people of California," in accordance with the provisions of the charitable trust established by James Irvine. It has been my privilege to have been associated with this endeavor from the beginning and to have seen at first hand the development and refinement of the Foundation's program for the support of charitable and educational institutions throughout the State. This period has witnessed changes in the status of private foundations which could not have been anticipated a third of a century ago. It is a fitting tribute to the wisdom and foresight of James Irvine that the freedom of action to meet changes reflected in his indenture of trust has permitted the Foundation to meet the needs of today and to plan for the needs of tomorrow.

FINANCIAL

In accordance with a provision of the Federal Tax Reform Act of 1969, independent appraisers were engaged to determine the fair market value of our common stock holdings in The Irvine Company. This appraisal reflects a value of $22.50 per share, or a total of $103,275,000. As the appraisal was not completed before the books were closed for the fiscal year, the nominal value of $2 is still reflected in the appended balance sheet with an explanatory footnote.

EDUCATION

Support for private institutions of higher learning in California has been the particular interest of the Foundation for some years. During the past year nearly one half of our available funds have been devoted to this purpose. Foundation support of educational needs took many forms and included scholarships and grants-in-aid to assist needy young Californias, and provisions for a wide range of "tools" to aid them in this pursuit.

An endowed Chair of Regional and Urban Planning was established at the University of Southern California. This professorship is designed to serve as a nucleus for an expansion by the University of its academic offerings in this field of ecology and to encourage long-range planning and preparation for a better environment.

The continued growth of the School of Law at Stanford University was assisted by a major commitment to a fund for construction of a new teaching and research complex. For the first time in history, the Law School will be housed in its own buildings, designed to provide separate but coordinated units for study, instruction and administration.

HEALTH

Medical knowledge and technology have undergone expansion and sophisticated development in the past quarter century far in excess of any period in recorded history. Unfortunately, the delivery of medical and health services has lagged behind this growth. The gap between ability to serve and availability of the services is now a prime focus in the field of health care. Economics have often been a contributing factor in the separation between patients and treatment. Many procedures traditionally performed only as "inpatient" functions at hospitals can, and are being transferred to "outpatient" status with resulting benefits of reduced costs, better utilization of facilities and, particularly in children, the elimination of trauma associated with overnight separations from family life. This is the goal of the new Ambulatory Surgical Unit now being constructed at Hoag Memorial Hospital in Newport Beach, California. Funded by a Foundation grant, it will provide services on an "outpatient" basis ranging from a child's tonsilectomy to setting an accident victim's broken leg.

This, and other allocations designed to provide for the prevention of illness, and the diagnosis, care and rehabilitation of the sick, comprised the second largest area of Foundation grants, — 29.4 percent of all commitments.

OTHER PROJECTS

Support for services designed for youth or the community s a whole included assistance to projects and programs in the areas of drug abuse, emotional illness, child care, counselling and the disadvantaged.

All grants approved during the past year are enumerated in this report. Unfortunately, they represent only a small portion of the total requests and applications for assistance received by the Foundation. Granting agencies in general find themselves in this unenviable position.

Based upon Treasury Department figures, it appears that in 1971 the 4 percent tax levied on the investment income of foundations reduced by more than 47 million dollars the funds of private foundations available for charitable grants. Legislators should take prompt steps to eliminate this burden on private philanthropy which, if continued, may have the unfortunate effect of depriving charities who are dependent upon private support of approximately 500 million dollars over the next ten years.

N. LOYALL MCLAREN, *President.*

FINANCIAL STATEMENTS

Statement of Assets and Liabilities as of Mar. 31, 1972

Assets:	
Cash, principally savings accounts and time deposits	$2,529,654.19
Property, real and personal property net of depreciation ($11,423.04)	33,275.02
Investments:	
The Irvine Co. common stock at nominal value, see note	2.00
Corporate stocks, bonds and U.S. Government obligations (at cost, quoted market value $6,663,914.00)	6,683,912.83
Other assets:	
Accrued interest purchased	1,625.00
Trust deed notes receivable	938,961.63
Total	10,187,430.67
Liabilities:	
Account payable to broker	140,528.53
Deferred gain on installment sales	147,168.28
Corpus	7,771,062.82
Undistributed income:	
Allocated as of Mar. 31, 1972	1,897,546.84
Unallocated	231,124.20
Total	10,187,430.67

NOTE.—The Irvine Co. is a closely held corporation with 8,415,000 shares of stock outstanding of which the Foundation owns 4,590,000 shares or 54.545 percent. The stock is not listed or traded and consequently has no quoted market value. In order to comply with certain provisions of the Tax Reform Act of 1969 the Foundation obtained an independent appraisal of the fair market value of its Irvine Co. stock. The appraisal, delivered in July 1972, places a fair market value of $22.50 per share on the stock giving the Foundation's holdings a total appraised value of $103,275,000. Following the valuation a proposed amendment to the California Constitution known as the "Coastal Initiative" was qualified for the November 1972 ballot. If passed, the Coastal Initiative may have a material adverse effect upon The Irvine Co. and require a revaluation of the Foundation's stock interest in the company.

Statement of Income and Undistributed Income for the Year Ended Mar. 31, 1972

Income:	
Dividends	$2,054,652.21
Interest	387,575.96
Rental income, net	2,739.71
Total income	2,444,967.88
Expense:	
Attributable to gross income	38,411.80
For exempt purposes	107,774.66
Total expense	146,186.46
Net income for the year	2,298,781.42
Federal excise tax	108,442.53
Charitable contributions	2,290,776.16
Excess of charitable contributions	(100,437.27)
Undistributed income, beginning	2,229,108.31
Undistributed income, ending	
Allocated as of Mar. 31, 1972	1,897,546.84
Unallocated	231,124.20
Total	2,128,671.04

PRESIDENT'S MESSAGE, MARCH 31, 1973

In the past fiscal year, The James Irvine Foundation intensified its efforts to increase higher education opportunities and expand medical and health services in California. The financial crisis in these fields is, of course, too great for this Foundation or all private foundations together to meet, but we can make significant contributions in strategic areas.

In higher education, the past year was marked by new highs in tuition and related student costs accompanied by reductions in government supported scholarship programs and loan funds for students. The Foundation responded by grants to seven institutions of higher learning in California which will provide financial assistance to more than 500 deserving students throughout the State. We also completed the project undertaken in a prior year to establish an endowed Chair of Urban and Regional Planning at the University of Southern California and made the final grant in our multi-year commitment toward construction of a new law school building at Stanford University. Other grants for facilities were made toward construction of a student activity center at La Verne College and for new equipment to modernize the language laboratory at the Monterey Institute For Foreign Studies.

In the medical and health services field, this was a year of unusually wide-ranging action for us. A grant to an infant intensive care unit in San Jose will provide life supporting equipment for high risk infants at birth. Two hospitals in San Francisco and one in Laguna Hills were given major grants to expand their radiology departments. Other grants provided new equipment and facilities for outpatient treatment units in Orange County and San Jose, a renal dialysis center in Berkeley, auditory training units for children with hearing impairments in Redwood City and Los Angeles, an intensive care unit providing specialized respiratory-pulmonary services in San Francisco, and a program for training retarded children in San Fruncisco. A construction grnt was made to provide a centralized blood bank which will service all hospitals and medical centers in Orange County.

Among other grants to youth programs, we assisted the CEDU Foundation of Southern California in the construction of an addition to its residential rehabilitation facility at Running Springs. CEDU is engaged in providing counseling, guidance and training to teenagers with serious emotional problems manifested by delinquent behavior and the use of drugs. Remedial academic

work and vocational training are major aspects of the rehabilitation progrm. The newly constructed ddition will house both classrooms and a library.

The grants of the past year also reflect our interest and continuing involvement in community service and cultural projects.

All of the grants approved during the year are listed by category in the succeeding pages of this report. They, of course, represent only a small percentage of the charitable projects and applications for assistance which were processed and studied by the staff and considered by the directors.

The accompanying financial statements, with explanatory notes, set forth the position of the Foundation at the close of its fiscal year ended Mrch 31, 1973 and its operating results for the year. It should be noted that a market value basis has been adopted in accounting for our investment assets. This change will be of assistance in administering and reporting our investments in accordance with the requirements of the Tax Reform Act of 1969.

N. LOYALL MCLAREN, *President.*

FINANCIAL STATEMENTS

Statement of Assets and Liabilities as of Mar. 31, 1973

Assets:	
Cash, principally savings accounts and time deposits	$2, 379, 058. 92
Property, personal property (net of depreciation—$16,698.22)	28, 088. 57
Investments:	
The Irvine Co. stock at market value as determined by appraisal	89, 505, 000. 00
Listed corporate stocks and bonds, and U.S. Government obligations at market value	6, 892, 705. 83
Other assets: Trust deed note receivable	406, 011. 13
Total	99, 210, 864. 45
Liabilities:	
Account payable to broker	155, 592. 90
Deferred gain on installment sale	63, 636. 21
Corpus	97, 232, 482. 56
Undistributed income:	
Allocated as of Mar. 31, 1973	1, 427, 026. 81
Unallocated	332, 125. 97
Total	99, 210, 864. 45

NOTES

In the fiscal year 1973 the Foundation changed its method of accounting for investments, other than the Irvine Co. stock, from a cost basis to a market value basis. In the same fiscal year the Foundation changed its method of accounting for the Irvine Co. stock from a nominal value basis to a market value basis. Investments other than the Irvine Co. stock are stated at quoted market values.

The Irvine Co. is a closely held corporation with 8,415,000 shares of stock outstanding of which the Foundation owns 4,590,000 shares or 54.54 percent. Since the stock is not listed or traded, the market value is based on an independent appraisal which places a value of $19.50 per share as of Mar. 31, 1973.

The Foundation has changed to the market value basis of accounting for investments in order to more clearly present assets and liabilities and its annual changes in corpus.

Statement of Income and Undistributed Income for the Year Ended Mar. 31, 1973

Income:	
Dividends	$2,543,780.93
Interest	353,715.33
Total income	2,897,496.26
Expense:	
For production of income	172,377.23
For exempt purposes	124,051.79
Total expense	296,429.02
Federal excise tax	96,750.44
Charitable contributions	2,873,835.06
Excess of charitable contributions	(369,518.26)
Undistributed income, beginning	2,128,671.04
Undistributed income, ending	
Allocated as of Mar. 31, 1973	1,427,026.81
Unallocated	332,125.97
Total	1,759,152.78

CHARLES F. KETTERING FOUNDATION: 1972 ANNUAL REPORT

The Kettering Foundation owns assets amounting to approximately $112,702,-238.00, made up principally of bonds and notes amounting to $11,676,785.00 and diversified corporate funds amounting to approximately $100,105,983.00; the remaining assets consist of cash, accounts receivable and deposits and advances. The asset value of The Irvine Foundation as of July, 1972, and based upon the appraisal of Morgan Stanley and Company is approximately $113,000,000.00; the Irvine stock being appraised at $103,250,000.00 and the remaining $7,000,-000.00,consisting of miscellaneous stocks and bonds and account receivable from a trust deed note. Therefore, the negligent performance of the trustees of The Irvine Foundation in connection with the management of its trust fund should be considered in the light of the 1972 Annual Report of the Kettering Foundation and the difference between the two managements very definitely supports the removal of the Irvine trustees.

Attached hereto are xeroxed copies of the Kettering Foundation Financial Management under its board of trustees, as set forth in its 1972 Annual Report, the first year when Section 4942 became applicable to private foundations, following the two year transition period of 1970–1971. The Directors of the James Irvine Foundation were required, by Section 4942, to have organized their financial portfolio the same as the Charles F. Kettering Foundation, and other major foundations did in order to comply with the minimum investment return requirements of Section 4942.

FINANCIAL MANAGEMENT—DIVERSIFICATION GETS MAJOR EMPHASIS

Fiscal year 1972 was a period of significant change in the endowment management of the Foundation.

After a careful study of recent research findings in both the professional and academic literature, the Foundation has taken steps to diversify its portfolio and to increase the management of our investments from two to four external advisory services.

These changes in our financial policy reflect certain recent and still evolving theories of endowment management for optimum long-term return. They are expected to put the Foundation in a position to effectively fulfill its corporate objectives—namely, to undertake research on the most critical societal problems.

The decision to diversify the Foundation's holdings was prompted by a number of factors. To assure prudent endowment management, we must maintain an efficient portfolio of securities. Efficiency in this financial context implies

that investment policy should seek to attain as attractive a return as possible at a given prudent level of risk or, in other words, that the total risk involved in holding investment securities should be kept as low as possible for the desired total rate of return.

Empirical studies of the investment rate of return on New York Exchange stocks indicate that, on the average, approximately 75% of long-term returns from high-grade common stocks have been produced in the form of capital appreciation and 25% in dividend yield. For common stock investment, a total return concept (a concept to which the Foundation has subscribed for several years) requires that expected portfolio return be viewed in terms of total current dividend and interest income plus expected capital gains, rather than in terms of current income alone. Past performance is, of course, also measured by total return.

A widely accepted definition of portfolio risk is related to the volatility of the portfolio's return from quarter to quarter, with the implication that higher risk portfolios will do worse than a market average, such as the Standard & Poor's 500 Stock Index, when the stock market return is declining. It is this exposure to downside risk which may have an important effect on Foundation planning for program expenditures. Conversely, empirical evidence indicates that higher risk, more volatile or aggressive investment portfolios tend to produce higher returns than a market index in a market when the S&P Index is rising. The consistency of this relationship between the expected total return on a portfolio of securities and the volatility of the portfolio's return depends, in part, on the extent of diversification in the portfolio.

A nondiversified portfolio, one concentrated heavily in the stock of a single company, increases the possibility of realizing an investment return substantially less than the overall return on a broad-based market index. This increased exposure to risk does not imply that the risk in General Motors stock, or that of any other single company, is extraordinary. The decreasing risk exposure of a more diversified portfolio simply stems from the averaging out of unanticipated changes in the stock value of a greter number of issues in the portfolio. In this sense, the overall risk or the total variability of the portfolio's return is less for a well diversified portfolio of high-quality companies than it is for a portfolio concentrated in large part in one high-quality company.

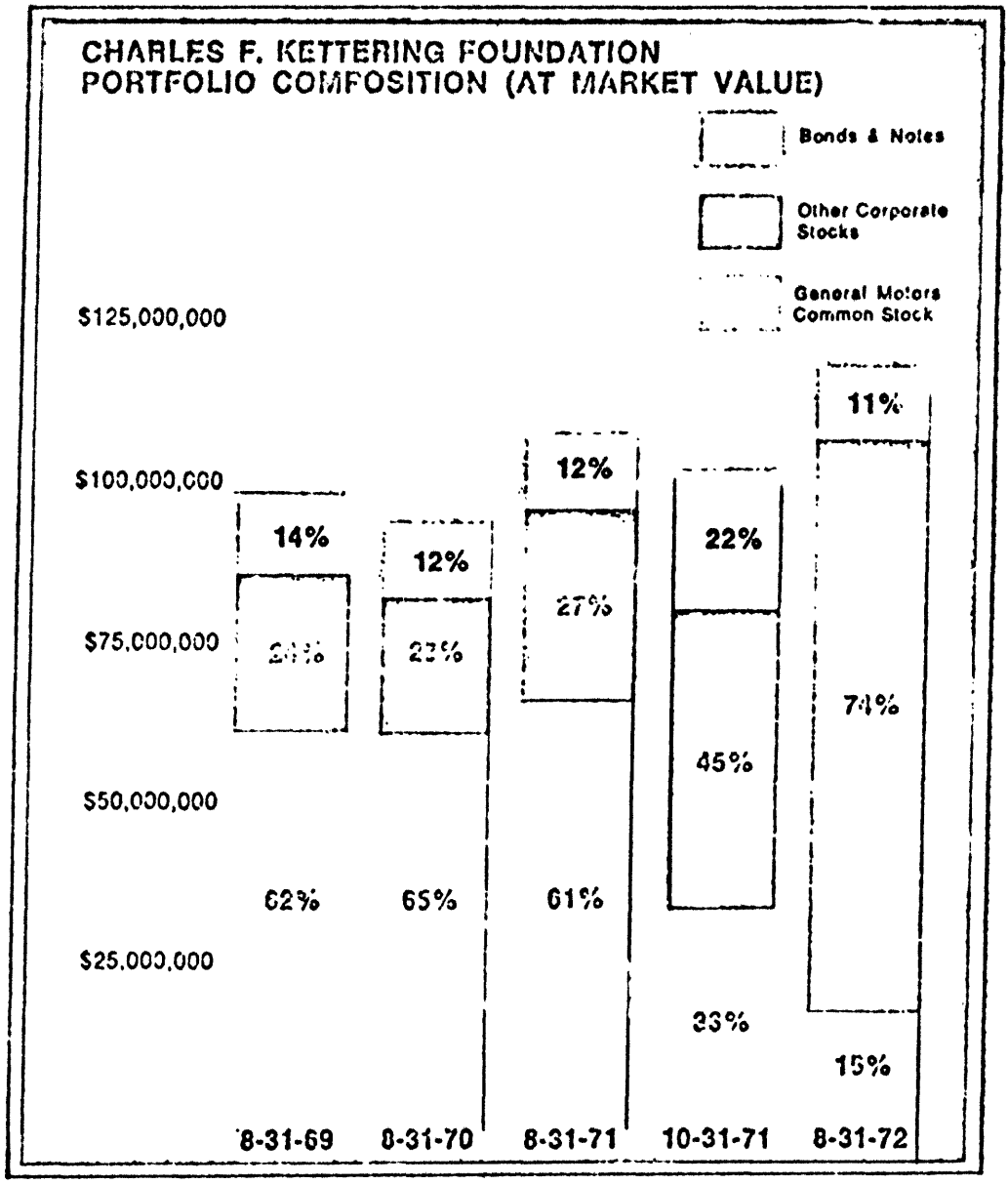
Following the decision to seek a more diversified position for the Foundation's portfolio on these grounds, a large block of General Motors common stock was sold in October, 1971, and additional holdings were substantially diversified during the fourth quarter of calendar 1972. Overall gains in capital appreciation, plus income produced in this period, relative to what would have been produced if diversification had not taken place, have been estimated to be in excess of 3.8 million dollars.

After the decision to diversify the Foundation's holdings, a committee of Trustees and Officers was appointed to select additional investment management services for the proceeds of the sale. After a study by this committee of a number of investment management firms, including interviews and site visits, two new advisors were selected: Capital Guardian Trust Company of Los Angeles and Standard & Poor's/InterCapital, Inc. of New York. Certain Foundation assets are now managed by these advisors, and other portions are managed by previously selected Morgan Guaranty Trust Company of New York and Winters National Bank & Trust Company of Dayton.

The Foundation views its endowment resources and programmatic needs as a total system. Investment objectives and policy, along with the expected return on portfolio assets, are closely related to our projected objectives and expenditures for Foundation programs. For this reason, the Foundation is engaged in a continuing effort to improve financial management and long-range planning of endowment resources and programmatic expenditures. One result has been the development of long-range forecasting models which will enable the Foundation to adequately plan for social research programs in the future. The Foundation is currently projecting extensive increases in program expenditures over the next five years.

The most significant result of these changes in Foundation endowment management, however, is the effect on our financial ability to address critical societal problems and bring about constructive solutions.

In another action by the Foundation's Trustees that is closely related to financial policy, a study was initiated on the question of corporate responsibility and our obligation as an institutional investor. It is expected that this study will form the basis for a formal policy to be adopted by the Foundation during the coming year.



The above chart shows the effect of the Foundation's diversification program during fiscal year 1972.

THE FORD FOUNDATION: 1973

TAX REFORM ACT OF 1969

The Foundation is subject to the provisions of the Act as it relates to private foundations. The Act imposes, among other requirements, an excise tax of 4 percent on net investment income, defined as dividends, interest, and net realized gains on securities transactions, reduced by related expenses. The Foundation paid taxes of $9.4 million for 1972; the tax for fiscal 1973 is estimated at $5.4 million, the decrease reflecting reduced net investment income.

The Act also requires private foundations to distribute income (as defined in the Act) by the end of the year following the year in which earned. The amounts to be distributed are determined on the basis of either income or a percentage of the market value of assets (4¼ percent in fiscal 1973 and rising in stages to 6 percent by fiscal 1976), whichever is higher. The Foundation's actual distributions for the first three years under the Act substantially exceed the required amounts, as follows:

[In millions]

	Distributed[1]	Required
1971	$275.6	$138.2
1972	259.9	112.3
1973 (estimated)	234.3	125.6

[1] Distributions are defined specifically under the Tax Reform Act and will therefore differ from cash disbursements as reported on p. 84.

The Ford Foundation was able to distribute approximately 8%, based on the value of its assets of approximately $3,000,000,000.00, to its charitable beneficiaries in the years as indicated in the foregoing report for the years, 1971, 1972 and 1973, because during the transition period of 1970 and 1971, it had adopted the total return concept and the diversification principle for its investments and through the employment of competent money-managers and advisors. The investment return standard established by the Ford Foundation should be accepted and followed by all private foundations as the "Prudent Private Foundation Investment Rule."

There is no necessity for the adoption of the Schnecbeli Bill, or any other amendment, to the Tax Reform Act of 1969, which reduces the minimum investment return and payout requirements of Section 4942 of the Act at any lower current percentage than 4⅞%, or the ultimate percentage in 1976 of 6%, of the fair market value of the assets of any private foundation.

There does, however, appear to be an amendment, which could be considered by the Subcommittee on Foundations involving the liability for any tax penalty that is assessed by the Internal Revenue Service for violation of any provision of the Tax Reform Act of 1969, or the regulations connected therewith. These tax penalties, as specified in various sections of the Tax Reform Act of 1969, are in some cases imposed on the managers of foundations and generally against the trust fund that belongs to the beneficiaries and should not be resorted to for the payment of tax penalties, as the beneficiaries are not responsible for violations of the law or regulations of the Act. It is the established law that is applicable to charitable trusts, the same as private trusts, that the directors of a charitable corporation and the trustees of a charitable trust, are individually and jointly and severally liable for the negligence or fraud of a co-director or co-trustee that is connected with the management of the trust fund. *Lynch v. John M. Redfield Foundation*, 8 C.A. 3d 393 (California). It would, therefore, seem appropriate that the adoption of an amendment, which will impose any tax liability that is assessed by the Internal Revenue Service against a private foundation, should be collected from the directors of a charitable corporation or the trustee or trustees of a charitable trust.

There are two provisions in the Tax Reform Act of 1969 which place this dividend policy responsibility directly on the Irvine Foundation appointed

Directors of the Irvine Company, to wit: Sections 4942 and 4943 of the Act. In explaining to the United States Senate the purpose involved for the enactment of both Sections 4942 and 4943 the Report of the Finance Committee of said body to the United States Senate related as follows:

"The legislative intent in enacting Section 4942 of the Tax Reform Act of 1969 is to discourage private foundations in making investments in non-productive or low yielding assets, and to currently increase the flow of funds to charity."

With reference to Section 4943, said report stated as follows:

"Those who wish to use a Foundation's stock holdings to acquire or retain business control in some cases are relatively unconcerned about producing income to be used by the Foundation for charitable purposes. In fact, they may become so interested in making a success of the business, or in meeting competition, that most of their attention and interest is devoted to this, with the result that what is supposed to be their function, that of carrying on charitable, educational, etc. . . . activities is neglected. Even when the Foundation attains a degree of independence from its major donor there is temptation of the Foundation's managers to divert their interest to the maintenance and improvement of the business and away from their charitable duties. Where the charitable ownership predominates, the business may be run in a way which unfairly competes with other businesses whose owners must pay taxes on the income that they derive from the business. To deal with these problems, the Committee (Finance) has concluded it is desirable to limit the extent to which a business may be controlled by a private foundation."

The foregoing conversation with Mr. Watson occurred on April 10, 1974, during a telephone conversation between him and Lyndol L. Young, attorney for Joan Irvine Smith. Mrs. Smith had sent a telegram from her home in Middleburg, Virginia, to be deliverey on April 8 to Mr. Watson, a director and President of The Irvine Company, and the directors of The Irvine Company, Newman, Allen, Lund, Wheeler and Gaede, requesting the postponement of the meeting of the Board of Directors on April 9, 1974.. The agenda for the directors' meeting on April 9, 1974 included the approval of the operating and capital budget of The Irvine Company for the fiscal year, 1974–1975, that involved a gross income of more than $100,000,000.00. A copy of this budget was only received by Mrs. Smith at her home in Middleburg, Virginia, on April 1, 1974, which gave Mrs. Smith a period of approximately seven days to review the budget with her attorney, Lyndol L. Young. This budget is a matter of great importance to Mrs. Smith as a 22% stockholder of The Irvine Company. All of the directors of The Irvine Company, with the exception of herself, had either participated in the preparation of said budget or had been consulted with in reference thereto. This budget, which was prepared by The Irvine Foundation, appointed and controlled management of The Irvine Company, projected a dividend for fiscal year, 1974–1975, of only $5,806,800.00, when it is necessary in order for The Irvine Foundation to comply with Section 4942 of the Tax Reform Act of 1969, that a dividend of not less than four times this projected amount be paid during said fiscal year. Mrs. Smith's request that the meeting be postponed was preemptorily rejected by the foundation directors of The Irvine Company, and the regular meeting of the Board of Directors for May 14, 1974 was cancelled. A telegram sent by Mrs. Smith, copies of which were sent to each of the above named directors of The Irvine Company, was received in the office of The Irvine Company on April 8, 1974, and was followed a few days later with a letter from Mrs. Smith to Mr. Raymond L. Watson, President of The Irvine Company, which calls for a special meeting of the shareholders of The Irvine Company to be held on May 13, 1974, in the head office of The Irvine Company, 550 Newport Center Drive, Newport Beach, California. A copy of the telegram and a copy of the letter are attached hereto.

The following telegram was sent by Joan Irvine Smith to Messrs. Raymond Watson, John Newman, Howard Allen, William Lund and Charles Wheeler, as Directors of The Irvine Company on April 6, 1974, and delivered on April 8, 1974:

[Telegram]

After the belated receipt last Monday and a preliminary reading of the voluminous and complex proposed budget for 1974–75 which was prepared by the other directors without my participation, it is blatantly obvious that the planned policy committee meeting for May 15 to consider increasing Irvine Company dividends is just one more bad faith deliberate stall to enable the James Irvine Foundation control prestigious puppet directors of the Irvine Company. To wit: Raymond Watson, John Newman, Howard Allen, William Lund and Charles Wheeler to continue the flagrant Watergate level mismanagement operation of the Irvine Company to restrict and minimize dividends for both the charitable beneficiaries of the James Irvine Foundation and the Irvine Company individual minority shareholders.

You are therefore hereby placed on notice that I am calling a special meeting of the shareholders of the Irvine Company for Monday, May 13, 1974, to consider among other things 1. the responsibility of the directors of the Irvine Company to charitable beneficiaries of the James Irvine Foundation to fully comply with the charitable pay out provisions of the Tax Reform Act of 1969 because of the status of the Irvine Company as a private foundation controlled business enterprise, 2. to consider the payment of substantial special dividend for the years 1973–1974 and the 1975 dividend proposed rate, 3. complete 1974–75 proposed budget disclosure and discussions and comparisons with budget for previous years, 4. complete disclosure concerning negative actions of the Irvine City Council toward the Irvine Company development.

In consideration of the material contained in the agenda for the Board of Directors meeting on April 9, 1974, and as I am the largest individual stockholder owning 22 percent of the stock of the Irvine Company and the only stockholder who is a director of this corporation will be unable to attend this meeting, said meeting should be adjourned without transacting any business until the next regular meeting of the Board of Directors scheduled for May 14, 1974.

JOAN IRVINE SMITH.

APRIL 9, 1974.

Mr. RAYMOND L. WATSON,
President,
The Irvine Co.,
Newport Beach, Calif.

DEAR MR. WATSON: Pursuant to Article II, Section 3 of the Bylaws of The Irvine Company, a West Virginia corporation, which provides that special meetings of the shareholders, for any purpose or purposes whatsoever, may be called at any time by one or more shareholders, owning in the aggregate at least one-tenth of the number of shares outstanding, the undersigned, Athalie Irvine Smith, holding more than one-tenth of the total shares outstanding of The Irvine Company, to wit, 900,000 shares, out of a total issue of 8,415,000 shares, hereby calls a special meeting of the shareholders of The Irvine Company, to be held on May 13, 1974, at 10 o'clock a.m.

You are hereby requested that you, as President of said corporation, and Charles S. Wheeler, as Secretary of said corporation, give notice of the time and place of said special meeting of the shareholders of The Irvine Company, pursuant to this call of the undersigned shareholder, to be held at the principal office of The Irvine Company, on May 13, 1974 at 10 o'clock a.m., at 550 Newport Center Drive, Newport Beach, California.

The above notice should further state that the general nature of the business of The Irvine Company to be inquired about and transacted at said special shareholders' meeting will be:

1. To discuss and consider the responsibility of the individual directors of The Irvine Company to the charitable beneficiaries of The James Irvine Foundation to fully comply with the charitable payout provisions of The Tx Reform Act of 1969, because of the status of The Irvine Company as a private foundation controlled business enterprise.

2. Complete 1974–75 proposed Budget disclosure and discussion and comparison with budgets for previous years.

3. To discuss and consider and to take such action as advisable concerning the present dividend policy of The Irvine Company, and particularly to consider and vote on the adoption of a resolution to be made and seconded at said special shareholders' meeting, which will provide that the regular and special dividend distribution to the shareholders of The Irvine Company for the dividend year, 1973–1974, shall amount to not less than 4⅜% of the market value of the 8,415,000 shares of stock outstanding of The Irvine Company, amounting to $210,375,000.00, based upon the sale by Macco Corporation in 1968 of 13½ shares of the old Irvine Company stocks at $250,000.00 per share, which as of the present time due to the stock split of 10,000 shares to one share would now be $25.00 per share.

4. To discuss and consider any matter that is connected with the management operation of The Irvine Company and its subsidiary corporations, including salaries and awards to executives and the standards on which they are based, administration expense, the number and duties of employees and the payrolls, including a complete disclosure concerning the capital and the income requirements of The Irvine Company.

5. To discuss and consider any matter that a shareholder may inquire about concerning The Irvine Company or the majority shareholder, the James Irvine Foundation, through questions addressed to President Raymond Watson, Chairman of the Board of Directors, John Newman and Vice President–Finance, Lansing Eberling, Guy Clair, Howard Allen, William Lund, Charles S. Wheeler, Howard J. Privett, or any other proxy holder for the James Irvine Foundation.

6. Complete disclosure concerning negative actions of the Irvine City Council toward The Irvine Company development.

7. Complete discussion and consideration of the lawsuit filed by the Big Canyon Country Club against The James Irvine Company for damages in the sum of $27,000,000.00 and the total expenses and legal fees already paid and incurred and to be paid.

8. To discuss and consider and vote on the adoption of any motions which are made and seconded at the special shareholders' meeting.

Please send a copy of this letter to all of the shareholders of The Irvine Company with the Notice of Special Meeting of The Irvine Company to be held on May 13, 1974 at 10 o'clock a.m.

Sincerely,

ATHALIE IRVINE SMITH.

In the message from President Mason to the stockholders of the Irvine Company for the year 1970, he states:

"In today's dynamic business climate diversity and expansion are the keys to a broad base success. This company has a firm grip on these keys, and our continuing progrm is producing substantial growth (with very little net income). Successful diversification requires capable personnel, at all levels, in each area. Irvine is meeting this challenge in building a specialized management team.

Despite the short term situation, management is optimistic about the long term potential for substantial increases in earnings and after growth. The basis for these increases is being created in shopping centers, office buildings and apartment fields.

During the past year (1969–1970) it was possible to continue–the construction program on funds generated primarily from operations and mortgage financing on completed projects. During the next fiscal year the company will enter into a period which will require using its bank lines of credit for construction of income producing projects which, upon completion, will be refinanced from long term mortgage financing.

Irvine enters the new year with existing income-producing properties (but not net income) which will account for approximately one-half of the forecasted gross income for fiscal 1970–1971; the other half of the gross income will come from residential and industrial activities and new commercial projects which will be completed during the year. Further, the continuing expansion program includes approximately One Hundred Million Dollars of construction

for future income producing properties which are now under design or construction."

On January 1, 1970, the Tax Reform Act of 1969 was in full force and effect. While the James Irvine Foundation had a trnsition period for the years 1970–1971 to reorganize its investment portfolio, by selling its Irvine stock and in reinvesting the proceeds from such sale in diversified securities, or by adopting a program that would substantially increase the current dividend fund of the Irvine Company, it did neither. Obviously under the announced program of Mr. Mason in his above mentioned message to the stockholders of the Irvine Company, there was no thought or intention on the part of the Irvine Foundation Directors of the Irvine Company to make any effort to comply with Section 4942 of the Tax Reform Act, and to fraudulently evade the law.

Mr. Mason's report to the stockholders of the Irvine Company, for the fiscal year 1970–1971 discloses the continuing anti-dividend and expansion and diversification and investment plan disclosed by Mr. Mason in 1967. In this report Mr. Mason states:

"All operations have been formulated to provide balances between income growth and after growth. The major source of income growth is sales of lots for single family homes, and the fee sale of industrial sites. New assets are created by construction of apartments, shopping centers, office buildings and the leasing of various commercial and industrial sites. The value of existing assets both land and buildings—is influenced favorably by the planning and construction of new developments.

The change in organization is further evidence of the changing character of this company. In the past ten years the company has gone through the transition of a land-owner—agricultural to a successful real estate developer, while continuing its operations in agriculture. The amount of development activities this company undertakes increases each year. The quality of real estate holdings, to wit: shopping centers, office buildings, apartment buildings, marinas, ground leases increases each year."

Mr. Mason did not submit a message to the shareholders at their Annual Meeting in June 1972, but in the Annual Report for 1973 there is a letter from Mr. Mason to the stockholders of the Irvine Company. This letter contains the following paragraph:

"The company made a net investment of $20,302,883.00 in property additions during 1972–1973 (commencing in 1972 The James Irvine Foundation, as a tax exempt organization, was under the Congressional mandate contained in the Tax Reform Act of 1969 to fully comply with the minimum investment return pay-out requirements to the charitable beneficiaries). A majority of these expenditures were in income producing investment properties. These properties, office buildings, shopping centers, apartments, industrial inventory buildings, etc. . . . will add to the company's long term earning producing capacity. Long term debt amounted to $61,194,553.00. This debt is secured by income-producing properties which are producing annual cash flows in excess of the debt service. In addition, the company has mortgage loan commitments totaling Thirty Nine Million Dollars to be funded as various projects are completed. Management believes that with the funding of the above mentioned loan commitment, and the company's bank lines of credit, totaling Thirty Million Dollars, the company has adequate sources of funds to increase further growth."

The above mentioned sum of $20,302,883.00 which went into property investments during the year 1972–1973, was diverted from the dividend fund which otherwise should have gone to the charitable beneficiaries of the James Irvine Foundation, and the minority stockholders. Mr. Mason died in July 1973.

While the investment properties program, which was instituted by Mr. Mason when he became President of the Irvine Company in 1966, and thereafter until his death in 1973 proceeded under the orders and directions of Mr. McLaren as President of the James Irvine Foundation, and Chairman of the Board of Directors of the Irvine Company, this program, not only violated the intent of the Congress as expressed in Section 4942 of the Tax Reform Act of 1969, but it was deliberately carried out in defiance of the mandate contained in Section 4942.

The real estate taxes and the interest that was paid on the mortgage that covered each and every investment properties project that was constructed,

such as multi-family apartments, shopping centers, office buildings, nd industrial buildings substantially reduced the net income which otherwise should have been distributed as dividends.

On July 1, 1966, when Mr. Mason became the President of the Irvine Company, real estate taxes were $2,763,649.00, and interest expense was $125,716.00.

In 1967 real estate taxes have been increased to $3,481,742.00.

In 1968 real estate taxes had increased to $5,875,000.00, nd interest had increased to $726,035.00.

In 1969 real estate taxes had increased to $5,754,458.00, and interest had increased to $1,804,172.00, and the long term debt during the period 1967–1969 had increased from $3,231,055.00 to $22,320,616.00.

In 1970 real estate taxes had increased to $5,949,699.00, and interest had increased to $1,830,064.00, and the long term debt had increased to $29,211,609.00.

In the year 1971 real estate taxes had increased to $5,790,824.00, and interest expense had increased to $2,371,420.00, and the long term debt had increased to $43,106,159.00.

In 1972 the real estate taxes had increased to $6,128,637.00, and interest had increased to $3,695,644.00. The long term debt had increased to $56,551,406.00.

In the year 1973 real estate taxes had increased to $8,309,583.00, and interest had increased to $4,550,600.00 and long term debt had increased to $62,363,116.00.

The budget for 1974–1975 discloses that during this fiscal year real estate taxes on The Orange County eighty three thousand acres owned by the Irvine Company will be $12,157,800.00, and that interest will amount to $8,600,000.00, and that the long term indebtedness of the Irvine Company will be increased to approximately Seventy Five Million Dollars.

The 1974–1975 operating budget for the Irvine Company discloses that during this fiscal year the Irvine Company will show a loss of $3,334,800.00 from the investments the company has made in shopping centers, office buildings, multi-family buildings and industrial buildings. The Irvine Foundation management of the Irvine Company attempts to justify these losses by stating that their investment property program, through equity funding with dividend money, will begin to show some profit in the next ten to twenty years.

Section 4942 of the Tax Reform Act of 1969 prohibits the use by The Irvine Foundation Management of The Irvine Company of after-tax net income from the sale of the capital assets of The Irvine Company for the investment properties program involving long term periods before any net income is available for dividend purposes as this investment use of net income in non-productive or in low yield assets precludes the current increase of the flow of funds to the charitable beneficiaries of The Irvine Foundation. The basic objective for the enactment of Section 4942 of the Tax Reform Act of 1969 is to require private foundations to dispose of their unproductive assets and low yield stocks so that charity will currently receive the minimum investment return income that calls for a percentage distribution to charity of 4⅛% to 6% by 1976 of the value of the assets held by private foundations. The program of The Irvine Foundation directors of The Irvine Compny to divert this after-tax net income for investment purposes in non-productive or low yield assets is a violation of Section 4942 of the Tax Reform Act of 1969 and never should have been continued subsequent to December 30, 1969, when the Act became effective.

It would appear, from Mr. Mason's statement, that this so-called investment fund of $20,302,833.00 came from net income earnings for the fiscal year 1972–1973, and that the use of said money as indicated by Mr. Mason, came from dividend money which should have been distributed to the charitable beneficiaries and the minority stockholders of the Irvine Company. Mr. Eberling should also disclose to the shareholders at said meeting the total amount of money which has been diverted from net income and used for investment property purposes, during the period from July 1, 1966 to the present time.

At the meeting of the Board of Directors in September 1973, the Irvine Foundation Directors passed a resolution that provided for the payment of a pension to N. L. McLaren, retired Chairman of the Board of Directors of the Irvine Company and President of the James Irvine Foundation since the death of Myford Irvine in January, 1959.

Another resolution was adopted at the same time to pay the widow of William R. Mason the sum of $51,000.00. The resolution for McLaren's pension granted

him the sum of $500.00 per month during his lifetime, and upon his death the sum of $250.00 per month during the lifetime of Mrs. McLaren.

The other resolution for Mr. Mason's widow authorized a straight cash payment of $51,000.00 to her which the resolution stated is one-half of the annual salary that Mr. Mason was receiving at the time of his death. Mr. Watson should disclose to the shareholders, at said Special Meeting on May 13, 1974, the authority that is vested in the Board of Directors of the Irvine Company to authorize and direct any officer of the Irvine Company to pay either the pension of $500.00 per month to Mr. McLaren or the sum of $250.00 per month to his widow, or the payment of $51,000.00 to the widow of Mr. Mason.

At the time of Mason's death he was receiving substantial bonuses or awards $39,000.00, in addition to his salary of $102,000.00 per year, and he also had a vested interest in the Executive Award Plan for an unknown mount, which would be payable to his widow.

So far as McLaren is concerned the Executive Incentive Award Plan expressly provided that McLaren was excluded, as Chairman of the Board of Directors, from participating in the Plan. Neither did the Irvine Company have a Retirement Plan for executives of said corporation. The only duties McLaren performed as Chairman of the Board of Directors, was to preside at meetings of the Board and during the period of thirteen years that he was Chairman of the Board of Directors of the Irvine Company, he received approximately the sum of $300,000.00 for his nominal service and expenses to come from San Francisco to Los Angeles for the purpose of presiding over not more than nine or ten meetings per year of the Board of Directors of the Irvine Company during said period of thirteen years.

Upon the death of James Irvine, in 1947, which occurred under mysterious circumstances, when he allegedly was discovered floating in the river on the Irvine Ranch in Montana by two individuals who had gone to Montana with him, his son, Myford Irvine was elected President of the Irvine Company. At this time Myford Irvine was vice President and Director of the Irvine Company and President of the James Irvine Foundation. During the lifetime of Myford Irvine the Irvine Foundation did not attempt to interfere with the management of the Irvine Company, but upon the death of Myford Irvine, in January 1959, through alleged suicide, the Foundation President, Mr. McLaren, who succeeded to this office upon the death of Myford Irvine, and the Foundation Vice President, Mr. McFadden, moved in lock, stock and barrel and took over the management control of the Irvine Company.

McFadden was elected as President, but as he had planned a trip to Europe, McLaren was elected as Acting President during McFadden's absence. After the return of McFadden from his trip to Europe, McLaren was elected as Vice President and Director of the Irvine Company, and soon thereafter he became Chairman of the Board of Directors of the Irvine Company. In 1960 the Irvine Foundation selected as President of the Irvine Company, Charles S. Thomas, whose only qualification for this appointment was that he was a personal friend of McLaren. Thomas served as President from 1960 to June 30, 1966, and received a salary of $60.000 per year. Upon his retirement as President on June 30, 1966, Thomas was retained as a no time, no duty consultant for a period of seven years, and at a salary of $30,000.00 per year. This give away payment of $210,000.00 to Mr. Thomas is a typical example of the Irvine Foundation management of the Irvine Company, which has deprived the charitable beneficiaries of the Irvine Foundation from receiving the distribution of substantial dividends from the Irvine stock held by the Irvine Foundation, as Trustee.

On July 1, 1966 William R. Mason was elected as President of the Irvine Company to succeed Mr. Thomas. In Mr. Mason's First Report to the Stockholders of the Irvine Company, at the Annual Meeting of the Stockholders in June 1967, he states:

"From 1960 to the present The Irvine Company has undergone a dynamic transition from a mainly agricultural operation to an array of widely diversified activities. The business has become more and more complex as the activities are producing more volume and scope.

"One of our key public relations and advertising slogans, 'the six part world of the Irvine Ranch,' as indicated by the advertisement, reproduced on this

page. The six part world exemplifies our corporate activities in the residential, commercial, industrial, agricultural, and cultural fields. It reaffirms our policy of giving concurrent attention to those basic elements which will enable us to offer the finest planned and best balanced communities in the nation."

Nothing is stated in Mr. Mason's Report, or in any subsequent report to the stockholders of the Irvine Company, up to and including his final report in June, 1973, a short time before his death, that gives any indication of any kind that the major business of the Irvine Company, under the control of the James Irvine Foundation, as a tax exempt organization was and is to produce the maximum amount of current dividends to be distributed to the charitable income beneficiaries of the Irvine Foundation.

After the adoption of the Tax Reform Act of 1969, when the Irvine Foundation received a mandate from the Congress that it had to change the management policy of the Irvine Company in order to comply with the minimum investment return requirements of Section 4942 of the Act by currently increasing the flow of dividends to said charitable beneficiaries, nothing whatever took place with reference to changing the policy of the Irvine Foundation management of the Irvine Company which indicated any attempt to comply with Section 4942.

When Mr. Mason died in July 1973 the Foundation Directors of the Irvine Company elected Raymond L. Watson to succeed Mr. Mason as President. Mr. Watson at this time was Executive Vice President of the Irvine Company, and in charge of the Planning Department. Mr. Watson, like Mr. Mason, had never had any experience with financial matters or corporate affairs. Prior to joining the Irvine Compny in 1960, his entire experience had been that of an architect who worked in the office of an architectural firm in San Francisco. To demonstrate Mr. Watson's lack of experience, to understand the economic problems which confront the Irvine Company under the control of the Irvine Foundation, with reference to producing substantial net income with which to pay the dividends required by Section 4942 of the Tax Reform Act, is the schedule contained in the 1974–1975 Operating and Capital Budget for the Irvine Company, which discloses that although Mr. Mason increased the number of employees of the Irvine Company from three hundred, when he became President on July 1, 1966, to nine hundred nineteen at the time of his death in July 1973, Mr. Watson has increased the number of employees, commencing with the new fiscal year 1974 to one thousand one hundred four employees.

Realizing the opportunity by management to take advantage of the cash flow program inaugurated by Mr. Mason, and now being carried on by Mr. Watson, to receive higher salaries and bonuses, the Foundation controlled Board of Directors of the Irvine Company, in 1970, adopted the Executive Incentive Award Plan. The objective of this Plan is solely to increase the salaries and bonuses of the executives of the Irvine Company, and, of course, it does not include any bonuses or increased dividends to the charitable beneficiaries of the Irvine Foundation. The stated objective of the Plan is as follows:

"The primary objective of the present study was to recommend to the Employees Compensation and Benefits Committee an effective incentive award which would meet the stated objectives of rewarding exceptional performance with exceptional compensation. The primary objectives of the studies were those which relate to executive compensation.

To attract and retain the high caliber executive and managerial talent needed to improve the company profitably in an increasingly competitive market for experienced executives. *To secure a joint interest between management and the ownership in the optimum long term profitability and performance of the Irvine Company.*

To assist executives in building personal estates and providing security for their families.

To help executives reduce some of the effect of high personal tax rates upon their compensation.

The proposed Plan, which later was adopted, further states:

"*Nonetheless, the basis for the present award plan and intentions of the Committee are in agreement that top management should have a sense of sharing in company growth over the long term, and should be able to participate in*

this growth. Consequently the design of the award plan should continue to emphasize the joint interest of both parties as much as possible"

As part of the Executive Incentive Award Plan the President of the Irvine Company, in addition to his salary of approximately $100,000.00 receives an annual bonus of anywhere from thirty percent to sixty percent of his annual salary, and the Senior Vice President of the Land Development Division, in addition to his salary of approximately $75,000.00 per year, receives from twenty-five percent to fifty percent of his annual salary, and all of the other Vice Presidents, in addition to their very substantial salaries, receive all the way from ten percent to forty percent of their annual salaries.

Actually what has happened under the Irvine Foundation management of the Irvine Company, is that through the diversification and investment property program and the substantial cash flow that is received from the operation of this program, and the large sums of money that are paid to the executives of the Irvine Company for their salaries and bonuses and awards, another transition has occurred that has substituted the executives of the Irvine Company, N. L. McLaren, President of the James Irvine Foundation, James V. Newman, Director and Vice President of the Irvine Foundation and Director and Salary Chairman of the Board of Directors of the Irvine Company, Chrles S. Thomas, retired President of the Irvine Company, James H. Metzgar, Vice President and Director of the Irvine Foundation and Broker for the insurance of the Irvine Company, Mrs. Kathryn L. Wheeler, Director of the Irvine Foundation, and whose husband, Charles S. Wheeler is Secretary of the Irvine Company, at a salary of $25,000.00 per year, the members of the McCutchen law firm, attorneys for the James Irvine Foundation, and the Irvine Foundation Directors and the Foundation Directors of the Irvine Company, and the excessive employee payroll recipients of the Irvine Company—as the real charitable beneficiaries of the James Irvine Foundation.

This unauthorized scuttling of the "People of California" as the beneficiaries of the James Irvine Foundation completely disregards and violates the Indenture of Trust executed by James Irvine, as Trustor, and the James Irvine Foundation, as Trustee, and the charitable motives of James Irvine, as described in said governing instrument and the Articles of Incorporation of the James Irvine Foundation and the Tax Reform Act of 1969, and jeopardizes the tax exemption of the Irvine Foundation as a charitable tax-exempt organization.

JOAN IRVINE SMITH,
By LYNDOL L. YOUNG, *Counsel.*

LOS ANGELES, CALIF., *March 22, 1974.*

EDWARD W. CARTER, MORRIS M. DOYLE, JOHN S. FLUOR, ROBERT H. GERDES, A. J. MCFADDEN, N. LOYALL MCLAREN, JAMES H. METZGAR, JOHN A. MURDY, JR., JOHN V. NEWMAN, RUDOLPH A. PETERSON, MRS. KATHRYN L. WHEELER, *Directors of The James Irvine Foundation and Trustees of the Foundation's Trust Fund*

DEAR SIRS AND MADAM: On January 18, 1973, I sent to each of the directors of The James Irvine Foundation, including yourself, certain legal demands on behalf of Mrs. Joan Irvine Smith and stated to you that, unless you indicated by a reply to said letter, through your attorneys, an action would be filed by Mrs. Joan Irvine Smith on behalf of and for the benefit of the beneficiaries of the Trust Fund of The James Irvine Foundation, to remove each of you, as a Director, of The James Irvine Foundation and to surcharge each of you, as such director, with damages amounting to substantial sums of money and based upon your fraud and gross negligence in the management of the Trust Fund of The James Irvine Foundation.

The letter above mentioned particularly demanded that you cause the Foundation's attorneys to dismiss the fraudulent action that was instituted against the Attorney General of California on December 31, 1971; to immediately cause a Registration Statement to be prepared and filed by The Irvine Company with the Securities and Exchange Commission covering a proposed secondary public offering of the 4,590,000 shares of the Irvine stock held by

the Foundation, as Trustee, at the price of your own appraisal of not less than $22.50 per share.

I never received a reply to this letter, and I understand that your failure to reply was based upon your assumption that the only party that could institute an action for your removal and to surcharge you for your fraud and gross negligence in the management of the Trust Fund of The James Irvine Foundation is the Attorney General of California and further that you had been assured that he would not file such an action. It is quite true that the directors of the Foundation are possessed of considerable Republican party political clout as well known "elite Republicans" who make substantial contributions to campaigns of Republican politicians, who seek elections to State offices, like Mr. Younger.

You are now advised that I have received a letter from Attorney General Younger that, should such an action be filed by Mrs. Smith, his office will not oppose either the filing of such an action by her or the prosecution of the same by Mrs. Smith on behalf of and for the benefit of the charitable beneficiaries of the Trust Fund of The James Irvine Foundation. Mr. Younger, as the Attorney General of California, under the law will be named as a party defendant in such action, and I seriously doubt that he will refuse to cooperate with Mrs. Smith, who will appear only as the nominal party in this proposed action, for this is the only course that I am sure he would take, as the Attorney General of California, who is required by law to preserve, protect and enforce the rights of the beneficiaries of charitable trusts.

I am enclosing herewith a summary of the testimony of your attorney and representative, Mr. Howard J. Privett, which took place at hearings before Congressional Committees in Washington on April 6 and 10, 1973. You will note from Mr. Privett's testimony that he assured both of said Congressional Committees that, just as soon as judgment was entered in your pending case against the Attorney General, the directors of the Foundation would immediately cause all necessary steps to be taken with reference to the accomplishment of a secondary public offering of the 4,590,000 shares of Irvine stock held by the Foundation, as Trustees. Although there has been some discussion with your director, Mr. John V. Newman, and Mrs. Smith and me concerning the filing of a Registration Statement with the Securities and Exchange Commission, nothing has been done in connection therewith since the entry of judgment in said case on December 31, 1973. The latest conversation with Mr. Newman took place on March 12, 1974, following the meeting of the Board of Directors of The Irvine Company, when Mrs. Smith stated to Mr. Newman that she approved of the payment by The Irvine Company of the expenses connected with the preparation of this Registration Statement, which I understand is estimated to be approximately $250,000.00.

Long before the entry of the judgment, above mentioned, the Foundation was required as to its tax years, 1972–1973, and 1973–1974, to comply with the minimum investment return and the charitable distribution requirements provided by Section 4942 of the Tax Reform Act of 1969. On August 24, 1971, the California Legislature added Section 2271 to the Civil Code of California, and this statute expressly amended the indentures of trust, or other governing instruments of private foundations in California, to comply with the requirements of the Tax Reform Act of 1969. This statute was adopted as urgency legislation and, therefore, was operative and effective on August 24, 1971. Notwithstanding the adoption of this legislation and the automatic amendment of the Trust Indenture of The James Irvine Foundation, pursuant thereto, your attorneys filed the fraudulently motivated action against the Attorney General on December 30, 1971, solely for the purpose of fraudulently evading Section 4942 of the Tax Reform Act of 1969, and, by this action, you have attempted to defraud the beneficiaries of the Foundation Trust Fund from receiving the full distribution, which they were entitled to receive during both the Foundation's tax year, hereinabove mentioned.

Each director of The James Irvine Foundation is, therefore, subject to being surcharged for the amount of money which should have been distributed to its charitable beneficiaries during both of said tax years.

Had the directors of the Foundation complied with the requirements of Section 4942 of the Tax Reform Act during the transition period of 1970 and

1971, and sold their Irvine stock and reorganized the Foundation's financial portfolio investment, as did practically every other major foundation in the United States, your Foundation would have been able to distribute to its charitable beneficiaries not less than $10,000,000.00 during each of said taxable years. There is no question but that the stock of The Irvine Company could have been sold in the public market, by the Foundation during 1971 and 1972, for not less than $103,000,000.00 and, if this had been done, the proceeds of such sale could have been reinvested in a portfolio of diversified stocks and bonds which would have produced, according to the experience of the Ford Foundation and other similar foundations, a gross income of not less than 15% of $100,000,000.00, provided that the foundation directors employed competent, financial advisors as all other major foundations, according to their annual reports, did during the transition period of 1970 and 1971.

Mrs. Joan Irvine Smith and her mother, Mrs. Athalie R. Clarke, have called a special meeting of the shareholders of The Irvine Company for April 8, 1974, at the hour of 1:00 o'clock p.m. at the principal office of The Irvine Company, to wit, 550 Newport Center Drive, Newport Beach, California. One of the matters to be discussed and transacted at this meeting will be the adoption of a motion to be made and seconded that the shareholders of The Irvine Company authorize and direct the Board of Directors of The Irvine Company at their regular meeting to be held on June 11, 1974, to declare a special dividend of 4¾%, based on the price paid by The Irvine Company to the Macco Corporation in 1968 for the purchase of 13½ shares of Irvine stock at $250,000.00 per share. At the present time, the price reflected by this sale would be $25.00 per share because of the stock split in 1970 of 10,000 shares for one share, which gives the total value of $210,375,000.00 to all of the issued and outstanding stock of The Irvine Company. The share of this special dividend, which will be received by the Foundation should enable it to make a "good faith" gesture by the Foundation to comply with its pay-out requirements to the beneficiaries of the Foundation Trust Fund for both tax years, 1972–1973 and 1973–1974. The beneficiaries of the Trust Fund are entitled to receive their share of this special dividend, and it would be gross negligence and a breach of trust by each foundation director, should the proxy representative of the Foundation vote against the adoption of this proposed resolution and payment of said special dividend, and the directors will be individually subject to surcharge for their negligence if said proxy representative does not vote favorable on said proposed resolution.

This proposed special dividend can be paid very easily from retained earnings, which according to the consolidated statement of income and retained earnings of The Irvine Company for the year ended April 30, 1973, amounted to the sum of $44,868,427.00. This large sum of money principally consists of the accumulation of the profits received by The Irvine Company from the liquidation of capital assets.

You, as a director of the Foundation, are, or should be, aware that all regular and special dividends that have been paid by The Irvine Company to its shareholders have principally come from the profits derived from the liquidation of capital assets, and very little, if any, of the money represented by said dividends has come from net income resulting from management operations.

FISCAL YEAR ENDED MARCH 31, 1973

Gross Income: Land development operations $4,615,746.00. Agricultural operations $3,685,241.00. Land development sales $7,882,013.00. Total $16,183,000.00. Net income $8,718,563.00, but $5,140,591.00 thereof received from the liquidation of capital assets leaving net income from operations of $3,577,972.00. Dividend $1,218,375.00. This dividend should have been at least 50% of net income of $8,718,563.00, or $4,359,281.00, and the charitable beneficiaries of the Foundation should have received 54.5% of this dividend sum, or approximately $2,000,000.00, but only received $600,000.00.

The distinction which Mrs. Smith has made in criticizing the management of The Irvine Company that has been selected by The Irvine Foundation with reference to operating net income and profits received from the liquidation of capital assets was confirmed by your attorney, Mr. Privett, when he appeared

before the Committee on Ways and Means on February 21, 1969, and gave the following testimony during his examination by Mr. Corman, a member of the Committee:

"Mr. CORMAN. I had some misunderstanding of what the profit was for the Irvine Company (for the fiscal year, 1967–1968). At one point I understood that it was $1¼ million but maybe that was the part that went to the foundation (the amount of the dividend, as above stated, was $1,218,375.00). I am talking about the most recent year for which you have figures.

"Mr. PRIVETT. I said that our dividend was $1¼ million. I have before me the exact figure. In the last year, 1967–1968 fiscal year, we received a dividend of $2.225.00 per share, or $1,021,075.00 for the year. The dividend rate is currently $2,353.00 per share which would increase that to the figure indicated.

"Mr. CORMAN. Did I understand that in that same year that the profit for the company after taxes was $8,000,000.00?

"Mr. PRIVETT. *Not if I say operating profit after taxes.*

"Mr. CORMAN. That is what we got as the difference from the $13,000,000.00 figure.

"Mr. PRIVETT. The total income, which includes return from sale of capital assets as well as operating income, was $13,000,000.00. After taxes the total income, including the capital transactions, was $8,718,000.00. Now, of that $6.4 million of this $8.7 million was from the disposal of capital assets. Principally, that was the San Diego Freeway condemnation and the Corona del Mar Freeway condemnation. There are condemnations of land and the money is paid in. It is income, but it is a return on a capital asset which is not operating income. That is, it is not the profit or the return from operations."

FISCAL YEAR ENDED MARCH 31, 1968

Gross Income: Land development operations $9,406,748.00. Agriculaural operations $4,180,856.00. Total $13,587,604.00. Net income $2,988,843.00, but $2,549,-167.00 thereof received from the liquidation of corporate assets, leaving net income from operations $439,676.00. Dividend $1,539,000.00.

FISCAL YEAR ENDED MARCH 31, 1969

Gross Income: Land development operations $20,857,474.00. Agricultural operations $4,788,500.00. Total $25,645,974.00. Net income $5,496,251.00, but $2,348,-457.00 thereof received from the liquidation of capital assets, leaving net income from operations $3,147,794.00. Dividend $2,420,550.00.

FISCAL YEAR ENDED MARCH 31, 1970

Gross income: Land development operations $24,925,385.00. Agricultural operations $3,885,289.00. Total $28,810,674.00. Net income $6,485,677.00, but $4,785,-892.00 received from the liquidation of capital assets, leaving net income from operations $1,699,785.00. Dividend $2,608,650.00.

FISCAL YEAR ENDED MARCH 31, 1971

Gross Income: Land development operations $23,433,374.00. Agricultural operations $5,104,363.00. Total $28,537,737.00. Net income $6,297,367.00, but $6,240,-657.00 received from the liquidation of capital assets, leaving net income from operations of $56,710.00. Dividend $3,450,150.00.

FISCAL YEAR ENDED MARCH 31, 1972

Gross Income: Land development operations $32,738,748.00. Agricultural operations $7,827,116.00. Total $40,565,864.00. Net income $7,637,510.00, but $5,522,-393.00 thereof received from the liquidation of capital assets, leaving net income from operations of $2,115,107.00. Dividend $3,534,300.00.

FISCAL YEAR ENDED MARCH 31, 1973

Gross Income: Land development operations $39,403,746.00. Agricultural operations $8,373,803.00. Total $47,777,549.00. Net income $9,102,115.00, but $8,004,-

796.00 thereof received from the liquidation of capital assets, leaving net income from operations of $1,107,319.00. Dividend $4,375,800.00.

While the proposed special dividend is based upon the Macco sale of Irvine stock to The Irvine Company at $250,000.00 per share, this basis should not be understood to represent the fair market value of the underlying assets of The Irvine Company, as the same will be eventually determined by the Internal Revenue Service, which at the present time is making an appraisal through the firm of Marshal and Stevens under contract to the Internal Revenue Service. During the hearing before the Patman Committee on April 6, 1973, Mr. Privett stated to the Committee that the appraised value of the undeveloped land of The Irvine Company by the County Assessor of Orange County substantially agreed with the appraisal obtained by the Foundation from Morgan Stanley & Company amounting to $189,000,000.00. At this hearing, a much higher figure, representing the County Assessor's appraised value, was disputed by Mr. Privett However, when further questioned by a member of the Committee, Mr. Privett agreed to submit the actual figures of the County Assessor, showing his appraisal of the fair market value of the undeveloped land of The Irvine Company for the year, 1973, when the taxes levied by the County Assessor amounted to approximately the sum of $9,800,000.00. While Mr. Privett did not himself furnish the Committee, as he agreed he would do, with the Assessor's figures, the Washington law firm of Covington & Burling, by John T. Sapienza and Newman T. Halvorson, Jr., as counsel for The Irvine Foundation, wrote a letter on June 5, 1973, to the Committee and therein stated that the assessed valuation of the undeveloped Irvine lands, as allegedly determined by the County Assessor of Orange County, would be approximately $490,000,000.00, just $301,000,000.00 more than the figure of $189,000,000.00, given by Morgan Stanley & Company and Mr. Privett. On the basis of $490,000,000.00, The Irvine Foundation was required under Section 4942 to distribute to its beneficiaries that sum of money which represented 4⅛% for 1972–1973 and 4⅜% for 1973–1974, of $490,000,000.00. Furthermore, the actual amount which will be determined by the Internal Revenue Service, which would have been distributed to said beneficiaries, will be based upon the appraisal which is now being made by the Internal Revenue Service which Mr. Newman has indicated will be substantially higher than the Morgan Stanley appraisal and which undoubtedly will also be higher than the alleged appraisal of the Orange County Assessor in the sum of $490,000,000.00.

It, therefore, appears that the Foundation will be in serious difficulty with the Internal Revenue Service over the appraisal of Morgan Stanley & Company and that the fraudulent evasion by the foundation directors to meet the pay-out requirements to its beneficiaries under Section 4942 in both the fiscal years, 1972–1973 and 1973–1974, will result in tax penalties, if not in a suspension of the tax exemption of the Foundation for both of these fiscal years. If this does occur, the directors of the Foundation will certainly be surcharged for their fraud and gross negligence in their management of the Foundation Trust Fund and their violation of Section 4942.

The fiscal year, 1973–1974, will not end until April 30, 1974, so we do not have the exact figures for this period. The following figures are, therefore, based upon the budget covering the consolidated statement of income for the year ending April 30, 1974, which discloses that gross income from land development operations is $55,929,400.00 and gross income from agricultural operations is $11,165,500.00, or a total sum of $67,094,900.00. Although the net income is budgeted at $9,492,900.00, the gain from the liquidation of capital assets is the sum of $5,229,100.00, leaving a net income from operations of $4,263,800.00. Dividends for this fiscal period were two regular dividends in September and December, 1973, each for 12¢ per share, and March, 1974, at 15¢ per share. There will probably be the same 15¢ per share regular dividend in June, 1974, or a total regular dividend for 1973–1974, of 54¢ per share. As hereinabove mentioned, a special shareholders' meeting has been called by Mrs. Smith and Mrs. Clarke for April 8, 1974, for the purpose of considering the payment of a special dividend.

In connection with the Morgan Stanley appraisal, Mr. Privett testified before the Committee on Ways and Means on April 10, 1973, that the Internal Revenue Service asked the Foundation, because the Irvine stock had never been traded

in and had no market, to obtain an appraisal at that time. This statement is another flagrant example of Mr. Privett's deliberate misrepresentations to the Congressional Committee. The Internal Revenue Service did not expressly ask the Foundation to make an appraisal, and Mr. Privett knew it. The Annual Report of the Foundation for the year dated March 31, 1972, states at page 10, as follows: "In order to comply with certain provisions of the Tax Reform Act of 1969, the Foundation obtained an independent appraisal of the fair market value of its Irvine Co. stock. The appraisal, delivered in July, 1972, places a fair market value of $22.50 per share on the stock giving the foundation's holdings a total appraised value of $103,275,000.00."

This appraisal was made pursuant to TIR-1128, published on December 26, 1971, which was designed to provide guidance to a private foundation with respect to the valuation of certain of its non-charitable assets in computing its minimum investment return. Notice of this proposed rule-making under Section 4942 was published on June 7, 1971, and public hearings were held on August 5, 1971. The notice to all private foundations concerning TIR-1128 required private foundations to obtain an accurate, independent appraisal of non-charitable assets other than traded securities and cash. The notice further suggested that such an independent appraisal would be good for a five-year period. TIR-1128 responded to comments received at the public hearing and made it clear that the use of an independent appraisal was not mandatory. A foundation could, s an alternative, use any standard method of valuation, but this alternative would not have the same presumption of correctness as an independent appraisal. The final regulations under Section 4942 were published on February 5, 1973. These regulations provided that untraded stocks in a closely built corporation must be valued every year.

Another misrepresentation by Mr. Privett in his testimony, both before the Subcommittee on Domestic Fiuance on April 6, 1973, and before the Committee on Ways and Means on April 10, 1973, was the statement by Mr. Privett that The James Irvine Foundation was not required to comply with the minimum investment return pay-out requirements to its charitable beneficiaries, commencing with its taxable year, 1972–1973. Section 4942 requires generally that a private foundation distribute annually to charity the greater part of its adjusted net income or a fixed percentage of the fair market value of its non-charitable assets, whichever is higher. The legislative intent of this provision was to discourage investments in non-productive or low-yielding assets and to currently increase the flow of funds to charitable activities. With respect to a private foundation, organized after May 26, 1969, the income distribution standards, based upon a percentage of the fair market value of its non-charitable assets (i.e., the minimum investment return), apply to taxable years beginning after December 31, 1969. As to an older foundation, such as The James Irvin Foundation, however, the minimum investment return standard applies only to taxable years beginning after December 31, 1971. The first taxable year, therefore, of The James Irvine Foundation commenced on April 1, 1972, and ended on March 31, 1973. It was required to meet the pay-out requirements to charity under Section 4942 during its taxable year, 1972–1973, on the basis of 4⅛% of the fair market value f its non-charitable assets, to wit, its 4,590,000 shares of Irvine stock and its other miscellaneous investments amounting to approximately $10,000 000.00, and the return of the Foundation for this period was required to be filed on May 15, 1973. It is obvious from the Annual Report of the Foundation for the year ended March 31, 1973, that its return, whenever filed, for this period discloses that the Foundation is deliberately in default in meeting the pay-out to charity requirements under Section 4942, on the basis of 4⅛% of the fair market value of its non-charitable assets, even on its own Morgan Stanley appraisal of $103,375,000.00 for its Irvine stock.

In the meeting that Mr. Newman had with Mrs. Smith and me on March 12, 1974, he stated that the Foundation had not met the pay-out requirements under Section 4942 for its tax year, 1972–1973, and it did not do so for its tax year, 1973–1974, when the percentage pay-out was increased to 4⅜% and that it had until 1975 to meet these requirements. On the basis of the letter of your attorneys, Covington & Burling, dated June 5, 1973 to the Subcommittee on Domestic Finance, it is admitted by the foundation directors that the

assessed valuation of the underlying assets of The Irvine Company is $490,000,000.00, which is $301,000,000.00 more than the Morgan Stanley appraisal of $189,000,000.00. The basis referred to by Morgan Stanley & Company, in their appraisal in reaching the value of the total outstanding Irvine stock of $189,000,000.00, is a restricted valuation of The Irvine Company, as a going concern, and the treatment given to the earnings and dividends of this corporation for the period of five years before the date of the appraisal. Morgan and Stanley, whom your attorney, Mr. Privett, refers to as the most prestigious investment banking firm on Wall Street, knew or should have known of, and, of course, your attorneys, and particularly Mr. Privett, who claims to be an expert of tax law, as well as private foundation appraisal law, certainly was familiar with, Revenue Rule 59-60, which expressly states as follows: "The value of the stock of a closely held investment or real estate holding company, whether or not family-owned, is closely related to the value of the assets underlying the stock. For companies of this type, the appraiser should determine the fair market values of the assets of the company. Operating expenses of such a company and the cost of liquidating it, if any, merit consideration when appraising the relative values of the stock and the underlying assets. The market values of the underlying assets give due weight to potential earnings and dividends of the particular items of property underlying the stock, capitalized at rates deemed proper by the investing public at the date of appraisal. A current appraisal by the investing public should be superior to the retrospective opinion of an individual. For these reasons, adjusted net worth should be accorded greater weight in valuing the stock of a closely held investment or real estate holding company, whether or not family-owned, than any of the other customary yardsticks of appraisal, such as earnings and dividend paying capacity."

The final regulations covering Section 4942, which were issued on February 5, 1973, expressly state that the appraisal of closely held corporations, whose stock is not traded or listed, like the stock of The Irvine Company, shall be based on the above Revenue Rule, which is connected with Section 2031 of the Internal Revenue Code.

When Mr. Privett appeared before the Committee on Ways and Means on April 10, 1973, he charged Mrs. Smith with making a false statement concerning the investment made by The Irvine Company under the express instructions of the foundation directors in the Big Canyon Country Club. In his continuing misrepresentation of the true facts, he characterizes the lawsuit filed by Mrs. Smith and her mother, Mrs. Clarke, in West Virginia, for the purpose of restraining The Irvine Company from going ahead with this discriminatory country club project, as being of the same dilatory character as her other litigation. He stated that this country club project was a decision of The Irvine Company management, which you will recall he referred to as having been selected by the foundation directors, and which could have been fired by said directors at any time, if said directors did not approve of their management practices. Privett further stated that this foundation management obtained approval of the Board of Directors of The Irvine Company to go ahead with this country club project, but he did not mention that the Board of Directors was controlled by the Foundation. He further stated that Mrs. Smith filed another lawsuit in West Virginia, claiming that this country club action was *ultra vires* and was beyond the authority of the company under its articles of incorporation. He concluded his remarks by stating that on April 7, 1970, a special shareholders meeting occurred, and at this meeting the articles of incorporation were amended, according to West Virginia law. He did not state that the Foundation voted its 54.5% majority stock holding in The Irvine Company, which was all that was needed to amend the articles. Following this special meeting of the shareholders, the amended articles of incorporation were filed in West Virginia, and on April 14, 1970, the identical resolution to go forward with the country club project was placed back before the Board of Directors, and it was adopted by the foundation-controlled Board of Directors and carried out. The most flagrantly false part of his statement to the Committee was as follows: "The project has done well—much better than even the corporate management believed it would. The project was one of the highly successful ones for which our (foundation) professional management is deserving of credit and not the criticism they have received from Mrs. Smith."

When Mr. Privett made the foregoing statement to the Committee, he, as the attorney for the Foundation, knew that the members and board of directors of the Big Canyon Country Club had threatened to bring action against The Irvine Company for damages caused by the negligent construction of the country club golf course and club quarters. In September, 1973, approximately five months after Mr. Privett appeared before the Committee on Ways and Means, the Big Canyon Country Club, a non-profit corporation, and the members thereof filed a lawsuit against The Irvine Company for damages in the sum of $27,000,000.00 for "breach of fiduciary duty; fraud; conspiracy; accounting; breach of duty of care of directors; negligence; breach of contract, nuisance; and wrongful discharge of water."

I understand that negotiations are in progress between the foundation management of The Irvine Company and the foundation directors and the Big Canyon Country Club to settle this lawsuit for a substantial sum of money. In the event that any money of The Irvine Company is used for this settlement, the directors of The Irvine Foundation will be held responsible, as this country club project was strictly the creature of The Irvine Foundation directors, who deliberately violated the injunction of the West Virginia court by amending the articles of incorporation through their majority stock holdings in The Irvine Company, fr the sole purpose of going ahead with the completion of the country club project.

At the meeting with Mr. Newman on March 12, 1974, Mr. Newman stated that the Foundation was considering letters of interest received from certain undisclosed corporations to purchase the 4,590,000 shares of Irvine Company stock owned by the Foundation, as Trustee, and he indicated that an offer from one of these corporations would soon be received by the Fundation. Mrs. Smith, on this occasion, advised Mr. Newman that any proposed sale of the Foundation's Irvine stock to a corporation, or any other single entity or individual, was completely unacceptable to her, as a 22% shareholder in the Irvine Company, and that she would litigate any such proposed sale. Mrs. Smith further told Mr. Newman that the lesson that she had received from the foundation-control of the Board of Directors of The Irvine Company and the management of said corporation had taught her that never again, so far as she could control the situation, would her 22% stock holding in The Irvine Company be jeopardized by the substitution of another entity for The James Irvine Foundation, as the 54.5% shareholder of The Irvine Company.

There is nothing in the Conclusions of Law or in the Judgment signed by Judge Loomis in the case of the Foundation against the Attorney General which takes anything away from the self-executing impact of Section 2271 of the Civil Code, which automatically amended the Indenture of Trust of the Foundation on August 24, 1971, and which statute made the filing of such lawsuit completely improper and absolutely unnecessary.

Mr. Privett attended the hearings before the Committee on Ways and Means, The Tax Committee of the House of Representatives and the Committee on Finance of the United States Senate, which were held in connection with H.R. 13270, known as the Tax Reform Act of 1969. He is familiar, as the attorney for the Foundation, with the reports filed by each of these committees with the Congressional bodies, and he, therefore, knows from his own personal knowledge that the filing of the lawsuit on December 30, 1971, against the Attorney General constituted an overt act that was connected with the conspiracy of the foundation directors and their attorneys to fraudulently violate the pay-out requirements of Section 4942 in the Foundation's tax years, 1972–1973 and 1973–1974. The Report of the Finance Committee to the Senate includes the following statement at page 38 thereof, which refers to the pay-out requirements of Section 4942 as follows:

"*Effective date.*—The payout requirements apply to taxable years beginning after December 31, 1969. However, in the case of an existing organization, the minimum payout (the 5-percent rule described above) is not to apply until taxable years beginning after December 31, 1971.

"To afford existing organizations a greater opportunity to revise their investment and payout practices, the Committee added a phase-in period with regard to the 5-percent rule. For calendar-year organizations, this would mean that in

1972 the minimum payout would be 3½ percent, 4 percent in 1973, 4½ percent in 1974, and the basic 5-percent rule would apply thereafter. If the 5-percent figure is decreased by the Secretary of the Treasury before 1975, then the phase-in period percentages are to be proportionately adjusted.

"The minimum payout amount is not to apply to the extent it cannot be met because the foundation's existing governing instrument requires income to be accumulated, but only if this requirement in the governing instrument would not have caused the organization to lose its exempt status under present law. Also, the minimum payout requirement will not apply to the extent that the foundation's existing governing instrument forbids invasion of corpus to meet the payout requirement. These exemptions will continue after 1971 only to the extent that it is impossible to reform the foundation's governing instrument to permit it to comply with the general rule."

The last sentence of the above quoted statement is most significant in determining the true motivation of the directors of the Foundation and its attorneys that is connected with the filing of said lawsuit six months after the Indenture of Trust of the Foundation was automatically amended by the adoption of Section 2271 of the Civil Code. What was *impossible* for the Foundation to bring any action to reform its Indenture of Trust, as this instrument had already been automatically amended by the Legislature?

Mr. Privett, in his argument before Judge Loomis on July 12, 1973, stated that the Foundation desired a judgment based on the equitable jurisdiction of the court, because certain undisclosed underwriters, who were interested in underwriting the public sale of the Irvine stock owned by the Foundation, insisted that such a judgment be obtained. Whether this statement is true or not, these underwriters, of course, had no authority to make a request of the directors of The Irvine Foundation that the pay-out provisions of the Tax Reform Act be violated by such a shenanigan, as this lawsuit. The complaint filed by the Foundation in this action did not allege, as required by the final regulations covering Section 4942, that Section 2271 was invalid. Section 2271 of the Civil Code was adopted pursuant to a temporary regulation covering Section 4942, which was issued by the Treasury Department on June 5, 1971, and which provided that, if the states in which private foundations were located adopted legislation which automatically amended the governing instrument f private foundations to comply with the 1969 Tax Reform Act, any such lawsuit, as filed by the Foundation against the Attorney General, was completely unnecessary. When he testified before the Committee on Ways and Means on April 10, 1973, he admitted this knowledge with the following statement:

"I have only one final charge I want to answer. This is a serious one. Here Mrs. Smith says that the foundation, and I guess myself personally, since I am the lawyer that recommended this, am engaged in a charade by bringing in the California Superior Court a lawsuit which is wholly unnecessary to amend the terms of our Trust Indenture.

"Let's see how she gets there. Mrs. Smith says the reason the lawsuit is a charade and unnecessary is because of a Treasury Regulation, and she says under the Treasury Regulation you don't have to file a lawsuit if it turns out that the state has adopted a statute which affects the amendment. What that tax regulation says, in fact, I have it here before me, it says that a private foundation's governing instrument shall be deemed to have been so amended 'if valid provisions of state law have been enacted' and then it goes ahead to recite to do those things—it says 'valid provisions of state law.'"

On July 12, 1973, when the trial of the foundation lawsuit against the Attorney General commenced, Mr. Privett knew that the Treasury Department had issued Revenue Rule 72-103, which expressly approved Section 2271 of the Civil Code, as valid legislation and that the governing instrument of The James Irvine Foundation had been automatically amended by this statute, as required by Section 508(e) of the Internal Revenue Code. Mr. Privett knew, on July 12, 1973, that on February 5, 1973, the Treasury Department had issued its final regulations covering Section 4942 of the Tax Reform Act of 1969, and that these regulations expressly stated that any provision of state law, such as Section 2271 of the Civil Code of California, which had previously been

approved by Treasury Rule 72-103, shall be presumed valid as enacted, and that this rule not only applied to The James Irvine Foundation, but also to all other private foundations, that did not specifically, in a legal action, allege that such statute was invalid, and that a judgment had been entered that such statute was invalid by the highest appellate court of the state where the action was filed, or by the United States Supreme Court. The highest appellate court in California is the Supreme Court of California, and this court has not held that Section 4942 of the Tax Reform Act of 1969 is invalid.

It is also clear from the record in the plaintiff's lawsuit against the Attorney General that Judge Loomis intended that the Conclusions of Law signed and filed by him, wherein it is stated that Section 2271 of the Civil Code of California is valid and constitutional, was also an integral part of the Judgment entered by Judge Loomis.

On December 31, 1973, a hearing in the above mentioned case was requested by Deputy Attorney General Block and during this hearing Mr. Block brought the matter concerning the validity of Section 2271 to the attention of Judge Loomis, because in the Conclusions of Law signed by Judge Loomis, it was expressly stated that said statute was valid and constitutional. Mr. Block indicated to the court that it appeared to him that in the Judgment of the court that the court had ignored this statue, and Judge Loomis replied as follows:

"The court hasn't ignored the statute, I don't believe. The court hasn't ignored the statute because in its intended decision it has specifically made reference to such statute."

The reference by Judge Loomis to his intended decision is as follows: "The court is of the opinion that the passage of Civil Code Section 2271 represents a valid exercise of the power of the California Legislature. The court rejects the suggestion that such legislation, if self-executing to amend automatically instruments concerning charitable trusts, is unconstitutional."

It will be recalled that Mr. Privett had argued to the court during the trial that it was desired that the Judgment of the court be based upon its equitable jurisdiction, because certain underwriting firms stated that such a judgment would be helpful to the sale of the Irvine stock by the Foundation in a public market underwriting. Judge Loomis apparently had this statement of Mr. Privett in mind when he stated:

"Suppose in some other state the court should determine this statute as unconstitutional. Might that not affect any sale of this stock by reason of underwriting requirements? If that is so, isn't it necessary for the court to make a declaration under equitable powers?"

It is difficult to understand how any state other than California would have any jurisdiction to declare Section 2271 of the Civil Code unconstitutinal, when the Internal Revenue Service has already made a mandatory ruling which is applicable to all tax exempt organizations in California—this includes The James Irvine Foundation—that Section 2271 of the Civil Code is valid until the Supreme Court of California declares that this statute is invalid.

Insofar as the Judgment signed by Judge Loomis in the Foundation's lawsuit against the Attorney General is concerned, it was never the intention of Judge Loomis that the Foundation should use such Judgment for the purpose of defrauding the beneficiaries of the Foundation's Trust Fund by willfully failing to make the distributions to said beneficiaries, as required by Section 4942 of the Tax Reform Act.

Furthermore, in the complaint that will be filed by Mrs. Smith on behalf of and for the benefit of the beneficiaries, wherein the foundation directors and the attorneys for the Foundation will be the defendants, there will be an allegation to the effect that the Superior Court of the State of Califrnia, for the County of Los Angeles, did not have jurisdiction to entertain said action by reason of the adoption by the Legislature of Section 2271 of the Civil Code on August 24, 1971, and, therefore, that said Judgment is void, and is also void on the further ground that said Judgment perpetrates a fraud upon the beneficiaries of the Foundation Trust Fund and was obtained through collusion between the foundation directors and their attorneys and the Office of the Attorney General of California. By reason of said collusion, the beneficiaries of the

Foundation's Trust Fund did not have the proper representation by the Attorney General of California of their rights and interests as such beneficiaries. Because of this dereliction of duty by the Attorney General of California, the said beneficiaries have been defrauded of millions of dollars, which they were entitled to receive from said Fundation Trust Fund during the years, 1972–1973 and 1973–1974.

In my letter of January 17, 1973, to each of the directors of The James Irvine Foundation, I included two excerpts from the book entitled, "The Big Foundatins" by Waldemar A. Nielsen. This is an appropriate place to again bring these excerpts to your attention as a director of The James Irvine Foundation, as follows:

"For more than twenty years the interlinked ranch company [Irvine Company] and Foundation [Irvine] have gained a particularly unsavory reputation for financial misconduct, and the Foundation's philanthropic program is widely regarded as one of the poorest in the country.

"The Irvine Foundation is neither the first nor the only foundation to embellish its image with high flown verbiage. But given the many grounds for suspicion surrounding all its operations, its public reports suggest deliberate deception."

At the hearing before the Subcommittee on Domestic Finance on April 6, 1973, Mr. Annunzio also had something to say with reference to The Irvine Foundation directors as follows:

"Mr. ANNUNZIO. Well, due to the fact that the foundation, as was brought out in the testimony, owns 54 percent of the Irvine Co., will the books of the Irvine Co. also be available to us and the General Accounting Office?

"Mr. PRIVETT. I feel certain that they would, but that is a question, since that is a separate corporation with its separate board and separate counsel, that I will have to refer to them.

"Mr. ANNUNZIO. The foundation does have control, and I appreciate your answer and you can have a couple of weeks to think about it. You're going to be hearing from us again, and we would like to know if both of these books will be available to us.

"I looked, for a few minutes, at the report of the appraising company.

"Mr. PRIVETT. The report of the Morgan-Stanley Co.?

"Mr. ANNUNZIO. The Stanley Co.

"And I'm not going to quarrel with the Stanley Co. I know they are a highly reputable firm, but there are many things missing in this report: the appraisal that was made; the land values; the earnings and dividends; the cash flow; there are many things that are missing. I want to point that out to you.

"Another thing disturbs me, when I went through this report. You read the biography of these people (directors of the Foundation). It looks like a Who's Who of Great Americans. I read all of them.

"Mr. PRIVETT. We do believe that we have a distinguished board.

"Mr. ANNUNZIO. I look at this board of directors. It includes retired admirals, senior partners, trustees of the California Institute of Technology, and it goes on and on. Here I find three of these people drawing a salary, sitting on the board, and I'm talking about the foundation—Loyall McLaren, $10,200; James Metzgar, $2,400; John Newman, $2,400. They have a little expense account, too, the same three, not counting the others. McLaren, $2,100; Metzgar, $2,100; Newman, $1,950. Then you look further and there is one person on the staff, yes, it's a lady, at $7,200. At least she types. I wonder what the others do to draw their money.

"One staff person is getting $7,200 and all this money is being paid to these other people on the board who are officers of this particular foundation.

"Now, I do charity work in Chicago, and I will give you the right to investigate the charity work I do, and I don't even charge for a postal stamp or gasoline and I am chairman of the board of a large old people's home in Chicago, but these people have got to be paid, and this is not their money."

I have hereinabove referred to the Foundation's suit against the Attorney General as a shenanigan. When Mr. Privett appeared before the Committee on Ways and Means on April 10, 1973, he took great exception to the remarks by Mrs Smith that this lawsuit was a charade.

At this hearing on April 10, 1973, Mr. Burke, Acting Chairman of the Committee on Ways and Means, must have had the directors and attorneys of The James Irvine Foundation in mind, when he made the following statement to a panel, representing several private foundations, who were also present at said hearing, with the following remarks:

"Mr. BURKE. I want to make this observation before the panel leaves. We are not against foundations, but we have had a lot of complaints about activities of some foundations. Our hearing in 1969 brought out many of those shenanigans and, of course, this gave a black eye to many innocent foundations that were doing good work. That is the difficulty. Sometimes the innocent have to suffer with the guilty."

You will recall, I am sure, that Mr. Mark L. Sullivan was a director of both The James Irvine Foundation and The Irvine Company for several years before the year 1970, when he was required to resign his directorship in both of these corporations, because he refused to be a party to the fraudulent evasions of Sectin 4942 of the Tax Reform Act of 1969, which the other directors of the Foundation attempted to impose on him. I have in my possession a copy of a sworn statement from Mr. Sullivan, which in summarized form content is as follows:

With reference to the purchase of the Irvine stock from Macco in 1970, the foundation directors attempted to control the vote of Mr. Sullivan, as a director of The Irvine Company, to the effect that said Irvine stock be purchased by The Irvine Company, but not cancelled. Mr. Sullivan states that he, along with Mrs. Smith, was in favor of the purchase of the Macco stock, but insisted that the same be cancelled. At the time this matter came before the Board of Directors of The Irvine Company, Mr. Sullivan wanted to know what the foundation directors wanted the Macco stock for and what difference it would make whether it was cancelled or not; he further wanted to know what the foundation directors intended to use the Macco stock for and that it appeared to him that the foundation directors intended to use the Macco stock for stock options. He voted that the stock be purchased and cancelled and all of the other foundation directors of the Board of Directors of The Irvine Company, to wit, McLaren, Mason and Newman, voted against the calcellation.

I assume that Mr. Sullivan is a man of fireat integrity and excellent business standing in San Francisco, as, I understand, at one time he was the President of the Pacific Telephone Company of California and that he was on the board of directors of many other substantial corporations.

Mr. Sullivan further relates in said sworn statement that another reason he was required to resign as a director from both The James Irvine Foundation and The Irvine Company was due to the position that he took with reference to the obligation and responsibility of the Foundation and its directors to fully comply with the provisions of the 1969 Tax Reform Act. He states that the Act provides that the tax-exempt foundation must limit its investment in any one company to 20% of the outstanding stock of any controlled corporation, such as The Irvine Company, which is controlled by The James Irvine Foundation. He further states that the Foundation had a company, to wit, The Irvine Company, where practically 100% of the foundation was invested in The Irvine Company, that there was a provision in the Act that gave The Irvine Foundation a two-year breathing period, or a period of grace, within which to sell its Irvine stock. Mr. Sullivan further states that he took the position that the Foundation ought to get busy and sell out the Irvine stock and do whatever was necessary, so the Foundation could get in conformity with the 1969 Tax Reform Ace in an orderly way and safely within the two-year time framework (1970–1971), but the other directors were opposed to doing so, because if they did, it would mean that they would lose the control of The Irvine Company. To do this, in his opinion, constituted a violation of the Tax Reform Act, and he refused to go along with that. As a result of his refusal, he was required to resign as a director of both the Foundation and The Irvine Company.

Mr. Sullivan relates his position on another transaction which displeased the other directors of The Irvine Foundation. This concerned the purchase by The Irvine Company of stock in the San Joaquin Fruit Company. He states that John V. Newman, who was and is a director of both the Foundation and

The Irvine Company, held stock in this corporation; that the amount to be paid for said stock by The Irvine Company was in the neighborhood of $1,700,000.00 and that he did not, as a director of the Foundation and The Irvine Company, believe that this was a good investment for The Irvine Company, and he questioned the wisdom of doing so. The foundation directors replied that The Irvine Company could develop the land of the San Joaquin Fruit Company into residential districts, etc., but he couldn't see why The Irvine Company, which already held more than 80,000 acres of land wiating to be developed, needed to buy another 1,000 acres, which was represented by the purchase of said stock; particularly, he was opposed to the purchase because John V. Newman was going to get some profit out of the transaction, and he did not believe that it was proper for Mr. Newman, as a director of the Foundation and a director of The Irvine Company to receive this profit.

Mr. Sullivan also states that he believed that the foundation directors were making excessive payments to the executives of The Irvine Company and were attempting to give excessive bonuses and stock options and what-have-you to these executives, which in turn would serve the self-dealing interests of the Foundation. Mr. Sullivan further stated that during the period that he was a director of the Foundation and The Irvine Company that the Executive Committee of The Irvine Company held meetings in a secret office in San Francisco, so that Mrs. Joan Irvine Smith wuld not have any knowledge of such meetings.

Don't waste your time or mine by having your attorney, Mr. Howard J. Privett, reply to this letter. I have already notified Mr. Privett that his opinion of the actions of Mrs. Smith and myself, as her attorney, and his threats of dire results that will happen to us in the event any further litigation is filed by Mrs. Smith against the Foundation, carries about as much weight with Mrs. Smith and me as that of a feather flying in the breeze. If there is any discussion desired by the directors of the Foundation concerning any of the matters referred to in this letter, that can be accomplished only through a meeting between the foundation directors, or one director, and Mrs. Smith and me, as her attorney. Such a meeting could take place either before or after the shareholders' meeting on this coming April 8 or April 9, when the next meeting of the Board of Directors of The Irvine Company takes place. As Mr. Newman resides in Southern California, I suggest that he communicate with me by telephone with reference thereto before March 29, 1974.

Yours very truly,

LYNDOL L. YOUNG.

Howard J. Privett is the attorney for The James Irvine Foundation, and he also is authorized to appear as the representative of this foundation before the Committees of Congress. In this capacity, he appeared before the Subcommittee on Domestic Finance of the Committee on Banking and Currency, House of Representatives on April 6, 1973, and again appeared in the same capacity before the Committee on Ways and Means, House of Representatives, on April 10, 1973.

When Mr. Privett appeared before the Subcommittee on Domestic Finance, when questioned by Mr. Gettys, a member of the Committee, he identified himself as the duly authorized representative of The James Irvine Foundation as follows:

"Mr. GETTYS. Mr. Privett, I have several questions. Would you answer them just very briefly and the last three 'yes' or 'no.'

"What is your relationship to the foundation?

"Mr. PRIVETT. Solely as its counsel.

"Mr. GETTYS. Now, are you here today with the knowledge, consent, and approval of the board of directors?

"Mr. PRIVETT. I am.

"Mr. GETTYS. Have you been the authorized spokesman for the foundation before other Congressional Committees in the last five years?

"Mr. PRIVETT. I have."

Concerning the control of The Irvine Company by The James Irvine Foundation through its ownership of 54.5% of the stock of The Irvine Company, Mr. Privett testified under oath as follows:

"It (The Irvine Foundation) has selected what it believes to an excellent, professional management for that company, and that company is run by that professional management, and the foundation, as a stockholder, attends the meetings, gets the reports. If they lost confidence in the management they could, of course, fire the management and replace it.

"The CHAIRMAN. You mean the foundation directors could.

"Mr. PRIVETT. Yes. If they lost confidence in the management they had employed." (Page 273, Hearings on Domestic Finance)

Mr. Privett further testified as follows under examination by Mr. Crane, a member of the Committee:

"Mr. CRANE. Let me ask one final question, and this has to do with the net income of the foundation from its shares in the Irvine Co.

"Do you have the figures for the returns of the foundation for the past several years?

"Mr. PRIVETT. I have the most recent year and I could supply all of the years to you.

"Mr. CRANE. Well, rather than an absolute figure, if you would put the absolute figure in the records, I would appreciate that, but can you give me an idea of the percentage of return on the of Irvine Co. held by the foundation.

"I mean, if the value of the foundation's assets is $103 million—(based on the Morgan Stanley appraisal)

"Mr. PRIVETT. Yes.

"Mr. CRANE. Then what percentage of return on that has been produced over the last several years to the foundation?

"My recollection, and the reason I am asking the question is, I think the Tax Reform Act requires a return, does it not, of somewhat over 4 percent?

"Mr. PRIVETT. Yes; that is correct, Mr. Crane.

"Now, for the year 1973, the Irvine stock is projected to pay a dividend of 52 cents a share, and that is in my formal statement. We own 4,590,000 shares. So 52 times 4,590,000 shares would be——

"Mr. CRANE. Somewhere in the neighborhood of $2¼ million.

Do you have any idea—I'm not a mathematician—could you quickly break that down into a percent terminology?

"Mr. PRIVETT. It is a little bit over 2 percent is what the dividend income return is." (Page 285)

"Mr. PRIVETT. Now, since the 1969 Act we have filed the necessary proceedings and the California Attorney General is cooperating with us. We will go to trial in June on a case to correct the trust instrument so we may divest ourselves (of Irvine stock) because if we don't we will be subject to confiscatory taxation under the 1969 Act.

"Now, when we amend the trust instrument in that respect, we are also going to amend the other part of the trust instrument which states that we cannot make distribution out of the capital of the trust to charity.

"Now, under H.R. 4942 we have to make distributions equal to the minimum investment return established by the Secretary each year. If we were limited solely to use of the income, (from the Irvine stock) then the 2 percent obviously would not be sufficient in order for us to make it, but with those changes in the trust instrument, we will be able to apply the same total return concept that all other foundations are applying to realize the income necessary to make the distributions.

"Now, if we had the power to sell this equity and to go ahead with a marketing program which is in planning, and if we had the power to make distributions out of capital, then we will have ample in the way of both realized and unrealized capital gains which, coupled together with the dividend income, will be more than sufficient to meet this requirement.

"Mr. CRANE. Well, I would hope that those conditions which allow, enable the property to increase so astronomically over the past 25 years does not precede the pace over the next 25 years. *But I would gather that you would be sympathetic to the idea of the divestiture of the foundation (of its Irvine stock) at this point because you could get out from under those provisions of the initial grant from Mr. Irvine that insisted that you retain all of your assets and the property that was bequeathed, and you could then contemplate realizing maybe a 7 or 8 percent return at least.*

"Mr. PRIVETT. *That is correct. We've asked the superior court in Los Angeles to enter a judgment which will amend this trust instrument in the various particulars that I have mentioned.*

"*Now, let me say also that it is the record of this foundation's operations that they are charitable. They must operate implicitly in the public interest.*

"*Now, we immediately set about doing all of those things required by law and by the Securities and Exchange Commission, and other people who regulate the marketing of stock, to do those things necessary to make sure that we market this equity within the time allowed by the Tax Reform Act, and we feel that our job is to act implicitly in terms of what the 1969 act requires. That's our intention, and, if we fail in that, it will be not because of an intention on our part not to succeed, but because we lack the capacity to do so.*

"Mr. CRANE. Thank you.

"I have exceeded my time, but I would like to ask one more quick question, and that is, the appraisal on the value per share of stock (Irvine stock) that the foundation holds is $22.50 or thereabouts.

"When you divest, will you be divesting shares of stock, or will you be divesting pieces of real estate?

"Mr. PRIVETT. The only thing we own and the only thing we can divest is the shares of stock.

"Mr. CRANE. Now, when you do divest yourselves of the shares of stock, will those be sold to the public or how will that divestiture take place?

"Mr. PRIVETT. *That is under intensive study right now, Mr. Crane, and as soon as the directors have fixed upon a plan, that will be submitted to the California attorney general, and the California attorney general will then approve the plan or suggest changes of it, and then the directors will revise the plan.*

"*Now, there obviously are several marketing techniques that can be recommended or used in the marketing of this kind of equity. Which of those the directors will determine in their business judgment is the one that will produce the highest return consistent with our meeting the obligation of the tax law, cannot be stated yet. The directors haven't finally made that decision.*

"*Now, they are receiving the advice of what I believe are some of the premier investment banking houses in the country as well as other people who are knowledgeable in this area, and as soon as these studies are completed, they will put a plan together which will then be submitted to the California attorney general and with his approval that marketing program will go ahead.*" (Pages 287-288)

On April 10, 1973, Howard J. Privett appeared before the Committee on Ways and Means and identified himself as follows:

"Mr. PRIVETT. Mr. Chairman, Members of the Committee on Ways and Means: My name is Howard J. Privett. I am a member of the law firm of McCutchen, Black, Verleger & Shea. I appear here on behalf of the James Irvine Foundation of California. It has been my privilege to have represented this foundation for the past 15 years."

Mr. Corman, a member of the Committee on Ways and Means, examined Mr. Privett as follows:

"Mr. CORMAN. Mr. Chairman, I would like to try to wend my way through all the factual differences expressed by the witnesses (referring to the testimony of several preceding witnesses).

"We are trying to figure out if people can comply with sections 4942 and 4943. We have had a lot of foundation representatives complaining they cannot comply and that we are going to destroy foundations if we make that effort.

"I take it the testimony is that they can comply?

"Mr. PRIVETT. We can.

"Mr. CORMAN. I know that some time in the days ahead we will have witnesses sitting where you are telling us this can not be done. I would like to make two observations. First of all, you are having to dispose of assets that are not commonly traded. The stock itself is not, as compared to some other foundations with stock being sold on the market.

"Further, as I understand it, you have to dispose of all but 2 percent of the assets because of the ownership of disqualifying members of the family.

You will end up holding no more than 2 percent of the Irvine stock of which you now hold 54 percent.

"Mr. PRIVETT. That is correct. We will not be one of the foundations in here in a few years telling you we cannot meet that requirement. We are making the plans and studies and seeking the advice of prestigious banking concerns, and we have every assurance we will be able to comply with the law.

"That is our charitable obligation and that is our obligation as citizens.

"Mr. CORMAN. That is in marked contrast to the Kellogg people who do not seem to have given any thought to it yet. Do you know enough about the plans (Irvine Foundation plans) to know what kind of assets the foundation anticipates investing in when it divests itself of the company stock (Irvine stock)?

"Mr. PRIVETT. My guess would be based on what they have done with other funds. They have not specifically acted yet to decide what they are going to do with the money they realize (from the sale of the Irvine stock).

"What they have done is to hire competent investment conusellors and what they did with other money they received from a 1963 partial liquidation of the Irvine Co. was to invest that in a broadly based diversified portfolio of stocks and bonds that is professionally managed.

"Mr. CORMAN. What kinds of return are they getting on the portfolio?

"Mr. PRIVETT. The rate currently is about 5.4 percent on the average.

"As I read section 4942, the applicable percentage each year is supposed to be adjusted by the Secretary of the Treasury to that percentage which bears the same ratio to interest and returns on money as 6 percent did in 1969.

"Now, I have great faith in the Secretary in applying that rule and if he does apply that rule, then we should not have a problem. I did check just recently on Treasury bonds, we hold some in our portfolio at 8 percent, they are only selling at about 6⅛ percent now, Treasury bonds are.

"I would assume the Secretary over the years will adjust the pay-out percentage rate up and down. If he changes it at the same rate as the market changes, we should be able to comply without a significant reduction in capital.

YORK, MAINE, *May 17, 1974.*

Mr. MICHAEL STERN,
Staff Director, Committee on Finance, Dirksen Office Building, Washington, D.C.

DEAR MR. STERN: I am writing as a member of the Society For The Preservation of Historic Landmarks of York County, Inc. Our activity as a Society is centered in the Town of York, Maine. Our population in the winter is approximately 5500 people and in the summer period it rises to 15,000 with the arrival of summer visitors and summer home owners. Many of these summer home owners are members of the Society. Our membership including family memberships is approximately 200.

The Society as its title denotes is dedicated to the preservation of our colonial and early 19th century buildings and the contents therein.

Some families in York recognize the importance of preserving their old homes and in fact some on their death, donated them to the Society for continual preservation as museums. I say museums in the sense that our buildings are original, not replicas and they contain furnishings of permanent interest to visitors. Our Society maintains these buildings and contents by dues received from members and from some invested funds left to the Society by a few individuals who understood the need to preserve these properties for future generations.

I know that our officers and Board of Governors are making every effort to accomplish this task. However, I am discouraged when I learn that our Society had to pay over $2,000.00 income tax for 1973. In fact, I understand that it has been necessary to hire a tax attorney to determine the Society's status as a foundation. This will cost $3,000.00.

The tax attorney requires copies of our tax returns; an appraisal of real estate and building contents; and a statement showing monthly cost and market values of investments for a two year period starting January 1, 1972.

These requirements will cost the Society over $2,800.00. Thus, for $5,800.00 the Society must prove to the Federal Government that it is a Foundation of some type. One of the Society's Trustees when he learned about the foregoing said "I am unfavorably impressed with the heavy burden of legal and paper work the Government is increasingly levying on the small enterprise."

We are a small enterprise and are continually pressed for funds to perpetuate a colonial atmosphere and environment for all citizens and foreigners who will visit York. A modest museum such as we are should be exempt from the 4% Excise Tax.

We look forward to favorable action by the Finance Committee that will recommend relief for the small foundation/museums.

Respectfully yours,

OWEN R. JONES.

STATEMENT BY RICHARD A. SHORT, PRESIDENT, THE AMERICAN ASSOCIATION OF HOMES FOR THE AGING

Mr. Chairman and members of the Committee, I am Richard A. Short, Administrator of the Presbyterian Home, Inc., High Point, North Carolina, and president of the American Association of Homes for the Aging. This is the organization consisting of over 1300 private, voluntary non-profit homes and facilities for the againg throughout the United States. The basic and overriding purpose of our non-profit facilities is to assume responsibility on a long-term basis for a comprehensive spectrum of continuing services to meet the needs of the elderly in our society, with a unique emphasis on the social components of care, i.e., taking care of the spiritual, psychological and social as well as the physical needs of the older person. This vast majority of our homes and facilities are church oriented and/or church sponsored.

In behalf of our member-institutions, I wish to express our support for S. 3460, a bill introduced May by Senator Peter Dominick. S. 3460 amends the Internal Revenue Code of 1954 in such a way as to remove certain homes for the againg from classification as private foundations.

All of the homes in our Association are dedicated to charitable purposes, must and do meet the requirements of the Internal Revenue Service (under its ruling 1972-124) which requires the furnishing of housing, health care and income maintenance at the lowest feasible cost in order to qualify as 501(c)3 tax-exempt entities. They do this primarily as part of the ministry of the Church and in furtherance of the concept enunciated by the Federal Government, under both Republician and Democratic administrations, which encourages the voluntary, private, non-profit sector of our society to actively meet the needs of the againg. Both the Congress and the Administration have consistenly advocated the building and operating of such facilities, through the National Housing Act, the tax exemption provisions of Section 501(c)3 of the Internal Revenue Code, amendments to the Social Security Act, and many other enactments.

We now find that for a number of our homes, from New York to California, Texas to Illinois, Massachusetts to Pennsylvania, this basic concept is seriously endangered by the Tax Reform Act of 1969, which now seems to classify them as "private foundations" or "private operating foundations." Tests have been set up under Section 509(a)2 which require that no more than one-third of the income be from investment sources in order to qualify as a "public charity." This creates a curious anomaly. Many homes which are usually our oldest, many formed over one hundred years ago, which have prudently managed their funds and have been the fortunate recipient of gifts and bequests, which are now more capable of taking care of the destitute elderly than any other facilities in the United States, are really the only ones receiving a "private foundation" classification. This is so, in spite of the fact that they meet all of the other tests of being non-profit, charitable and not for private benefit. Thus, they are subject to all the additional taxes and other penalties of the Act which then requires them to render *less* service to the public, take care of *fewer* destitute elderly, and set *higher* charges. The more "charitable" our homes are, in the sense of taking care of the poor out of the private dollar rather than by the use of tax funds, the more

subject they are to this "private foundation" status. These homes were not, and cannot be, in the business of giving grants; they were not and cannot be controlled by any one individual. They bear none of the characteristics of a "private foundation" except, unfortunately, the burdens.

We do not think this was ever the intent of the Congress when the tax reform act was passed. Our Association recognizes and concurs in the correction of abuses in the use of private foundations. But we think that placing our most charitable homes within the ambit of the Act was an oversight which seriously needs correction. We strongly urge your support and passage of S. 3460.

Mr. Chairman and members of this Committee, we think you for giving us this opportunity to submit a statement, and offer you our continued assistance.

STATEMENT OF THE SAND SPRINGS HOME, SAND SPRINGS, OKLA.

This statement is being submitted by the Sand Springs Home, Sand Springs, Oklahoma, to acquaint the Subcommittee with problems created by the Tax Reform Act for certain charitable organizations. Charitable organizations engaged in the long-term care of individuals are experiencing difficulty, as are certain charitable organizations controlled by Masonic and other organizations described in Sections 501(c)(8) or (10) of the Internal Revenue Code. These problems result from the classification of these organizations as private foundations.

DESCRIPTION OF THE SAND SPRINGS HOME

The Sand Springs Home was founded by the late Charles Page on June 2, 1908. On August 9, 1912, it was incorporated under the laws of the State of Oklahoma. At the time the Home was founded, there was no federal income tax could not be imposed until 1913, after the passage of the Sixteenth Amendment. The Home was orginally formed for the purpose of caring for orphans; however, in 1914, recognizing that there was a need for a facility which would provide a place for widows to raise their children, there was formed a Widow's Colony. These activities have continue until the present time. At the present time, the Home has 68 dependent children in residence and in the Widow's Colony, there are 28 widows with a total of 75 children.

The Sand Springs Home, since its formation, has expended in excess of twenty million dollars for charitable and philanthropic purposes and has cared for a total of 800 dependent children for whom the Home has provided all necessities of life, and more than twice this number of children and widows. Thus, there can be no doubt that it is carrying out its charitable purpose. The Home is unique since Mr. Page, recognizing the need for such organizations at an early date, provided the organization with an endowment which has resulted in its never having to request that the public make contributions to it. The Home has been able to operate without having to further burden the public with requests for funds. However, what would be considered a virtue is now a detriment since if the Home had requested additioned funds through the years from the public for its support, it would undoubtedly be able to qualify as a public foundation. However, leaving the funds of the community available to be used for other charitable activities, the Home now finds itself in the position of being classified as a private foundation.

Children are committed to the Home by the order of the Oklahoma State District Court, which charges the Home with the duty of the care, maintenance and education of the children. Widows and their children are admitted to the Widow's Colony under rules and regulations authorized by the Sand Springs Home, but the children remain under the jurisdiction of their mothers.

Personal assets of children are held in trust under guardianships established under the Probate Division of the District Court of Tulsa County, Oklahoma. Individual bonded guardians are appointed by the Court, and all personal assets, including Soulal Security, Veteran's assets, and all increments ac-

cruing thereto, to said child on reaching his or her majority. No personal funds of any child are ever accepted into or co-mingled with the accounts of the Sand Springs Home. The Home's Legal Department protects each child in effecting settlement of claims for death, insurance, Society Security and Veteran's benefits from which such guardianship assets customarily accrue.

The Home makes available to the Public School System of Sand Springs and to the various churches of Sand Springs and immediate area lands belonging to it, as long as such lands are occupied and used for educational or religious purposes, as the case may be.

The Home's assets consist, in addition to the land and buildings directly utilized for the carrying out of the exempt activities, of large tracts of land which are increasing in value, as Tulsa, Oklahoma expands, stock in several small but prosperous wholly-owned companies [e.g., the Sand Springs Railroad Company], oil properties, and investments in governmental obligations and certificates of deposit. It is difficult to assess the total value of the assets [this being one of the problems presented by the Tax Reform Act]; however, the total endowment is substantial and at a minimum this value exceeds twelve million dollars.

The trustees of the Home are appointed by the Oklahoma Grand Master of the fraternal society known as the Ancient Free and Accepted Masons, which is a Section 501(c)(8) organization.

The Home has paid in excess of $50,000 in taxes as required by Section 4940 of the Code. These funds have, of course, thus been diverted from charitable use and have not been available for use by the Home for the benefit of dependent children and widows and their children. It is submitted that the Home should not be forced to pay the tax but should be accorded the same treatment as colleges and hospitals receive.

The Home is also experiencing severe problems with respect to the minimum distribution requirement of Section 4942 of the Code. While Section 4942 is not a great problem to grant-making organizations which simply spend more in the form of grants to meet the distribution requirement, the Sand Springs Home and other such organizations which must meet obligations of long-term care, and have already invested considerable sums in the assets used to carry out their charitable purposes, are experiencing problems with the requirements of Section 4942. These organizations, with the ircontinuing obligations, must be careful that overspending now does not prevent them from meeting their continuing obligations to the residents of their facilities. However, not only ate the general distribution requirements of Section 4942 of the Code causing problems for this type organization, but they also have difficulty meeting the private operating foundation requirements of Section 4942. In order to qualify as a private operating foundation, an organization must normally expend directly for its operating purposes an amount equal to 85% of its adjusted net income and an amount equal to not less than two-thirds of its minimum investment return. It is the second requirement, known as the "endowment test", which provides problems for the Sand Springs Home and many similarly situated homes.

The Sand Springs Home must be in a position to hold assets which will appreciate in value to insure that it will be able to meet the continuing responsibility to the children and widows for whom it has accepted responsibility. This is, of course, even more important with the current inflationary trends. The Home must be in a position to invest for the future as well as for current income. Of course, some could argue that the Home could simply increase its expenditure per widow or child. However, there are of course limits to the providing of support, and the Home should not be forced to engage in wasteful, needless spending to meet an artificial requirement of the tax laws. Profligate spending will only serve to prevent the Home from meeting its long-term charitable responsibilities. Also, it should be remembered that the Home already has its substantial investment in facilities and it is not feasible continuously to simply rebuild the Home.

DISCUSSION OF THE PROBLEMS

When the Tax Reform Act of 1969 [P.L. 91–172] was enacted, two classes of charitable organizations were created—'private foundations' and 'other than private foundations.' Section 509 of the Code provides the definitional pro-

visions which govern which organizations are to be treated in one of the two respective classifications.

Prior to the Tax Reform Act of 1969, and before the substantial restrictions imposed on private foundations, there had been differences between charitable organizations but these differences involved Section 170 of the Internal Revenue Code which provided for differing limitations on the amount of deduction available to individuals who made contributions to charitable organizations.

Prior to the Tax Reform Act, there were charities that were 20% charities and 30% charities. Contributors to organizations classified as 30% charities under Section 170(b)(1)(A) of the Internal Revenue Code, as it provided prior to 1969, were permitted a greater maximum deduction for their contributions than was available for those contributors to arganizations classified as 20% charities.

With the changes in the law in 1969, the former provision with respect to charitable contribution deductions was picked up and placed into the definitional provision—Section 509—which distinguished between private and other than private foundations. Thus an organization which could qualify as what was than a 30%—now a 50%—charity because of other changes in the law—would qualify as other than a private foundation. This is provided under Section 509(a)(1) of the Code. Organizations covered by this provision are colleges, universities, hospitals, and publicly supported organizations such as the Red Cross, United Fund, Boy Scouts, and other such broadly based publicly supported organizations.

Because of definitional problems that existed under Section 170(b)(1)(A) certain organizations, even though they had broad-based public support, could not be classified as Section 170(b)(1)(A)(6) organizations because they received support in the form of membership dues rather than contributions. Into this category fell educational and scientific societies which received dues income. With respect to these organizations, since they were broadly publicly supported, there was provided in Section 509(a)(2) a means by which they could qualify as other than private foundations.

In general with respect to organizations classified under Section 509(a)(1) and 509(a)(2), there was a requirement that the organization receive more than one-third of its support from the general public, or in the case of Section 509,a)(1), be among other types of organiations listed in Section 170(b)(1)(A). With respect to 509(a)(2), there was a limitation upon the amount of investment income which could be received.

In addition, there was provided another mechanism by which organiflations could qualify as other than private foundations. Under this method the organization was required to demonstrate that it was controlled, supervised or operated in connection with an organization described in Section 509(a)(1) or (2) and that it operated exclusively for the benefit of, to perform the functions of, or to carry out the purposes of a Section 509(a)(1) or (2) organization. Thus if there were an organization which was formed and controlled by a public organization—the trustees were appointed by the organization and it operated to perform the function of, to support or carry out the purposes of such organization—the organization qualified as a publicly supported organization—the organization qualified as a publicly supported organization. This was provided by Section 509(a)(3).

Still another means by which an organization could qualify as other than a private foundation was provided in the last sentence of Section 509, where it was provided that certain organizations could achieve other than private foundation status if they were controlled by organizations exempt under other specified provisions in the Internal Revenue Code. These organizations qualify for other than private foundation status even though the parent organizations are not charitable. This status was provided for organizations which were controlled by organizations such as the National Association for the Advancement of Colored People [Social Welfare, Section 501(c)(4)], Teamsters Union [Labor Union, Section 501(c)(5)], and U.S. Chamber of Commerce [Trade and Professional Groups, Section 501(c)(6) of the Internal Revenue Code].

The benefits of receiving classification under any of these sections of the Code, which will permit the organization to qualify as other than a private

foundation, are that the organization by being so classified escapes the requirements imposed on private foundations. Thus such organizations are not subject to taxes on investment income, nor are they subject to certain distribution requirements. The exclusion from other than private foundation status of the above referenced types of organizations was premised upon the conclusion that, given the nature of the organizations, they would not stray from the accepted paths of charitable organizations because of public scrutiny.

It was provided in Section 4942, which relates to the distribution requirements, that special status was to be given to certain private operating foundations. These are organizations that, while they cannot qualify as public foundations, engage in the *operation* of charitable activities. Mechanical tests were provided by which they could escape the requirements on distribution if they could establish that they met certain mathematical tests which were provided in Section 4942(j)(3).

There are certain organizations which are comparable to schools and universities [Section 509(a)(1) organizations] which are classified as private foundations under Section 509. These organizations are orphanages. Further these organizations, because of their support having come from a relatively few individuals, may not escape being classified as a private foundation by meeting the public support tests of Section 509(a)(1) or 509(a)(2).

In particular, this memorandum will deal with the Sand Springs Home, which is located in Sand Springs, Oklahoma. It is an orphanage which, because of its peculiar circumstances and as a result of the Tax Reform Act of 1969, is not classified as other than a private foundation or as an operating foundation.

SOLUTIONS TO THE PROBLEMS

There are two bills pending in the House [one of which has been introduced in the Senate] which would serve to eliminate the problems of the Sand Springs Home. The two bills were introduced to cure separate but widespread problems of certain charitable organizations. Uniquely, the Sand Springs Home is covered by the provisions of both of these bills.

H.R. 2258 will permit organizations which are controlled by organizations which are exempt under Sections 501(c)(8) and (10) [Masonic or fraternal orders] to qualify as other than private foundations. This legislation would cover the Sand Springs Home.

H.R. 14467 [the successor bill to H.R. 2259] which carries the Senate number S. 3460, will permit organizations which provide for the long-term care of orphans, widows or the aged to be relieved of tax imposed by Section 4940 and the distribution requirements of Section 4942. In order to qualify for such treatment, an organizations must spend an amount equal to 3% of its net investment assets each year.

Notwithstanding the fact that either of these bills would cure the problems created for the Sand Springs Home, the Home urges that the Subcommittee recommend the enactment of both bills, since they make separate and necessary changes in the laws to permit deserving organizations to carry out their charitable purposes.

H.R. 2258

As was indicated above, the Trustees of the Sand Springs Home are appointed by the Grand Master of Masons in Oklahoma. If this Masonic organization were classified as a Section 501(c)(4), (5) or (6) organization, rather than a Section 501(c)(8) organization, the Home would qualify as other than a private foundation. This classification would follow since the trustees are appointed by the Masonic Order through its presiding officer and the Home carries out a type of activity which is closely identified with charitable Masonic activities.

However, as indicated, the Masons are not a Section 501(c)(3) or a Section 501(c)(4), a Section 501(c)(5) or a Section 501(c)(6) organization. Thus even though an organization which is responsive to the public and which has broad public support has jurisdiction and control of Sand Springs Home by virtue of its power of appointment of trustees, the Home may not qualify as other than a private foundation. Organizations controlled by Masonic and similar organizations exempt under Section 501(c)(8) and under Section 501(c)(10) of the Interal Revenue Code should be extended the same treatment as organizations exempt under Section 501(c)(4), (5) or (6).

In a general explanation of the Tax Reform Act of 1969, which was prepared by the staff of the Joint Committee on Internal Revenue Taxation, the following is stated on Page 58, footnote 27: "Under the Act, an organization can also escape private foundation status by qualifying under the third category as an "affiliate" of one or more organizations described in Sections 501(c)(4) [social welfare organizations], 501(c)(5) [labor unions and granges], and 501(c)(6) [chambers of commerce and trade associations]. In such a case, the Section 501(c)(4), (5) or (6) organization must itself be broadly, publicly supported to such an extent that if it were exempt under Section 501(c)(3), it would meet the standards of the second category described in the text."

Thus, as is apparent, what Congress was seeking at that time was to provide that organizations controlled by broadly publicly supported organizations, even though not charitable organizations, be treated as other than private foundations. Certainly Masonic groups, exempt under Sections 501(c)(8) or 501(c)(10) meet this requirement. In particular, the Senate report on H.R. 1327 at page 59 stated: "(e). The Committee provided that a foundation which is run in conjunction with an organization exempt under paragraphs (4), (5) or (6) of Section 501(c) [such as a social welfare organization, labor union or agricultural organization, business league, real estate board, etc.] which is publicly supported is to be treated as meeting the public support test for purposes of being a public charity rather than a private foundation. This is an addition to present law [under which an organization is treated as being publicly supported to the extent that its support is received as grants or contributions for an organization that is publicly supported]."

From these glimpses of the Congressional intent for the enactment of the last sentence of Section 509(a)(3), it is clear that Congress was seeking that a public foundation status be conferred based upon a relationship with a public organization. It is unfortunate that it overlooked the Masonic orders during this legislation, but as can be seen from the language with respect to the organizations that were included there is no good reason for the organizations not being provided such treatment. There has been introduced H.R. 2258, which would amend the last sentence of Section 501(a) to provide as follows: "For purposes of paragraph (3), an organization described in paragraph (2) shall be deemed to include an organization described in Section 501(c)(4), (5) or (6) or an organization incorporated before June 1, 1939 and described in Section 501(c)(8) or (10) which would be described in paragraph (2) if it were an organization described in Section 501(c)(3)."

The new language refers to Sections 501(c)(8) and 501(c)(10). The importance of this to the Sand Springs Home is that since its trustees are appointed by the Grand Master of Masons in Oklahoma, which is exempt under Section 501(c)(8) and which could meet the requirement of Section 509(a)(2) if they were exempt under Section 501(c)(3), the Home, if H.R. 2258 is enacted, will be other than a private foundation. It is submitted that the grandfather features of the bill should be eliminated since regardless of when formed, an organization controlled by an organization controlled by an organization described in Section 501(c)(8) or (10) should be treated as other than a private foundation.

During the passage of the Tax Reform Act of 1969, there was considerable attention directed by the American Bar Foundation, the American Society of Association Executives, labor unions and the Chamber of Commerce of the United States to foundations which received most of their support from or were controlled by labor unions or business or professional associations [such as the American Bar Association] and that would have otherwise been classified as private foundations under the initial proposed definition of private foundations. The House version was amended accordingly by the Senate an dthis was finally adopted as a part of the Internal Revenue Code to provide that organizations that were controlled or operated in connection with designated organizations would not be classified as private foundations. If it were not for the last paragraph of Section 509(a), a foundation which received all of its funds from the International Ladies Garment Workers Union, or the trustees of which were appointed by the Chamber of Commerce of the U.S., for instance, would be classified as a private foundation.

It is this paragraph of Section 509(a)(3) that is proposed to be amended. The purpose of this proposed amendment is to provide that the same treatment shall be extended to organizations controlled by organizations described in Sections 501(c)(8) and 501(c)(10). There is no reason for organizations, the governing bodies of which are appointed by the Masons, and other similar organizations such as Knights of Columbus, not to be extended the same treatment as organizations, the governing bodies of which are appointed by unions or trade associations, since the control is in a "public" organization. In the case of the Sand Springs Home, whose trustees are appointed by the Grand Master of Oklahoma Masons, it is clear that the control is in a public organization.

It is submitted that H.R. 2258 should be enacted since undoubtedly it was only because of oversight that this provision was not placed in the Internal Revenue Code in 1969 at the time similar language was added providing such treatment for organizations controlled by trade associations and labor unions.

S. 3460 and H.R. 14467

S. 3460 (H.R. 14467) should be enacted. It provides that organizations such as the Sand Springs Home formed before October 31, 1969, which expend an amount equal to 3% of the net fair market value of their assets as defined in Section 4942(e)(1)(A) would not be subject to the tax imposed by Section 4940 or the distribution requirement of Section 4942. S. 3460 was introduced in the Senate by Senator Dominick and H.R. 14467 was introduced in the House by Congressmen Brotzman, Armstrong, Burleson and Conable. It is submitted that this legislation should be enacted. The fact that the Home's endowment has come from one ndividual should not prevent its being classified as other than a private foundation since there are other sections of the Internal Revenue Code which permit organizations to be classified as other than private foundations even though the endowment has been supplied by a limited number of persons. Examples of this are medical research organizations as well as universities and schools which are classified under Section 170(b)(1)(A)(ii) and (iii) of the Internal Revenue Code and by virtue of Section 509(a)(1) as public organizations. Therefore, there is ample precedent for the treatment requested.

Many organizations are exempt from private status due to the function which they serve. Churches, schools, hospitals, and units of government are types of organizations which are treated as other than private foundations because of the function they perform or the benefits they confer on society. Certainly organizations which operate facilities for the long-term care of children, widows and elderly persons should be accorded the same status as these organizations.

Another factor should also be considered. There are numerous other homes for children and the elderly in the United States which are operated and/or sponsored by churches, fraternal organizations and labor unions. These organizations already are relieved of the private foundation requirements. It is submitted that the Sand Springs Home and other organizations which have been privately endowed and which care for children and the elderly should not be treated differently and should be relieved of the requirements imposed on private foundations, including the 4% annual excise tax on net investment income imposed by Section 4940 of the Code.

S. 3460 amends Section 4942 to exempt organizations which operate and maintain as their principal purpose or function facilities for the long-term care, comfort, maintenance or education of resident permanently and totally disabled persons, elderly persons, needy widows and children, and which expend annually for such purposes an amount equal to not less than 3% of the value of their investment assets.

S. 3460 seeks to afford to organizations which operate facilities for the long-term care of the elderly and children a status similar to that now accorded to hospitals and medical research organizations, except for the added requirement that annual expenditures for operation of the facilities must equal or exceed an amount equal to 3% of endowment. If enacted, S. 3460 will exempt such organizations from the 4% annual excise tax on net investment income and permit the funds otherwise payable as taxes to be devoted

to care of residents. The bill would also eliminate the uncertainties associated with qualification of such organizations as operating foundations under Section 4942 of the Code. Attached as an exhibit is a letter from the Treasury commenting on H.R. 2259. S. 3460 is the successor to H.R. 2259 and answers the Treasury objections.

SUMMARY

For the reasons stated above, it is respectfully requested that the Subcommittee make a favorable recommendation with respect to both H.R. 2258 and S. 3460.

DEPARTMENT OF THE TREASURY,
Washington, D.C., Dec. 10, 1973.

Hon. WILBUR D. MILLS,
Chairman, Committee on Ways and Means, House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This in response to your request for the views of the Treasury Department on H.R. 2258 "A BILL to amend the Internal Revenue Code of 1954 to exempt certain organizations from private foundation status."

The private foundation provisions apply only to organizations which are exempt from Federal income tax under section 501(c)(3) of the Internal Revenue Code—that is; exempt organizations to which tax deductible contributions may be made. UUnder section 509(a), a section 501(c)(3) organization is a private foundation unless it falls within a specific exception. The first excepted group includes certain categories of charities that have been accorded a preferred status under the income tax provisions, in that charitable deductions for contributions to such organizations are subject to a 50 percent, rather than a 30 percent, limitation. Also excepted are certain charities that receive broad-based public support. A third exception applies to charities which are organized and operated to assist one or more of the organizations falling within either of the first two exceptions in carrying out their charitable functions, and which are "operated, supervised, or controlled by or in connection with" such other organization(s). The justification for this third exception is, of course, that the relationship between the "parent" and the "support" organization ensures that the support organization will be as responsive to the public interest as the parent organization itself.

Many support organizations that are exempt from tax under section 501(c)(3) are affiliated with a parent organization that is exempt from tax under some other provision. In cases where the parent organization, were it a section 501(c)(3) organization, would qualify under the second exception described above, it would appear appropriate to accord the support organization an exclusion from private foundation status. Section 509(a) presently provides such an exclusion for support organizations affiliated with sections 501(c)(4) organizations (civic leagues and employee associations), section 501(c)(5) organizations (labor, agricultural, or horticultural organizations), and section 501(c)(6) organizations (various business leagues). H.R. 2258 would extend this exception to support organizations affiliated with section 501(c)(8) and (10) organizations (fraternal beneficiary societies, orders, or associations).

The Treasury Department supports the enactment of H.R. 2258. Affiliation with a fraternal beneficiary society, order or association ensures indirect public scrutiny of the activities of the affiliated organization through the supervision of the parent organization.

However, we would suggest that the restriction of the amendment's applicability to charitable organizations supporting the charitable activities of such parent organizations incorporated prior to June 1, 1939, be deleted. The basic proposal is fair and sound. But, the limitation causes the proposal to look like special interest legislation to allow the continuation of a questionable practice (which is not the case).

If enacted, H.R. 2258 would result in an estimated revenue loss of less than $5 million, regardless of whether the reference to incorporations prior to June 1, 1939, is deleted.

The Office of Management and Budget has advised the Treasury Department that there is no objection from the standpoint of the Administration's program to the presentation of this report.

Sincerely yours,

FREDERICK W. HICKMAN,
Assistant Secretary.

FREEDOM OF INFORMATION REVIEW

The Freedom of Information Review includes the material from three sources: The Treasury Department file of formal reports on legislation, the correspondence received and sent by the Office of the Assistant Secretary of the Treasury for Tax Policy, the Freedom of Information Reading Room of the Internal Revenue Service. All bill reports plus selected items from the other sources will be summarized in Tax Notes

BILL REPORTS

Old age home contributions.

The Treasury Department gave qualified approval to a bill (H.R. 2259), sponsored by Ways and Means member Donald G. Brotzman, R-Colo., which would make charitable contributions to old age homes deductible up to 50% of the donor's contribution base compared with the current 20%. Moreover, it would exempt most old age homes from all the private foundation provisions of the Tax Reform Act of 1969. Treasury said it did not approve of the increase in the contribution limit nor in the exemption from several of the restrictions imposed by the 1969 act. It also said the revenue loss from the bill would not exceed $5 million a year.

Treasury noted that the private foundation provisions most pertienent to long-term care facilities are:

The requirement in Section 4942 of the Internal Revenue Code that a private foundation distribute or expend a specified percentage of its investment assets or its entire adjusted net income, whichever is greater.

The 4% tax on private foundation net investment income imposed by Section 4940.

Because many foundations must rely on their endowments to meet their long-term care commitments, Treasury said, too great a distribution requirement plus the 4% tax can seriously inhibit the organization's ability to fulfill its long-term care commitments.

Treasury is sympathetic to the "special needs" of the long-term care organizations, the report said, and agrees that it would be well to stabilize the long-term investment return and distribution requirements at a conservative, constant level, such as the 3% set by the bill. Treasury also has favored reduction or elimination of the 4% tax on net investment income, the report continued.

However, Treasury continued, there is no need to limit, as the bill does, the proposed changes to those organizations in existence on May 26, 1969. More important, there are four other private foundation restrictions which should be maintained, Treasury said. These are:

The tax imposed by Section 4941 on acts of self-dealing, such as sales between the organization and related persons;

The tax imposed by Section 4943 on excess business holdings;

The tax imposed by Section 4944 on the making of investments which jeopardize the charitable purpose of the organization; and

The tax imposed by Section 4945 on the making of certain taxable expenditures, such as payments for carrying on prapaganda or attempting to influence an election.

The bill was included by Brotzman in the list of miscellaneous bills scheduled to be taken up soon by the Ways and Means Committee (See Tax Notes, January 7, pages 8 and 8.)

STATEMENT OF GERALD A. DESMOND, SECRETARY, KOHLER FOUNDATION, INC., KOHLER, WIS.

This statement is being submitted on behalf of Kohler Foundation, Inc., Kohler, Wisconsin.

Mr. Chairman and members of the Senate's Subcommittee on Foundations, we appreciate the opportunity to submit this written statement to the Subcommittee on Foundations.

Kohler Foundation, Inc. is a Wisconsin non-stock, nonprofit corporation, organized in 1940 under the laws of the State of Wisconsin, and has been classified as a private foundation under Section 509(a) of the Internal Revenue Code. All of the substantial contributors, as defined under the Tax Reform Act of 1969, are deceased, as are all of the incorporators. It is a relatively small private foundation with total fair market value of assets of $7,731,659.91 as reported on Form 990-PF to the Internal Revenue Service for the year 1973.

Kohler Foundation, Inc. makes direct expenditures for cultural programs, scholarship awards, and for the operation and maintenance of a historic home called "Waelderhaus." In addition, contributions are made to organizations conducting educational, historical, cultural, religious or charitable activities. Kohler Foundation, Inc. was responsible for initiating and then participating in the development of an Arts Center in Sheboygan, Wisconsin, and Wade House State Park in Greenbush, Wisconsin.

As you indicated in a prior press release, Mr. Chairman, the hearings were to be conducted specifically in connection with the administration of the laws pertaining to private foundations by the Internal Revenue Service and the way in which the Tax Reform Act of 1969 and its implementation has affected the ability of foundations to serve grantees.

I attended the hearings on May 13 and 14, 1974, and would like to address myself initially to the testimony of some of the witnesses who question the propriety of exempting private foundations from paying income tax because most of the foundation programs are not serving the real needs of the general public. They contend, inferentially at least, that Government can and should take care of the programs fostered by private foundations. We submit, Mr. Chairman and members of the Committee, that the greater number of private foundations in this country today are serving the needs of the general public in the charities they support. We submit also that were it not for the huge sums of money contributed by private foundations as a whole, many worthwhile and absolutely necessary services could not be performed to help the unfortunate. Neither the State nor the Federal Government would be able to respond to all the pleas from those in need. The fact that there exists today in this country, the richest in the world, such abject poverty, is eloquent evidence that Government cannot take care of the basic needs of the entire society.

I need not remind you gentlemen that this country was founded upon the principle of independence and freedom of choice. Once we attack the concept of freedom of choice we ride headlong into a more sturctured state. We submit that freedom of choice is attacked when our citizens are told that they cannot exercise their independence by choosing the charity they desire and that Government will perform the function of funding all charitable endeavors.

With respect to the specific provisions of the Taffi Reform Act of 1969, I respectfully request your Committee to consider the reduction of the 4% excise tax on net investment income to an appropriate amount sufficient to provide the funds necessary for the Internal Revenue Service to perform its audit functions required by the Act. The 4% excise tax was levied to provide funds for this purpose. As stated by Honorable Dewey F. Bartlett, United States Senator from Oklahoma, in his testimony before the Subcommittee on May 14, 1974, "experience has shown that this figure produces revenue which is far in excess of what the Treasury needs to audit the activities of *all* exempt organizations, let alone what it needs to audit just private foundations." There are some that suggest that the excess amount be turned over to the State Governments so that they can police private foundations. We submit, gentlemen, that this action would merely be unnecessarily creating more Government jobs and would have the effect of spending money

for the sake of spending. Such action is wasteful, and is needlessly spending money that otherwise would be used to support charitable projects. In this sense grantees are adversely affected by this provision of the Act.

Your attention is directed, gentlemen, to another provision of the Tax Reform Act of 1969 which has affected the ability of private foundations to serve grantees.

Section 4942(d) of the Internal Revenue Code, in defining the term "distributable amount," provides that it is an amount equal to the minimum investment return or the adjusted net income (whichever is higher) reduced by the amount of taxes imposed under Subtitle A and Section 4940.

"Minimum investment return" is defined under Subsection (e) as the amount determined by multiplying the fair market value of the assets by 6% or by the percentage determined by the Secretary. 5.5% was the percentage fixed by the Secretary for the year 1974.

It is respectfully submitted that this provision places an unreasonable burden on foundation managers by requiring them to obtain a minimum return on these investments each year, regardless of the economic conditions prevailing in the country. This is not always possible to achieve, even by security analysts and investment bankers, not to mention the less financially erudite foundation managers. Consider the dividend yields of the 30 companies which make up the Dow Jones average as listed below. Note that this data was accumulated at a time of relatively low price and high yield.

DIVIDEND YIELD OF CORPORATIONS INCLUDED IN DOW JONES AVERAGES

	1973 yearly dividend	Market price as of Dec. 31, 1973	Percent yield
1. Allied Chemical	1.32	49	2.7
2. Alcoa Aluminum	1.34	48⅛	2.8
3. American Brands	2.38	32⅛	7.4
4. American Can	2.20	26¼	8.4
5. American Telephone & Telegraph	3.08	50⅛	6.1
6. Anaconda	.50	26⅛	1.9
7. Bethlehem Steel	1.80	33	5.5
8. Chrysler	1.40	15⅝	9.0
9. Du Pont	5.75	159	3.6
10. Eastman Kodak	1.91	116	1.6
11. Esmark	1.00	24⅞	4.0
12. Exxon	5.00	94⅛	5.3
13. General Electric	1.60	63	2.5
14. General Foods	1.40	23⅝	5.9
15. General Motors	5.25	46⅛	11.4
16. Goodyear	1.00	15⅛	6.6
17. International Harvester	1.60	25⅝	6.2
18. International Nickel	1.35	35¼	3.8
19. International Paper	1.75	52	3.4
20. Johns Manville	1.20	16⅜	7.3
21. Owens-Illinois	1.48	30⅛	4.8
22. Procter & Gamble	1.80	92	2.0
23. Sears Roebuck	1.85	80¼	2.3
24. Standard Oil of California	1.70	35	4.9
25. Texaco	1.76	29⅜	6.0
26. Union Carbide	2.10	34⅛	6.2
27. United Aircraft	1.80	23⅝	7.6
28. U.S. Steel	1.60	37⅛	4.3
29. Westinghouse Electric	.972	25⅝	3.8
30. Woolworth	1.20	18⅜	6.5
Average			5.026

Note.—14 or 46.6 percent, 5.5 or over.

It is to be noted that the average yield of all these companies was only 5.026%, and only 14 had yields of 5.5% or more. If any investment banker or securities analyst had the perspicacity to be able to choose the best 14 performing companies beforehand, he would be considered clairvoyant. We submit, gentlemen, that this is not possible for the experts and certainly not for the foundation managers. Your attention is directed to the inescapable conclusion that under these circumstances foundations are faced with the ultimate depletion of their assets if they are forced to make annual distributions on the basis now required under the Code.

The purposes and objectives of this section of the Act were to prevent private foundations from unduly accumulating their income, thus depriving charitable organizations of receiving aid on a timely basis. The purposes of this section can be accomplished by requiring private foundations to distribute 100% of their actual net income, thereby eliminating the distinct possibility of the assets of foundations being entirely depleted over the years because of having to liquidate them to make the annual mandatory distribution.

Finally, gentlemen, I submit that the high administrative, legal and accounting costs that private foundations must bear to insure compliance with the Tax Reform Act of 1969 and regulations issued thereunder have had an adverse effect upon small private foundations and consequently upon charitable institutions. All of these expenses have increased substantially for our foundation since the Tax Reform Act of 1969 became effective, as they undoubtedly have for other small private foundations. This has resulted in a reduction of the amount of money available for distribution. While I have no specific recommendation to make in this regard, except perhaps that different standards be applied under the Act for smaller private foundations, I suggest that your Subcommittee consider ways of alleviating the burdens placed upon the small private foundation with assets of less than $10,000,000.

Thank you for providing the opportunity to present our views.

ARNOLD & PORTER,
Washington, D.C., May 24, 1974.

HON. VANCE HARTKE,
Chairman, Subcommittee on Foundations of the Committee on Finance, U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: Our law firm represents a number of private foundations concerned with the existing transitional rules for the disposition of excess holdings. The enclosed statement reflects what we consider to be a serious problem existing in connection with the administration by the Internal Revenue Service of the Tax Reform Act of 1969 as it pertains to private foundations. We welcome the opportunity to submit this statement and would be quite willing to meet with members of your staff with regard to this problem.

Over the past four years we have conferred with the Treasury and Internal Revenue Service in an effort to demonstrate to them that the problems can be solved administratively. To date, neither the Treasury nor IRS has concurred with our suggestions or has suggested any procedure for dealing with a most serious problem. Consequently, if the transition problem cannot be solved administratively, it is clear that amendatory legislation has to be enacted. To that end, your Subcommittee is to be commended for its willingness to hold public hearings on this subject.

Sincerely,

MITCHELL ROGOVIN.

STATEMENT OF MITCHELL ROGOVIN, ATTORNEY, ARNOLD & PORTER, WASHINGTON, D.C.

HEARINGS ON PROBLEMS WHICH MAY EXIST IN CONNECTION WITH THE ADMINISTRATION OF THE TAX LAWS PERTAINING TO PRIVATE FOUNDATIONS BY THE INTERNAL REVENUE SERVICE

Introduction

Section 4943 of the Code, introduced into the law by the Tax Reform Act of 9169, requires divestitures, within certain time limits, of a private foundation's excess business holdings. Briefly stated, excess business holdings exist whenever a foundation and/or its trustees and officers and/or persons who have contributed to the foundation or any combination of the foregoing own 20% (in some cases 35%) of the stock of a business. The Congress recognized that in many instances the existing excess holdings then held by private foundations consisted of stock in closely held corporations whose stock was owned by so-called "disqualified persons" (that is, people who had made contributions or who were trustees or officers or who were otherwise closely related

to the foundation), for which stock there was little if any market outside the disqualified persons group. Accordingly, to afford foundations a means for complying with the divestiture requirements with respect to existing holdings, Congress provided a transitional rule, in section 101(1)(2)(b) of the Tax Reform Act, to the effect that the provisions of section 4941 of the Code (which in general prohibit any transaction between a foundation and related people, generally called, self dealing transactions) would not apply to a foundation's sale to its disqualified persons of the excess business holdings owned (or treated as being owned) by the foundation on May 26, 1969, if the sale price received by the foundation equalled or exceeded the fair market value of the property at the time of disposition.

Problem in implementation of the transitional rule

Many foundations that held substantial blocks of closely held stocks on May 26, 1969, or would be acquiring substantial blocks of such stock in the future under wills and irrevocable trusts executed prior to that date, looked to redemptions by the issuing corporation (a disqualified person) pursuant to this transitional rule as the only feasible way in which they would be able to comply with the divestiture provisions and raise moneys for their charitable activities. Without the transitional rule, such redemptions would have been prohibited as acts of self dealing. However, the present policy of the Treasury Department and the Internal Revenue Service in their implementation of the transitional rule makes it virtually impossible for a private foundation to dispose of its closely held stock through such redemptions without incurring excessive risks.

In order for such a redemption to come within the scope of the transitional rule, the corporate disqualified person must pay the foundation an amount at least equal to the fair market value of the stock being redeemed. This is an appropriate requirement, but without more it is almost impossible to deal with. Where the stock being redeemed is closely-held stock in which there is no trading or sales between unrelated parties, there is great difficulty in ascertaining fair market value. Even though a foundation may retain independent appraisers for the purpose of valuing the closely held stock to be redeemed, all history in this area of valuation teaches that in many instances the valuations of the independent appraisers may differ from each other and from the fair market value claimed by the Service and all of these may differ from the fair market value as finally determined by a court.[1]

Neither the transitional rule itself, nor the regulations, provide foundations with any guidelines for achieving the requisite fair market value. The Internal Revenue Service is not willing to change its prior practice of not giving advance rulings on fair market value questions and has been unwilling to agree to or propose any procedure for determining fair market value.[2] Yet, if the price paid by the redeeming corporation should differ from the finally determined fair market value, then the redemption transaction becomes an act of self dealing and a penalty excise tax is imposed on the foundation managers and the redeeming corporation. As a result, foundation managers must act at their peril if they dispose of existing excess holdings by redemptions made pursuant to the transitional rule. In effect, the managers are being held to a requirement of strict accountability in fixing the value of closely held stock for which there is no market and no arms length transactions because (i) no procedures are provided for determining fair market value and (ii) no provision is made for settling good faith differences in opinion of fair market value in cases where there is reasonable cause and where the foundation had employed independent appraisals in determining value.

In sum, foundation managers face the prospect not only of becoming liable for what may be a substantial penalty tax, but, more importantly, with

[1] The courts have recognized that the determination of the fair market value of stock representing a minority interest is a closely held corporation presents an extremely difficult and elusive question of fact. See, *e.g.*, *Morris M. Messing*, 48 T.C. 502 (1967); *Estate of Lucretia Eddy Cotchett*, 33 T.C.M. No. 31 (1974).

[2] Indeed, any program of advance ruling on the question of fair market value by the Service would likely be costly for the government time consuming and equally provocative.

the stigma of being considered manipulators of charitable funds. If a foundation manager or a disqualified person commits an act of self dealing because of a difference in opinion between the foundation's independent appraisers and the Service in connection with the value of stock redeemed under the transitional rule, his being an admitted self dealer may subsequently be used to impeach or discredit him, in some later civil proceeding between him and other private parties, completely unrelated to the governmental regulation of foundations. The determination that a fiduciary is a "self dealer" is not to be made lightly. In the case of the redeeming corporation, the prospect of inadvertently committing an act of self dealing may compel the directors, as prudent businessmen, to refuse to redeem any of the foundation's excess holdings because of the incalculable risks involved; *i.e.*, not only the possibility of a penalty tax, but also the possibility of subsequent minority shareholder suits.

Initially, the Internal Revenue Service took the position that in redemptions made pursuant to the transitional rule, if the redemption price were less than finally determined fair market value, the entire redemption transaction would become an act of self dealing and the self dealing and the self dealing tax imposed by section 4941 would be imposed on the entire amount involved in the transaction. The Service subsequently modified this position. Regulation §53.4941(e)-1(b)(2)(iii) provides that only the differential between the price paid and the finally determined fair market value is to be treated as the amount involved in the self dealing transaction upon which the penalty tax will be imposed, provided that: a good faith effort had been made to determine fair market value; the appraiser who made the valuation was not a disqualified person, was competent and was not in a position to benefit from the value utilized; and the method used in the valuation was a generally accepted method for valuing comparable property. But this approach only represents a difference in degree. Neither the penalty tax nor the amount of money that must be paid to correct the valuation variation is the real problem. The overriding concern of foundation managers and redeeming corporations is the onus of becoming self dealers even though best efforts were applied in reaching a valuation price.

Administrative solution

For the past several years, we have been trying to work out, with the Treasury Department and the Internal Revenue Service, an administrative solution to the fair market value problem. Our efforts have not been successful, principally because, in the view of the Service, there is no statutory basis on which to make a distinction between a willful, erroneous valuation and a good faith difference of opinion. The Service basically takes the position that the Congress intended that a good faith difference in opinion would have the same effect as a willful error.

We had originally proposed that where closely held excess holdings are redeemed pursuant to the transitional rule, if there was an ultimate determination by a court or an agreement with the Service that the fair market value of the stock at the time of the transaction was in excess of the redemption price originally paid, the transaction would continue to be within the purview of the transitional rule and would not become an act of self dealing if there had been a good faith effort to ascertain fair market value and the redeeming corporation had, by contract, bound itself to pay the foundation the difference between the original redemption price and the finally determined fair market value, plus interest. The Service feared that this proposal may have the effect of depriving the Service of standing to litigate. We then amended our proposal, to limit its scope to instances where the controversy on value is settled at the administrative level. We suggested as an alternative approach, giving the taxpayer the right of electing binding arbitration. Under both the alternatives contained in our amended proposal, the redemption transaction would not be case as an act of self dealing so long as the foundation had acted reasonably in estimating value and the redeeming corporation was bound to pay the foundation any differential in the value, plus interest. Our amended proposal has been rejected.

In the view of the Service, the self dealing provisions of section 4941 make no allowance for any difference in opinion in determining fair market value,

whereas such a provision is made with respect to determining fair market value for purposes of other provisions of the Tax Reform Act. Section 4942 and the regulations issued thereunder require foundations to make qualifying distribution each year of the greater of actual net income or an amount based on a percentage of the fair market value of the foundations' investment assets. Section 4942 provides that the determination of fair market value for such purposes is to be made pursuant to guidelines set forth by the Commissioner and further provides that if a foundation fails to distribute the correct amount of income as a result of an error in valuing its investment assets, no penalty will attach so long as the failure was not willful, was due to reasonable cause and is corrected within a specified time period after there has been a final court decision or a final agreement as to a different value. Because similar language does not appear in either section 4941 of the Code or section 101(1)(2)(b) of the Act, the Treasury Department and the Internal Revenue Service have concluded that the Congress intended no room for differences in opinion in fair market value determinations made in connection with dispositions of existing excess holdings pursuant to the transitional rule of section 101(1)(2)(b) and that regardless of the non-willful nature of the difference in opinion and regardless of how extensive the reasonable cause, nevertheless, if a foundation, in such a transaction, receives anything less than what the courts may, after the fact, ultimately determine to be fair market value, an act of self dealing has been committed. It is very doubtful that Congress had any such punitive intent in the relief provisions of the 1969 Act, which were enacted in recognition of the fact that the 1969 Act was a complete change in the law under which foundations had operated for generations, or any intent that the parties to a redemption have to be the insurer of an obvious impossibility, namely, that no one would ever come up with a different value. The Congressional purpose was not to punish foundations, but permit them to adjust to the new rules.

Legislative solution

Accordingly, after years of discussion, we are persuaded that the only solution of the fair market value problem is by statutory amendment if foundations are going to be able to carry out the Congressional purpose of divesting themselves of excess business holdings, without risks to their managers and constant uncertainty. The problem can easily be met by amending the self dealing provisions of section 4941 to incorporate therein, with respect to dispositions of existing excess holdings under the transitional rule, provisions similar to those contained in Section 4942 of the Code in respect to initially determining fair market value in arriving at the amount to be paid out each year and/or in respect to making adjustments where a court subsequently determines a dieffrent fair market value. Such an amendment would make no fundamental change in the Tax Reform Act rules governing private foundations. Such a change would be of limited scope, inasmuch as it would deal only with forced divestitures of excess business holdings held or treated as being held by private foundations on May 26, 1969. And the effect of the amendment would be of limited duration. As for those excess holdings actually owned on May 26, 1969, the grace period for disposing of those holdings will expire, except in a very limited number of cases, within the next 10 years.

Most importantly, incorporating the same fair market value provisions as are set forth in section 4942 into those provisions of section 4941 applicable to dispositions of existing excess holdings under the transitional rule of section 101(1)(2)(b), will not result in a foundation's receiving anything less than ultimately determined fair market value. If a mistake is made, it will have to be rectified.

The ameliatory effect of such an amendment would be that foundation managers and redeeming corporations will not face the risk of inadvertently committing a self dealing act. This will encourage redemptions to be made now and in the near future, to the advantage of charity.

Alternative solutions

Representatives of the Service with whom we have discussed this problem and who frankly recognize the real impossibility of determining the correct

fair market value of closely held stock, have suggested that if foundation managers and redeeming corporations are unwilling to be insurers of the fair market value determinations made by independent appraisers, there is an alternative method available to the foundation for divesting its existing excess holdings, namely to sell the excess holdings to persons outside the disqualified person group or to distribute such holdings to public charities. But charity will not be best served if foundations utilize either of these approaches.

Sales of minority interests of closely held companies to persons outside the disqualified person group could not realistically be made for any amount close to what an uncompelled seller would be willing to accept. Prospective purchasers not only would make substantial discounts in fixing the price because of the nature and lack of liquidity of the stock, but they also would be likely to take advantage of the forced nature of the sale and make further, unwarranted discounts from what might be called the stock's intrinsic value.

Nor would charity be served if foundations were to distribute their existing excess holdings in closely held companies to public charities. Public charities which receive gifts of securities otherwise than for endowment are usually interested in selling those securities to raise cash for their operations. And where securities are received for endowment, public charities are interested in disposing of those securities if they think the value is declining or is uncertain. Closely held stock, particularly a minority interest, is not regarded as an attractive addition even to an endowment portfolio. If the public charities decide to sell such stock interests, they generally would have no market for such stock other than within the private foundation's disqualified person group or among persons who would require a very substantial discount because of the lack of liquidity. Public charities face the same problems as private foundations in trying to dispose of minority interests in closely held corporations. And there may be no market available within the disqualified person group. The foundation's disqualified persons may be unwilling to face the risk of committing what the Service may consider to be an indirect act of self dealing, as well as the risk of incurring possible constructive dividend consequences. Corporate disqualified persons may also be unwilling to take the risk inherent in a redemption from public charities. The accumulation and use of corporate earnings to redeem excess business holdings is protected from adverse tax consequences only where a disposition of those holdings is required by the excess business holdings provisions of section 4043. The Service has regularly contended that in a closely held situation, use of corporate earnings to redeem shares is not a section 531 protected purpose. The only protection for such a use comes from section 537 which is not available in the case of redemptions from public charities. As a result, the only alternatives available to public charities may be the retention of such holdings in their portfolios or the sale of such holdings to third parties at a necessarily discounted price. Neither alternative would in any way achieve the fundamental purpose of the Tax Reform Act of making the resources of private foundations available to the maximum extent possible for operational charitable activities.

SUMMATION

The present statutory framework of the self dealing restrictions on private foundations, as interpreted by the Treasury Department and the Internal Revenue Service, makes no allowance for good faith differences in opinion on fair market value in transitional rule dispositions. If, because of the incalculable risks involved in committing an act o fself dealing even through best efforts were applied to achieve fair market value, members of the disqualified person group are effectively removed from the market for a foundation's existing excess holdings, the foundation's task of disposing of existing excess holdings of closely held stock for any amount close to fair market value, is rendered difficult and perhaps impossible.

UNITED STATES SENATE,
Washington, D.C., July 12, 1974.

Hon. VANCE HARTKE,
Chairman, Subcommittee on Foundations, Finance Committee, Senate Office Building, Washington, D.C.

DEAR VANCE: In accordance with your request for comments on the Federal Excise Tax on private foundations, I enclose copies of two letter received from a constituent, Mrs. Richard Parke, of North Conway, New Hampshire.

Her letters eloquently describe the plight of small civic, education and charitable organizations in dealing with the excise tax. It is difficult to believe that the Congressional intent in passing the Tax Reform Act of 1969 was to place such worthy organizations in financial jeopardy.

I hope the committee will give attention to this problem and find a solution that recognizes the injustice currently being worked on worthy civic organizations.

Would you please incorporate Mrs. Parke's letters in any permanent record of the hearings on this issue?

Sincerely,

THOMAS J. MCINTYRE,
U.S. Senator.

MRS. RICHARD E. PARKE,
North Conway, N.H., May 25, 1974.

Hon. THOMAS J. MCINTYRE,
U.S. Senate,
Washington, D.C.

DEAR SENATOR MCINTYRE: On March 20 I wrote you about the difficulty caused the North Conway Public Library by the excise tax on private foundations, levied on gross income regardless of the costs of operating. We shortened our week by two days but the savings were used up by added fuel and electricity costs.

I have just spent four hours with an I.R.S. agent on an audit which is costing us another $300 to $400. The agent mentioned his having to assess an excise tax of some $3000 on a struggling children's home, with the young director practically in tears. He said that legislative action is the only way to save these small organizations from this excise tax and that Congressman Cleveland endeavored to have corrective action taken but that "it never got off the floor".

Would you please take positive action to give exemption from the private foundation excise tax to small civic, educational and charitable organizations which have been granted income tax exemption?

The purpose of the tax is to cover costs of investigating the private foundations. I wonder what tax is paying for the current investigations in Washington.

We have asked Congressman Wyman for his assistance, also. It would be appreciated if you could send us copies of any documents which you may file with the Committee on Internal Revenue Taxation in support of such excise tax relief.

Sincerely yours,

CHRISTINE S. PARKE,
Treasurer.

MRS. RICHARD E. PARKE,
North Conway, N.H., March 20, 1974.

Hon. THOMAS J. MCINTYRE,
U.S. Senate,
Washington, D.C.

MY DEAR SENATOR MCINTYRE: Because of the strong mutual interest which I know you and I share in the welfare of small libraries, I hope that as our Senator you may start some action which will relieve a serious burden borne by our local library as well as by many similar small organizations.

The Revenue Act of 1969, in an effort to correct some unjustified tax benefits to wealthy individuals through use of private foundations, placed a tax upon them, with stringent reporting requirements. However, I do not believe that it was the intent of the Congress to tax small, non-profit, tax exempt organizations such as ours.

Our total income is only about $12,000, but as it comes mostly from income from investments we have been classified as an operating private foundation and subject to the special tax. This tax is not levied upon any income remaining after operating costs; it is taken from the top, *before* salary for the librarian,

building expenses, purchase of books, etc. Therefore, even if operating at a loss, we would still have to pay this tax which would increase it.

Last year this tax cost us over $400. In addition we had to pay an accountant over $300 because of the complexity of the Forms 990AR and 990PF required by the I. R. S. These forms are the same as those filed by foundations with assets in the millions.

This annual cost of over $750 before operating expenses for a tax-exempt educational association seems far beyond justice or the intent of the Congress. Would you please determine if this taxing of small libraries was spelled out in the act as enacted or is the result of the interpretation by the I. R. S. when it made up the regulations? Would you also please inaugurate corrective action, if you agree that it was not the intent of the Congress to so burden small *public* organizations under the guise that they are *private* foundations?

Very truly yours,

CHRISTINE S. PARKE,
Treasurer.

SALLY J. MILLER,
UTICA, MICH., *July 25, 1974.*

MICHAEL STERN, Esquire,
Staff Director, Senate Finance Committee,
Senate Office Building, Washington, D.C.

DEAR SIR: Senator Hartke, Chairman of the Senate Finance Committee on Foundations, has invited comments with respect to Internal Revenue Code sections 4940 and 4942.

Section 4942 imposes an excise tax on failure to distribute income. The private foundation is required to distribute as qualifying distributions the greater of adjusted net income or minimum investment return in order to avoid the excise tax imposed by section 4942.

This letter relates to the treatment accorded expenses incurred for the production of income by a private foundation under section 4942 by the Internal Revenue Service. Section 4942(g) defines qualifying distributions as follows:

"(g) Qualifying Distributions Defined.

"(1) In General. For purposes of this section, the term 'qualifying distribution' means—

"(A) any amount (*including administrative expenses*) paid to accomplish one or more purposes described in section 170(c)(1)(B), . . ."

The *underlined* portion was added by the Senate Finance Committee. The Senate Finance Committee report states (page 35):

"The committee's amendments made it clear that the audit fee (described above) and the unrelated business income tax reduce the amount the foundation must pay out to meet the minimum distribution requirements, *and reasonable administrative expenses of operating the foundation constitute qualifying distributions.*"

Further, the regulations provide that administration expenses qualify as a qualifying distribution. Regulation section 53.4942(a)(3)(a) provides:

"(2) DEFINITION. The term 'qualifying distribution' means—

(i) Any amount (including program-related investments, as defined in section 4944(c), and reasonable and necessary administrative expenses) paid to accomplish one or more purposes described in section 170(c) (1) and (2)(B). . . ."

Nevertheless, the Service takes the position, in connection with the instructions to the form 990PF, that expenses for the production of income by a private foundation can never be a qualifying distribution.

The *sine qua non* of every private foundation is the capacity to produce income for charity. The Senate Finance Committee Report referred to "reasonable administrative expenses of operating the foundation", as constituting qualifying distributions. The Committee Report did not say, *some* administrative expenses or only certain types of administrative expenses. The only limitation is that the expenses of operating the foundation must be *reasonable* in amount.

It is recognized that the Service has a problem with respect to the question of whether administration expenses are qualifying distributions. In the case where adjusted net income is the greater of adjusted net income or minimum investment return, it is clear that expenses relating to the production of income are a deduction in arriving at adjusted net income. Therefore, the taxpayer should not be allowed to deduct expenses for the production of income a second time as qualifying distributions.

However, in the case where the minimum investment return is the greater of adjusted net income or minimum investment return, administration expenses are not taken into account in arriving at minimum investment return.

It is suggested that the following is the proper rule: In the case where adjusted net income is greater than the minimum investment return, expenses for production of income are not deductible as qualifying distributions because they were deducted in arriving at the adjusted net income. However, in the case where the minimum investment return is greater than the adjusted net income, expenses for the production of income are deductible as qualifying distributions.

The current position of the Service produces an anomalous situation where expenses for the production of income are deductible with respect to the adjusted net income and are not deductible with respect to minimum investment return.

Very truly yours,

SALLY J. MILLER.

THE WILLIAM K. WARREN FOUNDATION,
Tulsa, Okla., July 25, 1974.

Hon. SENATOR HARTKE,
U.S. Senate,
Washington, D.C.

DEAR SENATOR HARTKE: I am writing this letter at the request of Mr. W. K. Warren, founder of The William K. Warren Foundation, and Mr. C. J. Senger, President of The William K. Warren Foundation.

I am writing to you to encourage your support in lowering the tax on private foundation income. The William K. Warren Foundation has without any federal or state funding built and equipped the largest and most modern hospital in Oklahoma. Last year The William K. Warren Foundation paid $140,000 in excise taxes. The net effect was that Saint Francis Hospital in Tulsa received $140,000 less than they would have otherwise received for the critically important expansion of the hospital and the services it provides. The patients at Saint Francis Hospital, which is a regional medical center, come from as far away as Denver, Colorado, and the hospital has many patients from western Arkansas, as well as Missouri, Kansas, New Mexico and Texas.

The tax on private foundation net investment income should be lowered to an amount equal to the actual cost of audit.

The tax now raises twice as much money as is needed to cover Internal Revenue Service audit activities of all exempt organizations. The revenue produced by a 2 percent tax will provide the Service with ample funds vigorously to enforce the exempt organization provisions of the Internal Revenue Code.

The Treasury has formally advised the Congress that it supports a reduction of the rate of tax from 4 to 2 percent.

The tax is not a tax on private foundations. It is a tax on operating charitable and educational organizations that depend on private foundations for support, and in some cases, survival. This is so because the law operates so that each dollar of tax paid reduces by one dollar the amount private foundations otherwise would be required to distribute for active charitable purposes.

This action by Congress may be viewed as a desirable interim measure, leaving for future consideration other key questions regarding the nature of the tax and whether the monies raised by it should be earmarked for specific purposes.

I appreciate your consideration and if I can be the source of any additional information as to how this tax effects foundations and their recipients, I would be glad to do so either by letter or by coming to Washington to meet with you personally.

Very respectfully,

DAVID M. BARRETT.

DALLAS, TEX.,
July 18, 1974.

Hon. VANCE HARTKE,
Chairman, Senate Finance Committee's Subcommittee on Foundations, % Mr. Michael Stern, Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR SENATOR HARTKE: The Trustees of The McDermott Foundation, a private foundation in Dallas, Texas, wish to submit their views on Code Sections

4940 and 4942 in response to your invitation to file these for the record and study of the Subcommittee on Foundations.

We believe the 4% tax imposed by Section 4940 is extremely punitive and unnecessary. It has more than doubled this Foundation's costs (for legal, accounting and administrative fees). Presumably the experience of other such foundations duplicates our own. These increased expenses obviously reduce the dollars available for the charitable purposes of the Foundation. Despite the substantial increase in the number of IRS auditors and the breadth of its investigations of such foundations, it is our understanding that the tax collected is six times greater than IRS costs of such audits. There is certainly some argument for abolishing this tax altogether since such foundations are the only entities in the nation which are charged for IRS audit services. If it is not completely abolished, we strongly urge that the tax at least be reduced to ½ of 1% of net investment income and that capital gains be excluded from investment income so funds set aside and required for charitable purposes will not be diverted to noncharitable government use.

The prevention of indefinite deferment of distributions to charities, the thrust of Section 4942, is commendable indeed. However the annual payout requirement of 6% of market value of investment assets is stringent and places too severe a burden on Foundation trustees to secure a sufficiently high rate of return to avoid:

1. Converting all its investment assets into bonds or other fixed income securities (thus dealing a severe blow to the nation's economy as well as to the ability of the foundation to protect itself against inflation).

2. The other alternative of slowly liquidating and terminating the existence of the foundation represents an even more severe blow to the churches, hospitals, and educational, medical and research institutions which depend so heavily on continued support from such foundations. We urge a reduction in the minimum percentage required to be distributed from 6% to 3%. This would permit private foundations to invest at least a part of their assets in equity securities and preserve their existence.

Many of the most vital services which meet public need were developed and inspired as well as made possible through the financial assistance of foundations which became classified as private under the Tax Reform Act of 1969. To continue to and further diminish their roles in our pluralistic society is, we believe, a disservice to the public. The size of foundations' assets and annual giving ability is negligible when compared to Federal Government expenditures in health, education and welfare. Failure to preserve the foundations, in our opinion, will have an unalterably negative impact on our nation's charitable institutions.

We shall appreciate your consideration.

Sincerely,

MRS. EUGENE MCDERMOTT,
President.

SUTHERLAND, ASBILL & BRENNAN,
Washington, D.C., July 26, 1974.

HON. VANCE HARTKE,
U.S. Senate,
Washington, D.C.

DEAR SENATOR HARTKE: On behalf of Carnegie Corporation of New York, a private foundation, this letter responds to the request of your Subcommittee on Private Foundations for comments with respect to section 4940 of the Internal Revenue Code. That section imposes a 4 percent tax on the net investment income of private foundations.

Mr. Alan Pifer, president of Carnegie Corporation, presented testimony to the Subcommittee on October 2, 1973. However, as Mr. Pifer's testimony was directed to other subjects, Carnegie Corporation believes that it is now appropriate to supplement the earlier testimony to indicate its support of proposals made to the Subcommittee that the rate of the section 4940 tax be reduced. Mr. Pifer also testified before the Finance Committee on October 6, 1969, in connection with the Finance Committee's consideration of what was to become the Tax Reform Act of 1969. In the course of his testimony Mr. Pifer stated that the imposition of a general revenue tax upon private foundations, or any other class of charitable organizations, represents an unwarranted departure from the long-standing tradi-

tion of tax exemption for such organizations. At that time Mr. Pifer and others suggested that an annual fee be imposed upon foundations to fund the costs of enforcement of the then proposed legislative restrictions on foundations. This alternative approach was adopted by the Finance Committee and by the Senate in 1969.

In practice, the tax imposed by section 4940 has produced revenues which greatly exceed the costs of enforcement. For this reason, Carnegie Corporation supports the proposal made to the Subcommittee by Senator Bartlett and others that, as an interim measure, the rate of the tax be reduced to a level which would bring revenues from the tax into line with the costs of the Internal Revenue Service's enforcement program. Such a reduction would, by reason of the operation of section 4942 of the Internal Revenue Code, increase the funds distributed by Carnegie Corporation and other private foundations for active charitable purposes.

The interest of the Subcommittee in this important issue is appreciated.

Respectfully submitted,

DONALD V. MOOREHEAD.

STATEMENT OF THE LILLY ENDOWMENT, INC., INDIANAPOLIS, INDIANA, BY LANDRUM R. BOLLING, EXECUTIVE VICE PRESIDENT

There is good reason for foundations to be subjected to continuous scrutiny. Foundations represent significant accumulations of wealth dedicated to public purposes, and such wealth entails both power and responsibility. How they dispose of their resources may affect, for good or ill, important aspects of our national life. At best, their grants may make possible genuine break-throughs in the solving of major problems. At worst, they may waste substantial funds on ill conceived or needless projects or they may prolong activities and institutions that have outlived their usefulness. In times past a few foundations have even operated in such a manner as to further the special economic interests of the supposed philanthropists, with little or no benefits to the needy persons and worthy causes the foundations were intended to serve. These were rare exceptions, but such things did happen.

The Tax Reform Act of 1969 was designed to eliminate such abuses and to establish standards of performance that would promote the wise and socially beneficial use of foundation funds. There may be sincere differences among honest people over some of the details of that law, but no thinking person will question the desirability of publicly declared guidelines for the responsible operation of foundations and effective enforcement of them. Nevertheless, it could well be that certain provisions in that act should be changed, as has already been suggested in the hearings of the Hartke Subcommittee on Foundations. A few comments on these proposals will be included later in this statement.

At the outset, however, there is good reason to examine certain basic issues that relate to the question of whether there is real justification for foundations to exist today and whether they should be permitted to exist tomorrow. To find any meaningful answer we must, in turn, consider these questions:

1. Whose money is it, anyway—the government's? or the original donor's?—or does it belong to the special non-profit corporate body set up to administer the foundation, or is there some other way to define "ownership" of foundation assets? In the past, there have been cases in which a foundation acted as if its resources were still the personal possession of the original donor and manipulated them to advance the donor's private economic interest and, in greater or lesser degree, to follow his whims in support of selected charities. Such a situation is not tolerable under the law or any sound social policy.

But what of the increasingly common assertion that foundation resources are really "tax moneys" which the government, by a kind of historical accident, has come to allow private persons to spend for it? This theory leads easily on to the idea that the government should take over these resources and have government officials spend them directly. Back of this thinking is the demonstrably false notion that if a foundation had not been created but the capital received by the foundation from the donor had been taken instead by the Government, the same amount of money now held by the foundation would have automatically come into the hands of government. This idea is based upon a partial truth and certain

misperceptions. Whether by gift or bequest, part of the funds originally set aside to establish a foundation would indeed have been collected as taxes had they not been directed by the donor into a foundation, approved and registered by the Internal Revenue Service in accordance with federal statutes. Yet rarely, if ever, is a donor compelled to make a simple choice between giving his money to a foundation or to the Government. He could donate the money or the property in question to a church, school or hospital and thereby avoid the tax. He could squander the money in personal extravagances or in non-profitable enterprises of various kinds. He could make investments in many different sorts of enterprises or make loans, good or bad, to his friends and relatives. Eventually, of course, it is to be assumed that the government would in most cases be able to collect an appropriate tax related to the funds in question—but almost never would the amount collected in taxes equal the amount originally assigned to a foundation—and would certainly not equal the appreciated value of foundation holdings that have been prudently managed over time.

Lilly Endowment, Inc., beginning in 1937, received its capital over the years in several gifts and bequests, totalling $95,000,000. Its gifts to schools, colleges, hospitals, social welfare agencies, units of government and other approved charities have by now equalled more than twice the amount of the total capital given; meanwhile, assets have grown to such a point that, at present rates, it will, every two years, give away to these public services grants equally the amount of the combined capital gifts. Had the full $95,000,000 been expropriated by the Government—it could not all have been taken in taxes—we may be sure it would all have been spent long ago.

The truth is that foundation assets are neither the private possession of the original donor nor "tax moneys" belonging to the government. They are private moneys "affected with a public interest," given a special tax-exempt status under the law, dedicated to serving some of the same public purposes—except for religion—which government itself is supposed to serve, but operating under private auspices, subject to public regulation.

2. An often-asked second question is this: Could not government agencies spend the money held by foundations more effectively than the foundations? The only wholly honest answer is to say that it depends on the individuals involved, the policies being pursued and the general political climate. Even a casual look at the record will show that in fields where their activities can be compared some government projects have succeeded and others have failed, some foundation-sponsored projects have succeeded while other foundation-supported projects have failed. By and large, however, it appears that government projects tend to have higher unit costs than do those sponsored by foundations. Moreover, foundations tend to put their money into projects for which there is a high level of volunteer participation and matching financial support. In situations where there can be direct cost comparisons—as for instance, the operating of day care centers or the supplying of American teachers or village development workers in the emerging new nations, through the Peace Corps or through privately financed agencies, there seems to be clear cost advantages on the side of the privately funded projects. Whatever the case against foundations, it cannot be based upon the argument that "the government can do it cheaper." This is an issue on which more research, of course, is needed.

In comparing private foundations and government agencies on the issue of prompt responsiveness to a critical need, the answer seems abundantly clear. Foundations, with their small staffs and easily assembled boards of directors, are, in most cases, able to respond to demonstrated needs more expeditiously than can the government. Lilly Endowment, like other foundations, receives, year after year, appeals from state, local and federal government agencies, for financial assistance to *them*, to help carry out projects officially approved but for which funding must be delayed for periods of a year or more while the more cumbersome processes of government grind ahead. The capacity to respond quickly is often of the utmost importance for both governmental and non-governmental programs, and the record of foundations on this issue of responsiveness gives them a clear comparative advantage, within the range of their resources.

3. Still other questions have to do with the scale of grant-making by foundations in relation to their assets. At what rate should a foundation be expected to pay out its resources? Should there be a fixed and permanent pay-out rate determined by law? And back of these questions stands the larger question of whether foundations should be placed under a kind of "death sentence", limit-

ing their existence to a specified number of years, or whether they should be regarded as having permanent value and, therefore, the right to continuing existence. When this latter issue was explicitly considered at the time of the writing of the Tax Reform Act of 1969 it was decided *not* to impose a legal limitation on the life expectancy of foundations but to establish an increasing scale of annual pay-outs, rising by 1975 to the tentative target of six percent of the capital assets. This is not the occasion for arguing for or against a particular percentage figure. What is at issue is the continuing legitimacy and desirability of private foundations as valuable institutions in American society. Whatever the formula, the pay-out requirements should be set at such a level as not to encourage a "salami slicing" approach to the gradual destruction of foundations.

As the two hundred years history of America has demonstrated repeatedly, our diverse, pluralistic society requires much flexibility in the handling of many phases of our national life. There is great value in a wide dispersion of power to deal with our public problems—through national, state and local governments and between government and private entities. For power to be effective there must be access to diverse sources of funds. Private foundations offer an important source of "risk capital" necessary to keep alive our national tradition of local initiative and of individual and group freedom. They are a significant part of the base on which to build a pluralistic and open society. Their continued existence should not be treated as a favor to special privilege but as a constructive means for trying to build a better world.

The legitimacy and positive value of foundations will no doubt have to be established over and over again. They are and will continue to be on trial. Each foundation in turn will have to answer both foundation critics in general and those from whom attacks have come to the individual foundation. Lilly Endowment was recently pointed to with apparent disapproval by Patricia S. Senger, a public interest lawyer, who testified before this committee. Her criticism of Lilly Endowment, primarily with respect to its pay-out rate, was based on information already more than two years out of date. She made no evident effort to bring her analysis up to date, to show what has happened to the dollar volume of Lilly grants and to the ratio of grants paid to total assets held, since the Tax Reform Act of 1969 took effect, although we would have been glad to supply her with that data if she had asked.

Lilly Endowment from its beginning has scrupulously abided by state and federal laws and regulations. Until the Tax Reform Act of 1969, with its percentage pay-out requirements, Lilly Endowment did what practically all active foundations did—it paid out each year its total earnings from its investments. Since its capital was primarily in a single low-yield stock, Eli Lilly and Company, its percentage pay-out was indeed low, around 1 percent, on the total value of the stock held. However that stock has been a rapid growth stock, has enormously increased in market value in recent years and thus provides far more resources for charitable giving today than would be available had the capital been placed in higher yield but slower growth equities. Moreover, the dollar amount of grants—due to the growth of the worth of the Endowment—did in fact increase substantially from year to year, even before enactment of the Tax Reform Act of 1969. Taking the entire 37 year history of the Lilly Endowment's operations, its grants have averaged an increase of 30.17% each year over the preceding year.

Since the Tax Reform Act went into effect, we have, of course, had a different situation for all foundations. Lilly Edowment's grants disbursements during the past four years are as follows:

1970: $9,254,000.
1971: $9,886,600.
1972: $14,262,600.
1973: $31,112,314.

For 1974 we estimate total grants of approximately $49,000,000.

For a witness to come before this committee in May, 1974, and, make the bold statement concerning the Lilly Endowment that "The record of charitable contributions has not changed . . ." is to misrepresent the facts and to ignore developments affecting all foundations that have resulted from the Tax Reform Act of 1969, and to fail to take into account the twelve month lag possibility in pay-out, as provided by that law. Not only has the dollar amount of Lilly Endowment grants increased substantially but the ratio of pay-out to total assets has risen by stages, as specified by law, to the rate of four and one-eighth (4⅛%) in 1972; four and three-eighths (4⅜%) in 1973, and five and one-half (5½%) percent

in 1974. Compare these facts with Miss Senger's present-tense statement ". . . the Lilly Endowment grants amount to only 1.1% of its assets (1972 figures)."

Linked to the misrepresentation of the Lilly Endowment's policies and performance on the pay-out of grants, is a further misleading judgment about management of the capital assets of the Endowment. The argument made is that because Lilly Endowment, Inc. has largely retained its stock holdings in Eli Lilly and Company (the form in which the original capital was received) the amount of funds available for charitable purposes has been made substantially lower than would have been the case had the original assets been converted into a diversified portfolio. The flat statement is made that: "If the Endowment directors were primarily concerned with contributions to charity, they would have reinvested some of the money years ago in stocks that pay higher dividends." The suggestion is put forward that "Even Savings and Loan Associations now pay up to 7.9% on savings accounts."

The merits of this kind of simplistic analysis can be quickly seen. The resources available for charity, *over time*, are not determined just by the rate of current income return but by annual income *plus capital appreciation*. On this total value basis, the record of the Lilly Endowment's holdings has been phenomenal. Compared to any mutual fund, the Dow-Jones average, the Moody list of Selected Stocks, or any other diversified portfolio offered as a yard-stick, the Lilly Endowment's equities in a well managed and rapidly growing company have since 1937 "out-performed" by a large margin all the alternative diversified funds that might have been substituted.

It is worth noting that the Kellogg Foundation, the Pew Foundation and certain other large private foundations created on the basis of family gifts of stock in a single company have comparable records that show that their concentrated holdings also far "out-performed" the market.

Lilly Endowment's experience with diversification in 1973 was instructive. During that year the Endowment sold off approximately $185,000,000 worth of stock in Eli Lilly and Company and reinvested the proceeds in diversified portfolios managed by expert investment counsel. At the end of the year when the results were in, it was determined that the assets of Lilly Endowment would have been approximately $75,000,000 greater if none of the Lilly stock had been converted into these supposedly "safer, more productive" diversified equities.

A favorite bit of folk lore among critics of foundations is the claim that diversification of investments is the road to financial health and expansion of assets for charitable giving. In some cases this, relatively speaking, may be true. But it is not necessarily so. It would not have been so for Lilly Endowment and for a number of the other large family foundations.

The real test of foundations, of course, will not be found in arguments over their pay-out rates and their investment policies. (Although here it would be useful to get the facts straight.) Foundations will be ultimately judged—should be judged—on their record of support of significant accomplishments for mankind. In this regard they should be rigorously, continuously, scrutinized and challenged. If they do well the work they are called on to do, and have abundant opportunity to do, they need not fear comparison with any government agency that any critic may propose should take over their funds and their functions. They are and can remain a catalyst to improve the work of government, to supplement the work of government, and to undertake creative risks for the public good the government may not be ready and able to undertake.

UNIVERSITY OF DELAWARE,
Newark, Del., July 23, 1974.

Mr. MICHAEL STERN, *Staff Director,*
Senate Finance Committee, Senate Office Building,
Washington, D.C.

DEAR MR. STERN: As Director of a program preparing nearly 50 young persons each year to enter the museum profession, I have been concerned about the provision of the 1969 Tax Reform Act that requires a small number of excellent museums classified as private operating foundations to pay a 4 percent excise tax on their endowment income.

Senator Roth of Delaware has suggested that I write you of my opinion. I agree with the testimony given to your Subcommittee on Foundations on May 13–14 by Kyran M. McGrath, Director of the American Association of Museums. The 1969

legislation has made these private operating foundation museums cut their programs and therefore reduce their services to the public. All museums accredited by the American Association of Museums—about 300 at present—and thus required to meet rigid professional standards, should be treated as public charities. The requirement of professional accreditation would be enough to prevent any abuse by a private operating foundation.

I shall greatly appreciate the attention of your subcommittee to this reasonable and practicable point of view.

Sincerely,

EDWARD P. ALEXANDER,
Director of Museum Studies.

EL POMAR FOUNDATION,
Colorado Springs, Colo., July 18, 1974.

Mr. MICHAEL STERN, *Staff Director,*
Senate Finance Committee,
Dirksen Senate Office Building,

DEAR MR. STERN: The El Pomar Foundation would like to thank you for this opportunity to express its concerns with Sections 4940 and 4942 of the Internal Revenue Code. The Trustees of the El Pomar Foundation feel that the provisions of the 1969 Tax Reform Act increase the awareness of foundations as to their responsibility in philanthropic endeavors, and it certainly has helped to curb those groups which use the foundation category as a refuge from taxation.

Our experience now indicates that in several areas protections have gone beyond those reasonably necessary to insure the proper application of foundation funds. Section 4940 of The Internal Revenue Code requiring a 4% excise tax on investment income would appear to be more than twice the needs of Internal Revenue Service in monitoring and regulating foundations. In 1972, the El Pomar Foundation paid $132,750.00, and in 1973, $125,057.00 in this tax. It is obvious that the request for funds for worthwhile programs and projects far exceed the resources available for distribution by the El Pomar Foundation. Colorado does not have a great many foundations, and by The Articles of Incorporation of El Pomar, our grants are limited to this state. If the excise tax were 2% rather than 4%, this would have meant in the last two years an additional amount in excess of $120,000.00 could be used for charitable endeavors within the State of Colorado. It would be anticipated that our situation is no different than that of most foundations, specifically those that limit their grant making to a particular regional area.

Section 4942 of The Internal Revenue Code which requires a minimum distribution of net investment income is really too high for sound investments. The need to use capital to meet this requirement deprives future generations of the benefits which El Pomar Foundation has been able to provide the people of Colorado over the last thirty-seven years. Through judicious management the assets of the El Pomar Foundation have grown and with this growth the amount of contribution has greatly increased. The Foundation feels that pay-out requirements in the area of 4% per year would be commensurate with the type of investment policy which could sustain a viable foundation system. It should be noted that the El Pomar Foundation has always had a policy that in those years of extreme need, additional contributions are paid far exceeding the proposed 4% mandatory pay-out requirement.

This Foundation would be glad to send a representative to testify on either or both of these Sections of The Internal Revenue Code, should this be the desire of the Committee.

The Trustees of the El Pomar Foundation believe very strongly in the institution of private charity and certainly hope that El Pomar may continue to make a significant contribution to the people of the State of Colorado.

Sincerely,

WILLIAM THAYER TUTT,
President.

THE ROBERT WOOD FOUNDATION,
Princeton, N.J., July 22, 1974.

MR. MICHAEL STERN,
Staff Director, Senate Finance Committee,
Dirksen Senate Office Building,
Washington, D.C.

DEAR MR. STERN: In response to your press release of July 1, we respectfully submit the following comments on Sections 4940 and 4942 of the Internal Revenue Code.

SECTION 4940

Under this section, there is imposed upon private foundations an "excise" tax equal to 4 percent of net investment income. For the purpose of the tax "investment income" includes all gains realized from the sale of property held for production of income with losses deductible only to the extent of gains. No carryover of excess losses to subsequent years is allowed.

Recommendation:

(a) The excise tax should be restated and termed an audit fee to better reflect the original intent of Congress.

(b) The rate of the fee should be reduced to bring it more nearly in line with actual cost of auditing.

(c) If losses on sale of property held for the production of income exceed gains, such losses should be permitted to be carried forward for three years.

SECTION 4942

Under this section a private foundation is required to distribute all of its income or a fixed percentage of the fair market value of its assets determined annually, whichever is larger.

There are no provisions in the present regulations for a foundation which receives a substantial block of one company's stock to have sufficient time to diversify before applying the payout provisions of Section 4942. A transition period is needed, for time, market conditions and the federal securities laws all have an important input in a sound diversification program.

Recommendation:

(a) There should be a more extensive transition period within which a foundation could adjust to the requirements of a payout provision such as imposed by Section 4942.

(b) The percentage payout should also be adjusted during the transition period.

(c) As an interim measure we urge passage of H.R. 1197, sponsored by Congressmen Mills and Schneebeli. This would reduce the percentage payout from 6 to 5, which is more in line with the actual rate of return of similarly invested portfolios and extend the Reform Act transition period so that the percentage payout would be 3½ for 1972 and 1973, 4 percent for 1974 and 1975, 4½ percent for 1976 and 1977, and 5 percent for 1978 and later years.

(d) H.R. 1197 should also include a provision that excess payout in any year may be carried over to future years.

Very truly yours,

WILLIAM R. WALSH, Jr.,
Treasurer.

STATEMENT OF NORMAN A. SUGARMAN, CLEVELAND, OHIO

This statement is submitted in response to the invitation of the Chairman of the Subcomittee on Foundations, Senate Finance Committee, to submit comments on Sections 4940 and 4942 of the Internal Revenue Code.

Section 4940

There were three principal reasons for imposing a tax on the net investment income of private foundations as provided in the Tax Reform Act of 1969: (a) To provide funds to meet the costs of auditing such foundations. (b) To see that such foundations paid some tax, and (c) To encourage more responsible reporting by such organizations by reason of the fact that they filed taxable returns.

There is serious question whether private foundations should be singled out for a tax for these reasons; but even assuming the validity of these reasons, experience has clearly demonstrated that the four percent (4%) tax is larger than is necessary for the purposes cited. Facts demonstrated that a one percent (1%) tax would raise the revenue needed for an audit of private foundations. Any tax in excess of that amount, even though used for audit of other exempt organizations, places an added burden on funds that otherwise would be used for charitable purposes.

Other provisions imposing restrictions and penalties on private foundations under the 1969 Act—which have been well publicized—are adequate to provide for more responsible reporting by private foundations. The Audit Program of the IRS is also directed to assuring this result.

It should be clearly recognized that a tax on the net investment income of foundations does not adversely affect the fundations but simply reduces funds held for or distributable to charitable recipients. A 1% or 2% tax on the net investment income of private foundations would fully serve the purposes for which the tax under section 4940 was intended. Accordingly it is recommended that the tax be reduced to 2% or, if the figures from the Internal Revenue Service as to audit costs permit, the tax should be reduced to 1%.

SECTION 4942

One of the major changes made by the Tax Reform Act of 1969 was to require private foundations to make current distributions for purposes forming the basis of their exemption. However, section 4942 of the Internal Revenue Code as finally enacted goes far beyond the requirement that a private foundation distribute its income for such purposes annually. Instead, the statute requires that the Foundation distribute the larger of (a) its adjusted net income and (b) its "minimum investment return." The minimum investment return is a stated percentage of the net fair market value of all assets of the Foundation other than those being used (or held for use) directly in carrying out the Foundation's exempt purposes.

The minimum investment return concept is a justifiable one where it is based on the concept of a reasonable rate of return and it is intended to provide distributions for charitable purposes of such a reasonable return without being involved in the distinctions of income or principal under trust accounting concepts. Thus, many foundations have gone to a "total return concept" in order to make a fair distribution based upon the value of their assets even though such distribution may exceed ordinary income and reflect, in part, gains on turnover investment assets.

However, section 4942 as enacted does not serve the purpose of insuring simply that a reasonable yield on investment assets will be distributed annually for charitable purposes. The statute as enacted provides that in the case of private foundations created on or after May 27, 1969 the applicable minimum investment return percentage is six percent. In the case of private foundations created before May 27, 1969, there are transition rules, i.e., 4½% in 1972, 5% in 1973, 5½% in 1974 and 6% in 1975 and thereafter. The Secretary of the Treasury is authorized to adjust these percentages but for 1974 the percentage for pre May 27, 1969 foundations is 5.5% and for those created thereafter is 6%.

OBJECTIONS TO PRESENT MINIMUM INVESTMENT RATE

The minimum investment return rates specified in section 4942 are objectionable as being too high for the following reasons:

1. *The rates as presently prescribed by the statute are clearly in excess of a reasonable rate of return based upon experience and practices in the managements of trust funds; and the higher rates prescribed by the statute have a punitive effect which from a long-range viewpoint will reduce charitable funds available for the public benefit.*

Ample evidence has been produced on numerous occasions to indicate that a reasonable yield on assets productively invested for charitable purposes, when there is balance between the desire for income and preservation of the principal, is between 3½% and 4½%. This, of course, does not take into account capital gains which result from turnover of principal in order to take advantage of appreciation which may lead to reinvestment at a higher yield. The Congress

itself has recognized the reasonableness of these figures by indicating, for example, in section 4942(j)(3), defining operating foundations, that a yield of two-thirds of the minimum investment return (e.g., 4%) is sufficient for a private operating foundation.

The 6% requirement has a distinctly adverse effect upon the long run ability of foundations to provide charitable distributions. Because the 6% distribution requirement is in excess of a normal yield of income in a prudent balanced investment program, foundations must in order to meet the requirement (a) invest in high yield securities, which either involves higher risk or little growth, or both, (b) invest in speculative securities for capital gain appreciation, which places a premium on risk taking ahead of prudence, or (c) invest prudently and distribute income and capital gains. Under any alternative, the 6% distribution requirement creates a forced liquidation, since available principal is reduced by lack of growth, by downside risks and by distributions of principal.

Under these circumstances, foundations will be unable to keep pace with inflation, the increasing needs for charitable funds and the increasing costs of operations and service of public charities which are supported by private foundations. Thus, the minimum distribution requirement under section 4942 is counterproductive from a long-range viewpoint in meeting the increasing needs and costs of services in our educational institutions, hospitals and other health and welfare community agencies. The long-range thrust of the present statute is to make such grantee organizations look to the Federal Government for support. Their services to the community will then be dependent on governmental largess and the vagaries of the expenditure policy of the particular administration in power. Such a result is bound to be harmful and should be guarded against by correcting the statute now.

2. *The 6% minimum distribution requirement is not necessary in view of other provisions enacted by the Congress requiring that assets held by the foundation be productive.* As has already been indicated, the distribution of a reasonable yield annually for charitable purposes has been and can be accomplished under section 4942 by a minimum percentage more consistent with reality of yields on investment assets. One of the other reasons for the minimum distribution requirement was to prevent a private foundation from continuing to hold blocks of stock in a family business where such business interest was unproductive of a current yield. However, this matter is covered by section 4943 of the Code as enacted in 1969, which, in effect, require the divestiture of business holdings in excess of a certain minimum interest (20%) after taking into account holdings by disqualified persons.

3. *Experience since the enactment of the Tax Reform Act of 1969 has revealed weaknesses and inequities in the 6% minimum distribution requirement and demonstrated that it is not necessary for the accomplishment of the purpose of requiring reasonable and current distributions for charitable purposes.*

Fluctuations in the value of securities and yield since 1969 show how dangerous it is to attempt to fix a high rate of return and consider it as representative of what may be reasonably achieved by foundations. When the 6% figure was fixed in 1969 there was a good deal of talk that foundations should be able to produce such a yield, and perhaps even a higher yield, as a regular matter. Experience, in particular with the stock market, since that time indicates the wide fluctuations that can take place and particularly the danger of encouraging foundations to invest in securities for capital gains rather than in a balanced program seeking a reasonable return.

As the technical requirements in the 1969 Act come more and more under scrutiny, it is apparent that foundations will have to be prepared to distribute more than the minimum return requirements under the statute in order to operate without being subject to a penalty. The following is but a partial list of the problems which foundations face in seeking to make distributions which will at least equal the minimum return percentage requirement:

(a) Under the statute, apparently expenses paid or incurred for the production or collection of income or for the management, conservation, or maintenance of property held for the production of income do not reduce the amount required to be distributed for exempt purposes where the minimum investment rate of return requirement is applicable. Thus, a foundation which pays fees to investment counselors to help manage an investment portfolio must derive sufficient yield or gain on its securities, not only to pay such fees but also to pay out for charitable purposes the minimum return, say 6%, based on the value of invest-

ment asset This not only discriminates against foundations seeking professional help in making investments, but it also requires foundations to produce a yield in excess of 6%.

(b) In seeking to comply with the statute in making distributions, there are substantial risks whether all of the distributions constitute "qualifying distributions" as defined in the statute. These risks include (i) the matter of classification of grantee organizations, e.g., there are many that have not yet been classified by the IRS, (ii) the uncertainties that may be involved as to whether all of the requirements imposed under the statute in connection with grants to certain organizations are satisfied, which may be a matter beyond the control of the grantor (such as where, for example, several foundations make grants to unrelated organizations that may be private foundations and there is a question as to whether the grantee private foundation distributes all of such grants as well as all of its income for charitable purposes and whether it makes sufficient reports of the same to the grantors), and (iii) uncertainties which exist as to whether certain assets are classified as investment assets or assets held for exempt purposes.

Anyone reading the regulations published by the Treasury Department will recognize that there are a great many pitfalls involved in attempting to meet the minimum distribution requirements because of the uncertainties that exist at every turn in the application of the law.

For the above reasons, foundations are generally advised to produce more than the minimum investment return and to distribute more than the minimum investment return in order to allow for expenses which are not deductible and a margin of error in computing the minimum investment return as well as qualifying distributions. No one knows how large the allowance for margin of error should be but, to be on the safe side it is certainly necessary for a foundation to be prepared to produce and distribute more than the minimum 6%.

Experience shows that the net effect of all of the above factors is that private foundations must be prepared to produce and distribute more than the minimum rate of return requirement and that this accentuates and aggravates the counterproductive effect from a charitable standpoint of the 6% requirement.

RECOMMENDATIONS TO REDUCE THE MINIMUM RATE OF RETURN

A number of proposals have been introduced in the Congress to reduce the minimum rate of return from 6% to a lower percentage. Realistically, if the purpose of the Congress is to provide for a reasonable rate of return for distribution to charitable organizations, the percentage should not be higher than 4½%. The Secretary of the Treasury should continue to have the authority to adjust the percentage in accordance with interest rates in relationship to those prevailing in 1969.

Legislation has been introduced which would make the maximum percentage 5% and it would provide an extended transition period before the 5% goes fully into effect. The Congress should promptly enact such legislation in order to maximize the use of the charitable funds for public purposes. Even a 5% minimum requirement will, for reasons stated above, result as a practical matter in distributions in excess of that figure. Accordingly, Congress need have no fear that reducing the figure from 6% to 5% will seriously reduce the amount of funds available for current use by public charitable organizations. Rather the opposite should be true because it will permit privately supported foundations to invest more wisely and distribute their funds on a reasonable basis and thereby provide continuous support for charitable purposes.

ADDITIONAL RECOMMENDATION WITH RESPECT TO DISTRIBUTIONS FROM CERTAIN BUSINESS HOLDINGS

There is an inconsistency between the policy reflected in section 4942 and that in section 4943, relating to certain business holdings of foundations. While, in general, section 4943 limits the holdings of a private foundation in a business enterprise to a twenty percent interest, the Congress recognized in 1969 that it was necessary to provide certain transitional rules in order to permit foundations with holdings in excess of the permitted percentage a reasonable period of time to reduce such holdings in order to prevent a sacrifice or losses on divestiture. Thus, the statute, in section 4943, provides for three phases during which business holdings are to be reduced. This period of time, depending on the circum-

stances, will extend from ten years to thirty-five years and possibly longer. In addition the Congress provided a minimum period of five years in which to dispose of excess business holdings received by gift or bequest.

The realistic transition rules under section 4943 are undercut by the provisions of section 4942, which include business holdings among assets on which the 6% minimum distribution requirement is to apply. In many cases such business holdings do not produce a 6% return and hence the impact of section 4942 is either to require a disposition of the business holdings prior to the transition period afforded under section 4943 or else to require a foundation to make distributions out of other assets, which is a result completely inconsistent with the intent of Congress to encourage diversification of holdings. Accordingly, there should be recognition in section 4942 of the policy reflected by the transition rules in section 4943.

For these reasons it is recommended that section 4942 be amended so that the minimum rate of return requirement does not apply to investments permitted to be held during a transition period provided under section 4943. For such holdings the minimum distribution requirement should be the actual earnings on such holdings. This can be accomplished by an amendment of section 4942(e) adding a provision to the effect that the minimum distribution percentage shall not be applied to any interest held in a busineses enterprise during the period such interest is, pursuant to section 4943(c)(4)(B) or (6), treated as held by a disqualified person rather than by the private foundation. In lieu of the minimum percentage being applied to such interest, the foundation should be required to distribute the amount of the income realized by it in the taxable year from its interest in the business enterprise. This would apply to the same principle as that stated in Section 17 of HR 8214, which has already been reported by the Senate Finance Committee and recommended by the Treasury Department.

IN DEFENSE OF FOUNDATIONS, STATEMENT BY HAROLD S. MOHLER, LEHIGH UNIVERSITY

I want to make some observations about foundations and some misconceptions about them which seem to be so widespread today. I claim no special expertise on this subject but I believe the time may be overdue for some board presidents and some university presidents to set the record straight from their point of view. Foundations were established by thoughtful and generous people to help their fellow men. They are now being treated as though they have done just the opposite.

In a general way, most of us have some idea of the effects of the Tax Reform Act of 1969 upon foundations. I would like to comment upon two requirements of that law, among the many new restrictions that have been imposed. These two requirements are the excise tax imposed and the minimum distribution or pay-out schedule.

Foundations must now pay a four percent excise tax on net investment income. Two things disturb me about this. First, total grants of foundations are reduced by the amount of the tax, which means, in effect, that the tax is being contributed by colleges, hospitals, churches and other similar groups. On this point, William H. Baldwin, the distinguished president of the Kresge Foundation, says:

It cannot be said too often that the four percent excise tax paid by foundations inevitably comes out of the pockets of potential foundation beneficiaries and that a lowering of the presently excessive rate would not benefit the foundations but their applicants.

Second, while the total amount of the tax collected would be a meaningful addition to charitable enterprises, it is an insignificant sum in terms of the national budget. In the three and a half years following the passage of the Tax Reform Act of 1969, $157.6 million was extracted from foundations by this tax. With about $42 million spent for foundation audits by the government, this means that some $115 million has been moved into the Treasury coffers instead of into charity.

Foundations must now distribute an increasing proportion of their assets, starting at four and a half percent back in 1972 and going up to six percent in 1975 and thereafter. One of the results of this requirement has been that some foundations have been forced to invade principal in order to make the required distributions. Another result has been that some foundations, and some major

ones, have been forced to change their investment portfolios in an effort to insure an average return of six percent. Even an unsophisticated investor will quickly recognize that this requirement "is somewhat too high for prudent management of endowment funds," to quote Alan Pifer, president of the Carnegie Corporation of New York.

These onerous developments, which are being forced upon foundations, come at a time in our history when the extent of misunderstandings about foundations is appalling. There is still a popular conception that foundations are enormous concentrations of wealth. This is simply not true. For example, the total assets of all foundations represent only about one-third of the *annual* budget of the Department of Health, Education and Welfare. Another misconception is that foundations dominate private giving. Again, this is not correct. To illustrate, in 1972 the total of all foundation grants amounted to only 9.7 percent of the total of all private giving. In fact, this proportion of giving has remained relatively constant during the last fifteen or twenty years.

The principal fact we ought to remember about foundations—and the feature we all should fight to preserve—is their freedom and flexibility to act promptly to meet human and social needs. Often their grants provide "seed money" or "venture capital" which will then attract individual or possibly public support. In other cases their grants provide an initial impetus to a project which, in turn, will attract the support of many, many others.

The Seeley G. Mudd Building is a perfect example of this. The generosity of the trustees of the fund is making possible the fulfillment of this urgent need. Trustees, alumni, friends, corporations and other foundations are not only stimulated by this generous act but they are also moved to do likewise so that the full cost of this great project can be underwritten.

In a day when it may not be fashionable to stand up for private enterprise and private philanthropy, I urge each of us to bring whatever influences we can to halt the constant erosion in the private versus the public sector of financial support. Through our businesses, our educational institutions, our representatives in government and our community organizations, our efforts should be unending to preserve the integrity of our private institutions. And foundations are a precious and necessary part of such private institutions.

Dr. Robert F. Goheen, former president of Princeton University, testified forcefully on this subject before the House Ways and Means Committee. In part, he said:

"A new climate of opinion is now merited, one which recognizes the capacity of foundations to help meet important human needs . . . it is time for Congress to show that it considers foundations a national asset and that it wishes to give encouragement to their activities."

I commend this point of view to all of us who have a deep interest in the future of higher education.

THE DUKE ENDOWMENT,
New York, N.Y., July 22, 1973.

SENATE FINANCE SUBCOMMITTEE ON FOUNDATIONS,
Washington, D.C.

COMMENTS ON SECTIONS 4940 AND 4942

GENTLEMEN: The following statement is submitted by the Duke Endowment, a special purpose private foundation which supports four universities, non-profit hospitals and child caring institutions in North and South Carolina and United Methodist churches in North Carolina.

1. The Endowment believes that the large tax imposed on major foundations under section 4940 is not justified if the tax is truly intended only to meet the Internal Revenue Service's costs of auditing foundations. The Duke Endowment pays about $1,000,000 a year in tax under section 494. It pays its own independent auditors about $15,000 a year to make a complete audit of its books. Assuming the Service's cost of auditing the Endowment's return are comparable to the costs of the independent auditors, in doing the same work, the disparity between those costs and the tax is enormous and it is the universities, hospitals, churches and child caring institutions which The Endowment supports that are deprived of the revenue.

We recognize that the larger foundations must pay a higher tax than the smaller ones because it takes a greater number of man-hours to audit the former

and because a time charge could represent a large portion of or even exceed the income of some small foundations. At the same time it should be realized, first, that the tax is essentially a fee designed to offset the cost of auditing the particular private foundation and, second, that the beneficiaries of the larger foundations, who ultimately bear the tax burden, are no less deserving than the beneficiaries of the smaller ones. The New York State Legislature apparently recognized these considerations in establishing a fee schedule in connection with the filing of annual reports by charitable organizations ranging from $10 on charities with less than $50,000 of net worth to $250 on those with over $10,000,000 of net worth. We suggest that the same considerations apply in the case of the section 4940 tax and propose that there be a ceiling on the section 4940 tax of perhaps $50,000 or $100,000.

2. Our primary interest is in reducing the section 4940 tax as suggested above. We have, however, certain other comments on the section in its present form.

Although the definition of investment-related expenses in section 4940(c)(3)(A) follows almost verbatim subsections 212(1) and (2), which have been the subject of extensive interpretation, its application in the foundation context is quite unclear. An examination of the information returns of a large number of foundations reveals that apparently similar expenses have been treated in very different ways by different foundations; for example, salary, rent, overhead and professional fees have been treated by one foundation as almost entirely 4940(c)(3)(A) expenses, by other foundations as almost entirely administrative expenses. Moreover, we understand that Revenue Agents have been as unsure of the proper application of that subparagraph as the foundations and its application has consequently been inconsistent. The problem of allocation is, as a matter of fact, still open in a pending audit of the 1970 and 1971 returns of The Endowment.

It is submitted that section 4940(c)(3)(A) should be amended to provide a clear guide to foundations, accountants, lawyers and the Internal Revenue Service as what expenses are investment-related and what administrative.

3. One of the principal purposes of the private foundation segment of the Tax Reform Act of 1969 was to increase the flow of money from private foundations to active charities. The allocation of overhead, professional fees and grant-making costs to administrative expenses achieves the opposite result.

In section 4942(g)(1)(A) Congress provided that administrative expenses not related to the earning of income or the management of investments shall be treated as if they were distributions to charities and, consequently, any expense which falls into the category of administrative expense reduces the amount which must be paid out to active charities. Congress at the same time enacted section 4940, calling for a 4 percent tax on net investment income to offset anticipated audit expenses. Net investment income equals gross investment income minus expenses related to the earning of income or the management of investments, that is, all expenses other than administrative expenses and capitalized or otherwise nondeductible expenses. If a given expense is categorized as administrative, the pay-out to charity is decreased and the tax is increased, whereas if the expense is categorized as investment related, the payment is increased and the tax decreased.

If it were merely a question of whether charity or the Treasury received an equal amount from a foundation, the problem would probably not be serious. However, sections 4940 and 4942, taken together, provide a different result: if income is equal to or less than minimum investment return, *for every $25 of expense allocated to administrative expenses, the Treasury gains $1 and charity loses $26.*

Example: A private foundation has investment assets worth $5,000,000 and the required minimum investment return under section 4942 for the year in question is 6% or $300,000. Its gross investment income consists of dividends and taxable interest of $300,000 and it has salary, rent, overhead and professional fee expenses of $25,000. If all expenses were treated as being investment-related, the section 4940 tax would be $11,000 and its required pay-out to active charities under section 4942 $289,000. If all expenses were treated as being administrative, the section 4940 tax would be $12,000 and its required pay-out to active charities under section 4942 $263,000. Thus, an increase of tax of $1,000 would cost the charities $26,000.

We propose that all foundation expenses be classified as section 4940(c)(3)(A) expenses except expenses incurred in connection with active charitable operations

or in providing goods or rendering services to active charities. We believe that only those "program" types of expenses which a school, hospital, church, museum or other active charity would normally bear should be classified as administrative expenses and treated in the same way as distributions to charity. All other expenses (except capitalizable and improper or otherwise non-deductible expenses) should be considered as part of the costs of "doing business" and should be deductible under section 4940(c)(3)(A). Specifically, we feel that expenses of a foundation in investigating, selecting and making grants to active charities should be deductible under section 4940.

Respectfully submitted,

THE GEORGE GUND FOUNDATION,
Cleveland, Ohio, July 22, 1974.

Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee,
Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: It is our understanding that The Honorable Vance Hartke, Chairman of the Senate Finance Committee's Subcommittee on Foundations, has invited written comments for the record on Sections 4940 and 4942 of the Internal Revenue Code. As a foundation executive for many years with this Foundation and previously with The Ford Foundation, I am pleased to respond on the basis of my personal experience and observations in general relative to philanthropic activities.

The present 4% excise tax is clearly an indirect tax on the hundreds of educational and charitable institutions to which we make grants, by simply deducing our available grant funds. While the valuable auditing function of foundations by the Internal Revenue Service involves increased operational expenses for IRS, it is my understanding that the 4% excise tax generates annually three to four times the additional IRS expenses. This would seem to indicate the appropriateness of a substantial reduction in the 4% rate.

I believe, also, that the basic principle and desirability of taxing philanthropic agencies in general should be raised in relation to this provision. Prior to 1969, taxation of such agencies was not considered in the public interest because of the broadly beneficial services provided. The present 4% excise tax seems to me discriminatory against foundations and establishes a principle which, in time, may well be extended to other types of philanthropic agencies, both donors and recipients.

The minimum distribution of net investment income requirement for private foundations has and will undoubtedly continue to result in the demise of many foundations. Depending on general investment conditions and inflation rates, the 6% distribution requirement anticipated in 1975 could well have the effect over the years of substantially reducing the assets of many, and perhaps most, foundations. While I subscribe to a minimum distribution requirement, I believe that under presently foreseeable conditions it should be no higher than 4–5% of assets or net income if higher.

Thank you for providing this opportunity to express my views on the two above provisions which are of great importance in the future role of foundations and philanthropy generally in our country.

Sincerely,

JAMES S. LIPSCOMB,
Executive Director.

FENNER FAMILY FUND,
New Orleans, La., July 15, 1974.

Re: 4 Percent Excise Tax.

Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee,
Dirksen Senate Office Building,
Washington, D.C.

DEAR MR. STERN: I understand from the press release dated July 1st that Senator Hartke has invited written public comments on the above matter.

The Fenner Family Fund, of which I am President, is a small foundation—assets approximately $50,000—and it stands to reason that the 4 percent excise tax serves no purpose for the Government and it constitutes a nuisance to the foundation. Last year, for example, it amounted to only $176.00.

The so-called Tax Reform Bill of 1969 which instituted this excise tax has acted as a discouragement to small foundations such as mine because of the nuisance tax and because of the requirement that "in kind" donations must be sold and distributed by the end of the first quarter of the succeeding year.

This has prevented me from building up the foundation when I had the opportunity to do so, and inasmuch as all of the funds from the Fenner Family Fund go toward private education it can be said that the Tax Reform Bill has been at the expense of those institutions. This applies also to the 4 percent excise tax because it reduces by that much the amount the foundation can donate each year.

I think it is clear that the Treasury Department was ill advised in the anti-foundation regulation that they passed in 1969 and I sincerely hope that the matter is being intelligently reviewed so it will reach those who use foundations, but not force those who provide funds for private education to pay an unreasonable penalty.

Sincerely,

DARWIN S. FENNER,
President.

SAUNDERS, CURTIS, GINESTRA & GORE,
July 17, 1974.

MR. MICHAEL STERN,
Staff Director, Senate Finance Committee,
Dirksen Senate Office Building,
Washington, D.C.

DEAR MR. STERN: This letter is being sent after learning of the request of the Honorable Vance Hartke for members of the public to comment on Sections 4940 and 4942 of the Internal Revenue Service Code.

The undersigned presently is a trustee of two small private foundations and, also, trustee of a third which will eventually have in its portfolio approximately Ten Million Dollars when said foundation is completely funded.

The foundations which I represent are as follows:

1. The Dameron Scholarship Foundation, established in memory of two of the children of Doctor John Dameron who were unfortunately killed several years ago when run down by a speeding automobile as they alighted from a public transportation bus.

The principal foundation, approximately $7,000 was contributed by myself and a few members of the medical profession in Broward County.

The sole purpose of this foundation is to provide annually a scholarship to a female student at Cardinal Gibbons High School here in Fort Lauderdale and a female student at Saint Coleman's Parochial School in Pompano Beach, who otherwise would have financial difficulty attending the schools. Awards are made annually upon the recommendation of the schools' principals and consists of a 50% split of the foundation's income to each of the two schools. This income is understandably of small consequence to the Internal Revenue Service, but of great consequence to the recipients. The 4% excise tax on such a small foundation serves no real purpose as far as the Federal Government is concerned and the same can be said of the minimum required distribution of income earned which seldom reaches 6%. To require invasion of principal to meet this tax and minimum distribution would only reduce the meager scholarships presently being awarded to less meager sums.

2. The second foundation on which I also serve is The Stephen Gore Trust for the Florida State School for the Deaf and Blind which trust was originally established many years ago by my now deceased father and consists solely of stock in a family corporation which he controlled. It was established in honor of my eldest son who attended this school at one time as a deaf student.

The sole purpose of the foundation is to benefit the students of the school, both deaf and blind to the extent they cannot receive aid from the State. Each year the entire net income is distributed to the Student Assistance Fund maintained by the school for medical treatment, furnishing of hearing aids and travel expenses for students whose parents cannot afford the same. Tuition, boarding and books at the school are furnished free of charge to all Florida residents.

I am advised by the school principal that the income of the foundation is well put to use, and they could use additional income, if and when, it becomes available. Fortunately, in my father's will, a further bequest was made to this school,

but the bequest will be in cash or other securities which will not be disqualified as were the original securities.

As concerns this foundation, my objections are the same as for the previous foundation, with, the additional objection that the current law places on the foundation an obligation that cannot be met. That condition is the requirement that where the foundation holds more than 2% of the issued stock of a corporation, the stock must be disposed of within a required period of years. As stated above, the original contribution consisted of stock of our family corporation and currently slightly exceeds by a fraction above the allowed 2% holdings. The problem presented to the trustees, under the current law, is as was stated by myself to the Internal Revenue agent when the foundation was audited for the year 1972, "How can the trustees be required to sell that which is not saleable?" As to the stock of the family corporation, none of the present stockholders have indicated a desire to increase their holdings nor can the corporation be required to redeem the stock held by the foundation. Further, no outsider would be interested in acquiring such a small minority interest in a closely held company where he could not possibly have representation on its Board of Directors.

The present capital of the foundation approximates $130,000 and will be increased by $47,000 when the bequest is received from my father's estate.

3. Finally, the third private foundation which I represent was established also under the Will of my now deceased father and is to be funded by an annual sum equal to 5% of his adjusted gross estate for a period of 14 years. The foundation was established shortly after my father's death and has received its first annual funding in the amount of approximately $700,000. Similarly contributions or funds will be made annually for the 13 years remaining so this foundation will eventually have in it approximately Ten Million Dollars, but none of it will be controlled stock or other prohibited assets.

This foundation was established principally to benefit handicapped children, by the award of direct scholarships to enable them to advance as far as possible up the educational ladder to make themselves self-sustaining and a benefit to society. Secondary beneficiaries are handicapped children, the aged and affirmed who will need medical attention for which they cannot pay. A third beneficiary is Holy Cross Hospital, but only to the extent of $100,000, and this money must be used in the expansion of its Pediatric's Ward. Further, and the final tier of beneficiaries are non-handicapped children who can use scholarship assistance and other charitable organizations who themselves qualify under Section 501(c)(3) of the Code and are deemed worthy of beneficial help by the foundation's trustees. This latter foundation will distribute its entire income to these above worthy stated causes, but there is no guarantee that the income will equal the required minimum distribution which under the current law will necessitate invasion of principal.

It is easy to understand that as in the previous instances Section 4940 and 4942, can have a detrimental effect on the worthy purposes and persons to be directly benefited by this foundation. The 4% excise tax will directly reduce the number of handicapped children who could otherwise be benefited and any encroachment of principal required to make the minimum distribution, will have the same effect only on an annual compounded basis. This foundation specifically prohibits the accumulation of income and requires that all income be distributed to the stated charitable purposes.

In closing, I can well understand Congress' desires to raise the most amount of revenue and to prevent the abuses by Foundations which have occurred in the past, but I see no reason why honest, charitable foundations which actually and directly serve the public welfare should in any way be penalized.

I might add that the 4% investment tax in each of the above foundations takes sustenance from the mouth of babes, and serves the Federal Government no real useful purpose in doing so. If there were more honest and charitable private foundations as the three above mentioned, the welfare burden now facing both the Federal and State Governments could be greatly reduced. There are better ways of overseeing the operation of private foundations without the penalty and anti-charitable provisions of Sections 4940 and 4942.

In my humble opinion, both of these provisions should be repealed or, at the least, limited in their application to foundations whose assets exceed Twenty-Five Million Dollars.

Sincerely,

GEORGE H. GORE.

P.S. No administration expense is incurred by the first two foundations, and cannot exceed 5% per annum in the third.

FEILD CO-OPERATIVE ASSOCIATION, INC.,
Jackson, Miss., July 18, 1974.

Re: Sections 4940 and 4942 Internal Revenue Code, as pertains to the 4 percent Excise Tax and Minimum Distribution Requirements of Foundations.

MR. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

GENTLEMEN: The Honorable Vance Hartke, Chairman of the Senate Finance Committee's Subcommittee on Foundations has invited "those interested" to make comments on the two captioned sections.

Our foundation, Feild Co-Operative Association, Inc., was begun in 1919 as an educational foundation and has operated in that capacity continuously since its founding, and in so doing approximately 15,000 young men and women through Feild financing have attained a college degree, and in many instances a post-graduate degree. The student (race, creed or color has no relevancy with us) borrows money from Feild on an open promissory note (a life insurance policy is taken out on the student's life with Feild as the beneficiary as its interest may appear). Our percentage of repayment has been extraordinarily high.

Feild does not now nor has it ever made a solicitation of capital funds. Feild now has capital assets (at cost) of approximately $2,840,000.00. These assets were derived basically from the original contributions and the realized increases thereon, most especially in Feild's first years.

The above is given to you as a preface for these below comments:

It is not probable that our capital assets can experience any detectable increase as the tax laws now stand—and realistically, with inflation running at an uncontrolled rate, it is logical to assume that there is now and will continue to be a diminution of our capital asset-dollar value. As the laws now stand we divest ourselves, less a percentage of our operating expenses, of all of our income—4% in Excise Tax plus a statutory minimum as a payout requirement of net investment income.

Our concern lies less with the increase in capital assets than it does with the preservation of our capital assets. Even so short a time as a year ago, our fund then was almost exactly as it is now—our effective dollar value was far greater than it is today, thanks to the ravages of inflation.

We fail to see the logic in the reduction of the Excise Tax without a similar reduction in the payout requirement. Some remedy would be granted if the realized capital gains were freed altogether from the Excise Tax provisions.

We do not quarrel with the basic idea that a foundation should serve its cause for being by making substantial distribution of its net income. We do quarrel with the extent and the degree to which, by statute, we are required to make distributions and we do seek and strongly urge that some relief be granted to private foundations in their payout requirements.

Very truly yours,

H. C. MCGEHEE,
President.

THE COLLINS FOUNDATION,
Portland, Oreg., July 15, 1974.

MR. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

MY DEAR MR. STERN: The present study being made by the Senate Finance Subcommittee on foundations relative to Sections 4940 and 4942 of the Internal Revenue Code is of utmost importance to the health of all service agencies in the United States which are dependent upon grants to enable them to carry on their work on behalf of the philanthropic causes in America. I am in an unusually objective position to recognize the effects of portions of the 1969 Tax Law as they affect the support which can be made available from private foundations for education, welfare and charitable programs in our country.

For 28 years I served as a college president of a small private college which literally cannot have existed had it not been for the help that came from the private sector in philanthropy. Today we are seeing one after another of these institutions which have served so nobly, now being forced to close their doors. Any decrease in the available dollars for education will further complicate their problems.

In the last five years, it has been my privilege to work as administrator in this private foundation which, for a quarter of a century, has been investing all of its income in the educational, religious, scientific, health and welfare programs of the State of Oregon. I have already seen during this period the increase in demand for such help during a time when inflation has reduced our capital and legislation has reduced our expendable income by the four per cent which the Government has taken.

I would strongly urge that the Committee give serious consideration to reducing the tax on income of foundations by at least fifty per cent. At the same time, it is urgent that another look be given to the maximum which we face in required disbursements under the law. The six per cent requirement is unrealistic over a long period of time without invading capital which has already been depleted by inflation. I would urge that this requirement be reduced to four and one-half to five per cent.

The Congress of the United States should be most sympathetic to the need to preserve the present private foundations for the work and the contribution they have made and to take steps to again encourage the addition of resources through gifts to these foundations and through the creation of new foundations which have been sadly depleted in recent years.

I strongly urge the favorable consideration of the Committee on Finance in these matters with the proper recommendations to the Congress for correction of some of the influences of the 1969 Tax Law.

Sincerely yours,

G. HERBERT SMITH,
Administrator.

E. S. DEWEY,
Boston, Mass., July 15, 1974.

DEAR MR. STERN: While I am in favor of minimum distribution of net investment income that is required for large private foundations. I am opposed to it for small ones.

I am a trustee of the Laura Stratton Dewey foundation with use of its $70,000. While looking for an area to make a meaningful contribution I am forced to give $3,500 a year for what I call "band-aids." I would think that it would be in the public interest to exempt those foundations with assets of less than $250,000 from the required income distribution.

Very truly yours,

E. S. DEWEY.

THE WESTERN NEW YORK FOUNDATION,
Buffalo, N.Y.

MR. MICHAEL STERN,
Staff Director, Senate Finance Committee,
Dirksen Senate Office Building,
Washington, D.C.

DEAR MR. STERN: As President of The Western New York Foundation, I am responding to the invitation of The Honorable Vance Hartke (D., Ind.), Chairman of the Senate Finance Committee's Subcommittee on Foundations, to provide a written public comment for the record on Sections 4940 and 4942 of the Internal Revenue Code.

With reference to the 4% excise tax, I have reviewed previous audits for the years 1972 and 1973 and find this tax amounted to ½ of 1% of the charitable distributions of 1973 and 1% of the charitable distributions of 1972. The reason for the smaller percent in 1973 was due to a substantially larger charitable distribution than required in the Internal Revenue Code, but made available by action of the Board of Trustees of the foundations. While this tax certainly could not be considered punitive, certainly every dollar that is withdrawn from the available income of a foundation reduces the effectiveness of the resources of that foundation on the community it serves. Without any factual basis it has been estimated in this community that loss to the community through this tax approximates $50,000 per year which of itself may not seem substantial but there are a number of organizations that have requested foundation funding that have

an annual budget of far less than this amount and thus could have been completely subsidized for an entire year or more from this fund.

I should now like to discuss briefly the minimum distribution of net investment income required of private foundations. Certainly one of the main purposes of this provision of the Internal Revenue Code was to urge foundations to look for investments of better return and therefore hopefully more stable. As this net investment income requirement has been tied to interest rates prevailing during the year under review it has very strongly persuaded foundation managers to attempt to reach for higher yields on their investments. In many cases such high yields can be far more dangerous from a management point of view than investments with less yield. Many corporate securities have above average yield available simply because there is distrust in the management's ability to continue these payments and thus the investment may be suspect for a good cause. The other side of this foundation's concern regarding the minimum distribution of net investment income has to do with the trustees' ability to continue to operate this foundation in a constructive manner for the fullest benefit of the community it serves. The year 1974 to date has provided an excellent example of the punishment that will be forthcoming to the foundation field if interest rates continue to remain at high levels and the market place for common stocks does not improve. Under these circumstances the minimum distribution of net investment income to a foundation will be substantial. It will be even substantially above that required by the Treasury in its most recent payout determination. As all of this interest earned must be paid out as distributions, there is no possible way for the foundation to build its capital base as it could do if it invested its assets in the common stock of American companies, for with this type of investment capital appreciation would be shielded from the minimum distribution and would provide a base for future increased income as the company builds its own earning base. The picture is not dissimilar with private foundations to that of corporations were they required to pay out all their earnings after taxes as dividends to their shareholders or be taxes on any earnings retained. This penalty on a profit making corporation could well stifle the growing capabilities of that corporation for there would be no retained earnings for capital growth which hopefully would provide for additional earnings.

The Western New York Foundation Trustees do not consider the foundation to be a liquidating asset that will through the years finally disappear as all of the assets are disposed of, but they consider more likely the role of the foundation one where its size in assets will grow at least as rapidly as the needs of the community in which it serves so that it will continue to be approximately as valuable today as it was 10 years ago and will be about the same 10 years hence. The Trustees feel a very strong obligation not to withdraw from the private foundation field and thus leave the many needy causes without this source of funding. Certainly it could be said another private foundation or some government subdivision can certainly pick up where a foundation leaves off. This may be so but it does not seem a realistic course. Under the present laws it is very doubtful that new foundations of size will come into being in the numbers they have in past years and if government will step in when the private sector withdraws and can do the job with as much invention and courage as the private source then why foundations at all. Past experience has shown that a good partnership between private philanthropy and government funding has produced the best results. Government by its very massiveness cannot have the blindman's touch to a social problem that a relatively small, local, private foundation can have. If these sensitive areas are to get assistance foundations such as The Western New York Foundation must not only continue but must continue to keep up with the cost of providing services as well as growing with the community they are serving. I trust that the foregoing will be of some constructive value to the Senate Finance Committee's Subcommittee on Foundations and to its Chairman, The Honorable Vance Hartke. If I can be of any further service in providing additional information to this Committee I will make every effort to do so.

Very truly yours,

WELLES V. MOOT, JR.,

ZALE FOUNDATION,
Dallas, Tex., July 16, 1974.

Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee,
Dirksen Senate Office Building,
Washington, D.C.

DEAR MR. STERN: We believe that the 4% Excise Tax on "investment income" should be reduced because a substantial amount of money is being denied to various operating charities.

In its consideration of the TRA–69, the Senate voted for an audit fee tax of one-tenth of 1% of a foundation's assets. Not only was that rate equivalent to roughly half of the 4% investment tax subsequently arrived at by the Joint House-Senate Conference Committee and enacted into law, but the Senate version had previously tied the rate to the costs of administering the new law. *We Recommend* that the rate be set again at a level closer to the actual auditing and supervisory costs, that it be earmarked for that purpose, and that the tax be redesignated as a fee for auditing and supervision.

This 4% excise tax is levied on "net investment income." In defining "net investment income," the Act includes realized long-term capital gains. A substantial percentage of the $76 million collected by the IRS from this tax during 1973 was from the 4% tax on investment income per se. As foundations are forced to sell capital assets, either to meet the pay-out requirements of Section 4942 or the divestiture requirements of Section 4943, the amounts available to charity are further reduced by the levying of this 4% tax on capital gains. *We Recommend* that the definition of "net investment income" in Section 4940(c) be modified to exclude capital gains as an income item.

Sincerely,

MICHAEL F. ROMAINE, Ph. D.,
Executive Director.

MARY L. PEYTON FOUNDATION,
El Paso, Tex., July 15, 1974.

Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee,
Dirksen Senate Office Building,
Washington, D.C.

DEAR MR. STERN: As executive director of a private operating foundation that assists individuals in need, it distresses me that we must pay a 4% tax to the government. This amounted to $6,922.00 last year. Since we spend all of our income, it means holding back aid to people in need.

What is so ironic is that most of the persons we help are in need because the government has fouled up their S.S.I., Social Security, G.I. or V.A. checks.

This Foundation has not been audited since the Tax Reform Act and we have paid in $14,737.80 in three years.

I am very much in favor of a minimum distribution of net investment income, but I am opposed to the 4% excise tax. A tax is all right, but 4% is much too high for us.

Sincerely,

MONICA A. HUNTER,
Executive Secretary.

ORSON A. HULL AND MINNIE E. HULL
EDUCATIONAL FOUNDATION,
Saint Paul, Minn., July 16, 1974.

Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: The Honorable Vance Hartke, Chairman of the Senate Finance Committee's Subcommittee on Foundations, has invited written public comments for the record on sections 4940 and 4942 of the Internal Revenue Code. I take great pleasure in the opportunity to make comment insofar as these two sections of the Code affect the Orson A. Hull and Minnie E. Hull Educational Foundation of which I am one of the trustees.

First, with relation to the 4% excise tax, I do feel that at the present rate this is a revenue producing tax which I believe it was not intended to be. I do feel that adequate funds should be gotten from the foundations to pay for the cost of reviewing the activities of the foundations. What the rate of assessment should be can now be determined after this past year's experience.

However, relative to section 4942 regarding a minimum distribution of net investment income, this foundation was started in 1963 with a gift of 18,000 shares of Minnesota Mining & Manufacturing Company common stock. The will creating this foundation required that the income be used to help financially needy, worthy high school graduates who were well qualified and had a desire to go on to college but were financially unable to do so. At the time of its creation Minnesota Mining dividend amounted to about 2% of its market value but had excellent growth potential. The trustees of the foundation felt that it would be to the foundation's advantage to sell part of the Minnesota Mining stock and reinvest in higher income producing securities and as a result over 50% of the 3M stock was sold and reinvested.

The trustees felt that it was good for the foundation, in order to keep up with inflation, to retain some growth stock as well as retaining good income producing securities, but it has been very difficult to accomplish this to the extent required by the minimum payout section of the Code. In other words, to have the advantage of common stock with growth potential plus the advantage of income producing securities with very little growth potential, has not been an easy goal to attain.

Speaking for myself and not for the foundation, I do not feel that private foundations whose assets do not include any closely held stocks, especially stocks of companies owned by the foundation creator, should be penalized by a harsh minimum payout rule.

I do believe that private foundations have a very important and valuable place in the welfare of our country and should be encouraged and not discouraged, and I am personally convinced that a harsh minimum payout requirement is very discouraging to the foundation managers and directors whose foundations are so badly needed in their community.

Very truly yours,

ARNOLD F. STROMBERG.

THE JOHN HUNTINGTON FUND FOR EDUCATION,
Cleveland, Ohio, July 17, 1974.

Re sections 4940 and 4942 of the IRS Code.

MR. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: As President of the John Huntington Fund for Education, which has been supporting education in the Greater Cleveland area for over 50 years, the Trustees and I do take exception to the provisions in Sections 4940 and 4942 of the I.R.S. Code to impose a 4% excise tax on income (including capital gains), as well as requiring a rather high minimum distribution of income—as a percentage of principal.

I do not believe it fair for any tax to be made, other than that required to police private foundations. We know that there have been some foundations who have used their tax-free status for their own personal good. However, in our case, the only expenses to the Foundation are less than 5% which includes the major item of excise taxes recently, legal expenses and a very minimal staff. The Trustees and Officers do not, of course, receive any remuneration for their work, except for two or three luncheons a year. The staff comprises an Executive Secretary on a part-time basis, and a Secretary-Treasurer (a lawyer) to take care of legal and tax matters, period.

The 4% excise tax on capital gains restricts our flexibility in handling our portfolio—to the detriment of hundreds of students receiving grants, scholarships, and/or loans from the Fund.

We are also against a percent of principal minimum distribution, since this again will restrict our program of buying and selling equities and fixed income securities.

Although we previously supported over 600 students with scholarships, now we support 10 to 12 local institutions and scholarship handling organizations to assist

the needy and worthy students in the Greater Cleveland area to obtain a good education, both at the college level, as well as post graduate work—with proper emphasis on the minority students' welfare.

In closing we strongly hope that the Honorable Vance Hartke, Chairman of the Senate Finance Committee and his Subcommittee on Foundations will delete the 4% excise tax or at least cut it to a feasible amount and give some flexibility as to the distribution of our net investment income.

Very sincerely,

A. DEAN PERRY.

PETER WESTON,
WESTFIELD, MASS, *July 18, 1974.*

Re: Senate Finance Committee, Subcommittee on Foundations.
Mr. MICHAEL STERN,
Staff Director, Senate Finance Commitee,
Dirksen Senate Office Building,
Washington, D.C.

DEAR MR. STERN: Senator Hartke has solicited public comments on Internal Revenue Code sections 4940 and 4942.

Under section 4940 a 4 per cent excise tax is imposed on net investment income of a private foundation. I feel this tax is excessive. In 1973, $76 million was collected by I.R.S. under this section. In 1972 $56 million was collected. I understand that some of the increase may be due to selling off of excess holdings by some large foundations. The I.R.S. estimated its fiscal year 1973 costs of operation for all exempt organizations to be $18.6 million. The costs for private foundations was $12.3 million. At best then, the I.R.S. could probably justify a tax rate of 1.62 per cent on the low side or 2.2 per cent on the high side under section 4940. The amount which is being collected in excess of what is being spent by the I.R.S. is money which is lost to worthy recipients of foundation grants.

The Minimum Payout Requirement under section 4942 of the Internal Revenue Code is also excessive and perhaps unnecessary. It is my fundamental belief that the many should not suffer for the sins of the few. Most people involved in private foundation work are responsible individuals. Another consequence of the Minimum Payout Requirement is that it tends to force managers to shovel money out to qualified organizations regardless of need because they incur a tax liability if they don't.

Thank you for your interest in my comments.

Sincerely,

PETER WESTON.

DEAR MR. STERN: I am writing in regards to Senator Hartke's invitation for public comment on tax laws affecting private Foundations.

I do not know what sections 4940 and 4942 of the internal revenue code encompass, as this information is not available to me. I do know that some Foundations enjoy a tax status that they do not deserve.

I do not see any reason the Foundations should not be taxed on their stock manipulations or any other wheeler-dealings, that they use to build up personal fortunes.

Some Foundations should not have the tax status they now enjoy, for the fact that grants paid out are self serving and benefit too few people.

All Foundations should be investigated and any Foundation that is granting or using money for movements or causes contrary to the Constitution of the United States and the Freedom of the American people, should lose their tax free status and be saddled with heavy tax laws.

Sincerely,

GEORGE G. WIARS.

THE WILLIAM G. IRWIN CHARITY FOUNDATION,
San Francisco, Calif., July 18, 1974.

Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee,
Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: According to a Press Release, The Honorable Vance Hartke, Chairman of the Senate Finance Committee's Subcommittee on Foundations, has invited written public comments for the record on Sections 4940 and 4942 of the

Internal Revenue Code. In response to Senator Hartke's invitation, I have the following comments:

Section 4940—Excise Tax on Investment Income

It is strongly recommended that the excise tax be reduced to a rate which would not produce revenue in excess of the cost to the I.R.S. of auditing private foundation returns.

It is also suggested that provision be made for a carry-back and carry-forward of capital losses to offset capital gains. Lacking such a provision, taxing of capital gains is a one-way street.

Section 4942—Taxes on Failure To Distribute Income

A minimum investment return of 6% appears to be unrealistically high. A 5% rate is more in the ball park.

Sincerely,

JAMES L. COCKBURN, JR.,
Secretary.

ALBERT KUNSTADTER FAMILY FOUNDATION,
Chicago, Ill., July 15, 1974.

Re: Subcommittee's work on code sections 4940 and 4942.

Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: In my opinion the 4% excise tax is excessive. It would appear that a tax on the approximate cost basis would seem reasonable, although any tax reduces grants to worthwhile organizations.

I thoroughly disagree with the provision for minimal distribution. While investigations did show that there were some abuses in accumulating capital as well as controlling businesses, these factors were insignificant in comparison with what foundations have done to benefit the socio-economic conditions of this country.

For the past ten years our foundation has consistently distributed more than its income to qualified organizations. There are several important reasons for our disliking the distribution clause:

1. The dividends in many progressive companies, which employ many people in gainful occupations, are less than the percentage required for distribution under the present law. This forces the sale of capital assets which are needed for future grants.

2. In any given year it may be sound judgment to hold back some income in order to expand a grant in the following year to an organization which originally had requested larger funds but had to prove its worth to the granting foundation. We understand that if a commitment is made for three years with a payment made for only one year the balance is reflected under unpaid grants on the books of the foundation.

Foundations are such an important factor in the development of our country that I hope careful consideration will be given to our point of view.

Sincerely yours,

SIGMUND KUNSTADTER,
Chairman.

ALEX. C. WALKER EDUCATIONAL & CHARITABLE FDN.,
Pittsburgh, Pa., July 18, 1974.

Re: Federal Foundation Sub-Committee—4% Excise Tax and Minimum Distribution Requirement.

Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: This is a personal response to the above subject and not a response representing our Foundation necessarily.

1. *The 4% Excise Tax*—My understanding of this tax when levied was to provide monies for surveillance of the operation of private foundations. This, I think, is in order but anything over and in excess of that which is needed to do this job should be returned to the foundations and only a tax in the future needs

to be imposed to properly regulate the operations of private foundations. A suggested way of handling this would be the same way you handle the minimum distribution and that is to set the percentage each year. That money not needed in any particular year for surveillance purposes should warrant a credit to the foundations or a corrective percentage rate levied each year.

2. *The minimum distribution requirement*—I understand the principle of this was to make sure that operating foundations that accumulate funds were to distribute essentially all of what they earned within a reasonable length of time. This may impose hardship on some foundations. I see no objection to this except that if the percentage rates were made excessively high then some foundations couldn't properly attain it because of their portfolio structure, it would mean that the balance of the percentage would have to be supplemented by reducing its capital to make up that difference.

I would hope that the Foundation Sub-Committee is cognizant of the fact that the present law pertaining to public and private foundations is extremely complex which makes it not only difficult to interpret the law but also to enforce it. I would hope the Committee would be mindful of attempting to eliminate some of the law and/or streamlining it so that it is much more simple.

Yours truly,

T. URLING WALKER,
Trustee.

ORDEAN FOUNDATION,
Duluth, Minn., July 17, 1974.

MR. MICHAEL STERN,
Staff Director, Senate Finance Committee,
Dirksen Senate Office Bldg., Washington, D.C.

DEAR MR. STERN: We appreciate the invitation of the Honorable Vance Hartke for the opportunity to submit a statement to be included in the Senate Finance Committee's Sub-committee on Foundation hearing record.

Ordean Foundation of Duluth, Minnesota has functioned as a 501 (c) (3) organization since 1933.

During the many years of its operation it has disbursed several million dollars which have directly and indirectly benefited thousands of the community residents.

Since 1965 the Foundation has also made grants to organizations providing the following services in our Community which has a population of 100,000:

1. The treatment, care and rehabilitation of persons who are chronically or temporarily mentally ill;

2. The treatment, care and rehabilitation of persons whose physical capacity is impaired by either injury, illness, birth defects, age, alcoholism, or other similar causes;

3. The conduct as one of their functions of youth guidance programs designed to avoid and prevent delinquency from lawful and healthful pursuits by youthful citizens of the City of Duluth.

Ordean Foundation currently has an annual income of approximately $500,000 which results in an excise tax of approximately $20,000 on the present basis. Such a sum represents several modest grants which cannot now be made for the above purposes. Inasmuch as the records indicate that the 4% excise tax has resulted in collecting more funds than required to audit and monitor Foundation activities Ordean Foundation hereby wants to go on record recommending that said tax be reduced to only 2% of a Foundation's net investment income.

Thank you for making the above statement a part of the Sub-committee's hearing record.

Sincerely,

J. HOWARD ALASPA,
Executive Director.

THE ALICE T. MINER COLONIAL COLLECTION,
"A HISTORICAL MUSEUM",
Chazy, N.Y., June 3, 1974.

MR. KYRAN M. MCGRATH,
Director, American Association of Museums.
Washington, D.C.

DEAR MR. MCGRATH: I am on the board of two historical museums and fully well realize how difficult it is for such museums to maintain a balance between income and expenses. At the same time, however, I feel it is imperative that.

museums submit their records to close audit and scrutiny by the Department of the Treasury in order to insure that such institutions may be able to continue to justify the favorable tax privilege which has been afforded them by the Congress of the United States. To that objective, I must state my firm conviction that the museums should be required to pay an amount equal to the cost of conducting such an audit. I do not believe this expense should be borne by the public out of general tax revenues but rather should be borne by those continuing to sponsor and support such an institution and/or from the fees paid by those using such institutions.

I suspect the present 4% excise tax represents a levy greater than required to recover such costs. I would not, however, favor total repeal thereof.

Very truly yours,

RODNEY B. LUNDY,
Vice President.

THE KRESGE FOUNDATION,
Troy, Mich., July 11, 1974.

Senator VANCE HARTKE,
Senate Office Building,
Washington, D.C.

DEAR SENATOR HARTKE: You have asked for comments from foundations about Internal Revenue Code Sec. 4940 (4% excise tax) and IRC Sec. 4942 (distributions of income), and we offer the following observations:

(A) *As to the 4% excise tax:*

Ideally, the 4% excise tax should be replaced by a foundation audit fee based on size of assets which could be similar to fees charged for audits for banks and savings and loan associations. Absent such a possibility, the 4% tax should be reduced to 1% or 2% as to ordinary income. Collections for 1972 and 1973 were far in excess of the cost of audit and both the Treasury Department and Internal Revenue Service agree that this is so. A 1% or 2% excise tax would more than suffice to provide the requisite funds for audit. In addition, it is our strong opinion that the excise tax should be eliminated entirely as to long-term capital gains. For example, on May 15, 1973 we paid a total of $5,711,190 with respect to the 4% excise tax for calendar year 1972. Of this amount, about $5,140,000 was attributable to 1972 realized capital gains resulting from a major secondary offering of capital gains resulting from a major secondary offering of S. S. Kresge Co. common stock. This secondary distribution was engaged in solely to diversify our holdings and to increase our rate of return since we have never had an excess business holdings problem. The fact is that there are a number of foundations, like ourselves, who are subject to the minimum investment return portions of the Tax Reform Act of 1969 and hold large (but not excess) business holdings which produce a modest dividend. In order to lessen the invasion of corpus occasioned by the pay-out requirements, a number of us had secondary distributions in 1972 and invested the net returns in higher yielding securities. In view of the fact that the 4% excise tax on ordinary income produces an amount which is five to six times the required amount for treasury foundation audits, it seems unduly harsh to our potential foundation beneficiaries to add to that amount. I am sure you understand and know that the lowering of the 4% excise tax rates and the elimination of the tax on capital gains would not benefit us but our applicants since whatever is not paid in tax would have to be paid out in qualifying distributions.

(B) *As to the pay-out requirements of sec. 4942:*

We consider that the minimum investment return provision, when coupled to present high inflationary factors, results in unwarranted deterioration of the effective levels of Foundation giving. Having fixed pay-out requirements makes us especially aware of any contraction in the purchasing-power we extend by way of grants to our applicant. This Foundation made a study of what would have happened had the maximum 6% pay-out rate been in effect since our beginning in 1924. While there would have been a comparatively modest increase in total grants over the forty-nine year period, the income-producing assets of the Foundation would have been drastically reduced by reason of invading principal to make the required distribution. That there will be a short term increase in benefits to the public is undeniable, but continued application of the present minimum investment return pay-out rates will seriously curtail these benefits for the long term. The answer to this problem, as in the case of the

excise tax, is reduction of rate. To be specific, in the year 1972 our appropriations for contributions were about $20 million and this meant an invasion of corpus in the amount of about $15,600,000. Similarly, in 1973 our appropriations for contributions were about $29,700,000 and this meant invading corpus to the amount of approximately $12,700,000. Obviously, this is particularly distressing at a time when the market is so depressed and inflationary rates are so terrifying.

I hope that you will believe me when I tell you that all the above suggestions, in my opinion, are for the long term interests of charity. As indicated, a reduction of the excise tax rate will be to the benefit of our potential beneficiaries since we will have to pay the money out in any event. Similarly, in my view, the preservation of our corpus will, in years to come, be to the best interest of all charitable organizations. The Foundation's sole donor, Sebastian S. Kresge, tithed on a grand scale leaving a personal estate at his death, in 1966, which was only one tenth of the book value of the gifts he made to the Foundation starting in 1924. Appropriations by the Foundation of approximately $175 million over fifty years amount to benefits which are treble the original gifts and, even in a depressed market, the Foundation's principal assets show an eleven-fold increase over the original donations. Such a long continued enhancement of the generous impulses of one man should, I think, be thoughtfully considered.

I shall be delighted to speak with you or any of your staff members about any of the points which I have raised and to document our point of view. In addition, we will be glad to answer any questions which you or any member of your staff may have about the points which I have raised or on any other point with respect to foundations and the 1969 Tax Reform Act.

Sincerely,

WILLIAM H. BALDEN,
President.

THE CHESAPEAKE CORP.,
West Point, Va., July 17, 1974.

Hon. VANCE HARTKE,
Chairman, Subcommittee on Foundations, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR SENATOR HARTKE: This letter is written in response to your invitation for written public comment for the record on Sections 49.40 and 49.42 of the Internal Revenue Code. As the unremunerated president of a Section 501-c-3 qualified private foundation, the Elis Olsson Memorial Foundation, c/o Carle E. Davis, 1400 Rose Building, Richmond, Virginia 23219, I take pleasure in submitting my thoughts on the two sections of the Code referred to above. The reference foundation has assets of approximately $1,000,000 and generates pretax income of between $37,000 and $44,000.

As regards the 4% excise tax imposed under Section 49.40, I do not feel this is an unfair reimbursement for the expense the Government incurs in ascertaining whether the operation of a foundation is proper or not under the existing law. I prefer the original name for this tax which was Auditing Fee since it more properly described the reason for the tax. Secondly, I see no reason why public foundations should not incur the same tax since if the Internal Revenue Service is performing its job properly an equal amount of auditing should be performed on the books of this second classification of foundations.

If it is the intention of Congress and the Internal Revenue Service, one through legislation and the other through regulation, to slowly but surely liquidate all private foundations, then this statement should be made in the preamble to Section 49.42 of the Internal Revenue Code for this most certainly will be the ultimate result as it stands today. If indeed Congress feels, as do I, that private foundations on the whole have performed most creditably in many areas where public money administration and public foundations have faltered, then Section 49.42 needs some clarification and it should provide a more realistic economic environment within which private foundations can function effectively and with a reasonable guarantee of being able to stay in business if properly operated. As I invisualize the situation, a continuing mandatory payout of 4¼ to 4⅜% could be made under most circumstances by a prudently directed investment program. When return on money or investment is low, there is little fear of inflationary erosion of the assets of a well run foundation. When money rates are high, such as at present, one may meet the higher percentage set by the Internal Revenue

Service as a minimum distribution; however, at this same time inflation is rapidly eating away at the investment portfolio value of the foundation and, thus, ultimate liquidation. It seems to me that no prudently-operated foundation can afford to be invested entirely in high yield fixed income securities for under inflationary conditions it is inherent that a substantial part of the high yield is to offset the inflationary effect on basic value. A mixed portfolio should minimize the chance of such circumstance happening. The average yield of a portfolio can be maintained to pay out a reasonable distribution to assist educational, health and other qualified charitable activities and still maintain the assurance that such foundation will be in business to continue helping in the future. I thank you for this opportunity to express the opinion of one small foundation.

Very truly yours,

STURE G. OLSSON.

THE BURROUGHS WELLCOME FUND,
Research Triangle Park, N.C., July 24, 1974.

MR. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: The Honorable Vance Hartke, Chairman of the Senate Finance Committee's Subcommittee on Foundations, has invited public comment for the record on sections 4940 and 4942 of the Internal Revenue Code.

In regard to the provision imposing a 4 per cent excise tax, it is our opinion that such a tax is too high as evidenced by the revenue collections versus the costs of the Internal Revenue Service services. We would favor reduction to the tax to a level sufficient to cover only the absolutely necessary costs of the Internal Revenuo Service services in this area. We would oppose further increases in costs as a result of the creation of a special agency and employment of additional numbers of persons.

Yours truly,

IRIS B. EVANS,
Executive Director.

STATEMENT BY GORDON A. MAC INNES, JR., EXECUTIVE DIRECTOR OF THE FUND FOR NEW JERSEY

The Fund for New Jersey is a grant-making foundation incorporated under the laws of New Jersey. The Fund is a 501(c)(3) tax-exempt organization held to be a private foundation under the Tax Reform Act of 1969. On December 31, 1973, the market value of The Fund was $16,330,698. In 1973, The Fund made grants totaling $1,434,751.22.

As its name implies, The Fund concentrates its grant-making on organizations operating in or for the benefit of the state of New Jersey. More than one-half of its dollars are contributed for research and policy analysis, citizen action, and litigation on the many problems found in New Jersey. Over the past four years, The Fund has initiated a number of projects which have resulted in the creation of organizations to deal with problems which heretofore had not received sufficient attention.

The 4% Excise Tax. In the first four taxable years since the enactment of the Tax Reform Act of 1969, The Fund has paid $88,120. in excise taxes. It was the clear intent of the Congress, in enacting the Tax Reform Act, that this tax should cover costs of auditing the regulating private foundations. We are informed that the actual cost incurred by the Internal Revenue Service since 1969 is appreciably less than the revenues collected for these purposes. The Fund does not object to a fee or tax to cover the reasonable cost of auditing private foundations. However, since the revenues generated by the 4% excise tax far exceed the cost of regulating private foundations, we recommend a reduction in the rate of the excise tax to no less than 1% and no more than 2%, depending on the actual cost requirements of the Internal Revenue Service. We urge this reduction for the following reasons:

1. The "excess" dollars collected by the Federal Government are dollars not used for charitable purposes. At a time when we must reject 15 applicant organizations for every one that we are able to assist, any additional dollars avail-

able to us would mean fewer discouraged applicants and, presumbly, a furtherance of the charitable objectives of the Federal tax laws. For example, if the excise tax had been set at 1%, an additional $66,000. would have been available for distribution to charitable organizations.

2. We believe a strong case can be made for the kind of grant-making practiced by The Fund for New Jersey. We concentrate on a single state, in which 8 of our 9 trustees reside. We are familiar with the many problems found in New Jersey and also with those organizations and individuals who bring unusual strengths to their solution. We assist a number of organizations which, by their nature, could never be assisted by government agencies. Specifically, we support organizations which provide a "watch dog" function to insure the prudent and proper operation of public agencies and regulatory bodies.

3. The excise tax rate can be reduced without jeopardizing the revenue needs of the Federal Government. To the foundations which pay the tax and to the charities which would otherwise receive these dollars, it represents an important marginal loss—to the Federal Government, it represents a *deminimus* source of revenue.

Minimum Pay-out Provision. The Fund supports the requirement that foundations distribute a set minimum of their net investment income to qualified recipients. We have found the minimum percentage set by the Secretary of the Treasury for existing foundations to be reasonable. We believe that the minimum distribution requirement encourages a prudent investment policy of diversification and reliance on the total-return concept. Moreover, this provision discourages creation of entities appearing to be charitable but intending to make only token contributions to charity.

It is ironic that the same Federal law which encourages the maximization of contributions to charitable organizations on the one hand would also—through the 4% excise tax—decrease the amount available for such purposes on the other.

THE JOHN RANDOLPH HAYNES AND DORA HAYNES FOUNDATION,
Los Angeles, Calif., July 23, 1974.

MR. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: This is being written in response to the Foundation's Subcommittee invitation for written public comments for the record on sections 4940 and 4942 of the Internal Revenue Code.

Any excise tax is defensible insofar as such tax is necessary to bear the expenses of implementing the Tax Reform Act of 1969 relating to foundations. However, an excise tax which exceeds the necessary costs of examining foundations and is imposed for revenue purposes is in conflict with the traditional policy exempting charitable activities from mandatory taxes.

Sincerely,

FRANCIS H. LINDLEY,
President.

ASSOCIATION OF AMERICAN COLLEGES,
Washington, D.C., July 26, 1974.

MR. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: This letter is in response to the Committee on Finance's press release of July 1, 1974, inviting public comments on sections 4940 and 4942 of the Internal Revenue Code.

We believe the excise tax on foundations should be consistent with the actual costs of auditing, based on experience to date. We support, therefore, the Treasury Department's position that the present 4% rate should be reduced to at most 2%.

We believe, further, the payout rate should represent a realistic balance between the long-range objectives of the individual foundations and an assessment of current needs in those areas which must rely on foundation support. A payout rate which would seriously diminish foundation resources would have a deleter-

ious effect on higher education which must continue to rely heavily on this source of support. Foundations have never been more needed than today.

Thank you for this opportunity to present briefly our views.

Sincerely,

HOWARD E. HOLCOMB,
Executive Associate.

ROBERT S. ADLER FAMILY FUND,
Chicago, Ill., July 24, 1974.

Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: My attention has been brought to the fact that you have invited statements or comments regarding the 4% excise tax and minimum distribution requirement of the Internal Revenue Code.

This is merely to record my view and that of the trustees of this fund that the 4% excise tax works a hardship and is out of proportion, in our opinion, to the needs for which the tax was supposedly levied. We strongly urge you to take every action possible to recommend the reduction of that excise tax to a figure more in keeping with the needs.

With regard to minimum distribution, we do not find this too difficult a matter to comply with. However we do feel that the distribution ought not to be excessively high since this would force distributions in a given period of time beyond what might otherwise be deemed desirable to accomplish the purposes of the commitments of the fund.

Yours truly,

ROBERT S. ADLER,
President.

DARTMOUTH COLLEGE,
Hanover, N.H., July 24, 1974.

Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: I should simply like to record with you the official position of Dartmouth College in regard to Senator Hartke's Sub-committee's work on Code Sections 4940 and 4942.

We wholeheartedly endorse the position taken in testimony on behalf of the Council on Foundations.

Sincerely,

R. J. FINNEY, Jr.

THE ROCKEFELLER FOUNDATION,
New York, N.Y., July 25, 1974.

Comments on sections 4940 and 4942 of the Internal Revenue Code.

Hon. VANCE HARTKE,
Chairman, Subcommittee on Foundations, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR SENATOR HARTKE: We welcome this opportunity to respond to your invitation for comments on sections 4940 and 4942 of the Internal Revenue Code which impose a 4% excise tax and a minimum distribution requirement on private foundations.

SECTION 4942: MINIMUM DISTRIBUTION

Notwithstanding its long-standing policy of making distributions for charitable purposes substantially in excess of its investment income, this Foundation believes that the mandatory payout requirement under section 4942(e)(3) (fixed by the Secretary of the Treasury for tax years beginning in 1974 at 5.5% for foundations organized before May 26, 1969 and at 6% for those organized thereafter) is likely to destroy the ability of private foundations to support charitable programs at current levels.

For many years, this Foundation followed a policy of appropriating funds for grants, programs and administrative costs substantially in excess of its

income. Prior to the enactment of the Tax Reform Act of 1969 it adopted, and has since followed, guidelines for charitable expenditures equal to 5.75% of the average market values of its investments as of October 31 of the preceding four years. As shown in the following table, for the ten years 1964 through 1073 this self-imposed distribution requirement resulted in expenditures for charitable purposes of $395 million, or 33% more than the income from the Foundation's investments.

Year	Total expenditures	Ordinary investment income	Expended from principal
1964	$32,617,564	$27,276,570	$5,340,994
1965	30,313,583	29,137,115	1,176,468
1966	34,893,371	30,784,237	4,109,134
1967	36,349,416	32,188,393	4,161,023
1968	41,488,096	32,838,247	8,649,849
1969	38,720,739	31,977,066	6,743,673
1970	47,115,774	30,353,638	16,762,136
1971	45,377,628	27,947,105	17,430,523
1972	44,027,315	25,259,226	18,768,089
1973	44,446,015	28,915,860	15,530,155
Total	395,349,501	296,677,457	98,672,044

Although this Foundation has voluntarily made distributions at a level comparable to the statutory payout requirement, it would now be obliged, but for the mandatory requirement, to consider the effects of inflation and erratic investment conditions on its ability to continue distributions at such a level.

In 1969, when the Tax Reform Act was under consideration, the recent history of inflation rates, and prevailing expectations concerning future rates of inflation, were in the range of zero to 3%. The requirement for a minimum payout based upon average market value, and related to a 6% rate under 1969 economic conditions, seemed reasonable, based upon an assumption of a 9% total return on investments, a 6% payout, and 3% inflation.

At the current time, however, worldwide rates of inflation have reached or exceed 10% per year. These increases have greatly outstripped any prudent long-run investment returns and have indeed borne a marked negative correlation to the value of equity investments. While it is true that bond rates have risen in the wake of mounting inflation, it would be unrealistic to expect sizable investment portfolios to shift from equities to bonds rapidly without serious trading losses and substantial transactions costs. It is therefore especially critical, given the current state of the country's and the world's financial condition, that the inflation factor be taken into account in arriving at a meaningful payout requirement.

In determining the payout requirement for 1974 and later years, the Secretary of the Treasury is required by section 4942 (e)(3) of the Code to take into account "the relationship which the money rates and investment yields for the calendar year immediately preceding the beginning of the taxable year, bear to the money rates and investment yields for the calendar year 1969." Although a comparison of money rates in 1973 to those existing in 1969 might be said to justify the recent increase of the payout requirement to 6%, a similar comparison of investment yields, taken on a total return basis, clearly indicates the need for a *reduction* in the payout requirement. The Secretary has not indicated what factors were deemed relevant in the determination of the payout requirement for any given year, and specifically whether any consideration was given to recent negative investment yields on equity investments or to the effect of inflation in comparing investment yields in question to those existing in 1969. In any event, the current administrative practice results in the imposition of a level of payout requirements which could lead to gradual liquidation of the charitable functions performed by private foundations.

At least for the foreseeable future, inflation is a fact of life that can no longer be ignored. From the point of view of private foundations, it has become a critical factor in determining the amount of annual expenditures that can safely be made without pertmanently damaging the effectiveness of their program activities. We respectfully recommend, therefore,

(1) that the Secretary or his delegate publish the formula used to determine the annual percentage of payout requirement;

(ii) that the Secretary or his delegate take into account total-return investment yields on equity investments as well as fixed income rates in determining the annual payout requirement; and

(iii) that the Code be amended to require that the Secretary or his delegate take inflation into account in determining the annual payout requirement.

SECTION 4940: THE 4% TAX

We favor reduction of the private foundation excise tax from 4% to 2%. The Committee is undoubtedly familiar with factors which favor such reduction. The fact that the anticipated revenue from such tax at the reduced rate of 2% will be more than adequate, even at current inflation rates, to defray the Internal Revenue Service's cost of auditing exempt organizations (the original objective of the tax) argues strongly for such reduction.

It is also important to note that the effect of any reduction in the minimum distributable amount as proposed in the first part of this letter would be offset to some extent by an increase in that amount resulting from a reduction in the excise tax, since under section 4942(d)(2) each foundation would be required to make distributions for charitable purposes in an amount equal to any savings in tax.

In the case of The Rockefeller Foundation, a reduction in the excise tax would provide a significant saving. The 4% excise tax has resulted in taxes on the Foundation for the last three years in the following amounts:

1971	$1,166,450
1972	2,010,943
1973	2,651,270

For all foundations, the estimated savings based on revenues derived from the 4% tax during 1973 would insure the availability of approximately $40 million per annum for charitable purposes at a time when many educational, scientific, and other charitable institutions in the private sector are finding it increasingly difficult to continue their programs at current levels.

Respectfully submitted,

JOHN H. KNOWLES, M.D.,
President.

BALL BROTHERS FOUNDATION,
Muncie, Ind., July 24, 1974.

MR. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: Regarding the Sub-Committee on Foundations, we would like to express our opinion of Sections 4940 and 4942 of the Internal Revenue Code. Section 4940, of course, relates to the 4% Excise Tax imposed on private foundations, and we understand that this tax is producing a revenue far in excess of the moneys needed to audit private foundations which was the original intent of the law imposing the tax. We feel that this excess should be going to charitable and educational organizations. This result would be achieved if the tax were lowered because then the private foundations would have additional funds which they are required to pay out to qualified charities.

Section 4942 dictates the amount of moneys the private foundation must distribute as being the greater of the adjusted net income or the minimum investment return. During the past two years that our foundation has been subject to the minimum investment return, we have had to pay out moneys from our principal fund as our actual adjusted net income from intangible securities and real estate did not meet the minimum investment return. For 1974 with the higher minimum investment return of 5.5%, we will have to take a greater amount from our principal assets and we do not believe that it was the intention of the Congress to force a steady depletion of private foundations. We feel that if the management of the foundation is doing a reasonable job of investing, then only the actual net income should be required to be paid out.

Very truly yours,

ALEXANDER M. BRACKEN,
Vice President and Foundation Manager.

GRANT F. NEELY,
Latrobe, Pa., July 22, 1974.

MR. MICHAEL STERN,
Staff Director,
Senate Finance Committee,
Dirksen Senate Office Building,
Washington, D.C.

DEAR MR. STERN: We appreciate the opportunity to comment on sections 4940 and 4942 of the Internal Revenue Code upon the invitation of The Honorable Vance Hartke, Chairman of the Senate Finance Committee's Subcommittee on Foundations. These two provisions impose a 4% excise tax and a minimum distribution of net investment income requirement on private foundations.

First, we would reinforce what many foundation spokesmen must have already said: private foundations have made and continue to make tremendous contributions to society and for the benefit of all mankind. Every dollar collected under section 4940 reduces the moneys available for charitable activities.

We do not have any particular quarrel with the minimum distribution requirement except that the percentage rate for the minimum investment return is geared to interest rates on debt investments rather than the actual average experience of bank, foundation and pension fund portfolios. We are now experiencing exceptionally high interest rates, some resulting from inflation and others intended to help control inflation. Portfolios balanced to provide both income and reasonable growth should not be measured solely by an interest rate yardstick. To meet excessive minimum distribution requirements means an invasion of a foundation's corpus or a continued churning of portfolio assets, either of which can jeopardize the foundation's future.

We respectfully request your consideration of a reduced excise tax to provide more funds for contributions and a realistic minimum investment return requirement in keeping with a well managed, balanced fund designed to provide moderate growth and a reasonable rate of return for current distributions of investment income.

Respectfully yours,

GRANT F. NEELY,
Executive Director.

KVIE, CHANNEL 6,
Sacramento, Calif., July 23, 1974.

MR. MICHAEL STERN,
Staff Director,
Senate Finance Committee,
Dirksen Senate Office Building,
Washington, D.C.

DEAR MR. STERN: I am writing to you about the Senate Finance Committee's Subcommittee on Foundations hearings on Sections 4940 and 4942 of the Internal Revenue Code.

As a working member of public television, I am very interested in helping foundations retain their funds to use for worthy causes. Among those causes is public television and our industry has benefited tremendously by receiving grants from foundations.

It would appear to me that foundations should be permitted to distribute their funds in accordance with their governing directives without the restrictions of additional taxes and minimum distribution of investment income requirements. My vote is in favor of removing these restrictions from foundations whose charter directs the foundation to good causes in the public welfare.

Very truly yours,

WALTER T. CARTER,
Director of Development.

KVIE CHANNEL 6,
Sacramento, Calif., July 23, 1974.

MR. MICHAEL STERN,
Staff Director,
Senate Finance Committee,
Dirksen Senate Office Building,
Washington, D.C.

DEAR MR. STERN: This letter is about the Senate Finance Committee's Subcommittee on Foundations hearings on Sections 4940 and 4942 of the Internal Revenue Code.

As a lay member who represents public television, I am very interested in seeing that foundations are able to retain their funds and use them for worthy causes. Public television as a whole has benefited tremendously over the past fifteen years.

In my opinion, foundations should be permitted to handle their funds in accordance with their by-laws without the restrictions of additional taxes and minimum distribution of investment income requirements.

I am definitely in favor of removing these restrictions from foundations whose charter directs their funds as an investment in the public welfare.

Sincerely,

MARILYN B. SHEARER,
Lay Representative.

KVIE CHANNEL 6,
Sacramento, Calif., July 23, 1974.

MR. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: I understand the Senate Finance Committee's Subcommittee on Foundations will be holding hearings on Sections 4940 and 4942 of the Internal Revenue Code in September.

As General Manager of a public television station and a member of the Board of Managers of the Public Broadcasting Service, I fully support the removal of restrictions caused by additional taxes and minimum distribution of investment income requirements for foundations.

I firmly believe foundations should be permitted to retain their funds to use for worthy causes—one of which is public television—and distribute them in accordance with their by-laws. There is no question that public television is deeply indebted to and has greatly benefited from grants received from foundations.

This is to confirm that KVIE fully supports removing these restrictions from foundations whose charter directs the foundation to invest in worthy public causes.

Sincerely,

ARTHUR A. PAUL,
Executive Vice-President and General Manager.

ROBERTS & HOLLAND,
New York, N.Y., July 19, 1974.

Senator VANCE HARTKE,
Chairman, Subcommittee on Foundations, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

Attention: Mr. Michael Stern, Staff Director

DEAR SENATOR HARTKE: This is in response to your invitation to submit written comments concerning sections 4940 and 4942 of the Internal Revenue Code. I testified before the Subcommittee on Foundations on October 2, 1973, and am pleased to submit additional comments at this time. Our comments are directed to the minimum investment return provision of section 4942 and, more specifically, to the procedure in section 4942(e)(3) for establishing the "applicable percentage."

Section 4942(e)(3) gives the Treasury Department the authority to set the rate which, when applied to private foundation investments, establishes the minimum amount that a foundation must distribute on an annual basis if income is less than such amount. The only standard provided by the statute is that the rate must rise and fall proportionately with "money rates and investment yields," and the Treasury Regulations merely repeat the statutory standard. Treas. Regs. § 53.4942(a)-2(c)(5)(i). For the reasons set forth below, it is apparent that this arrangement is unsatisfactory.

I. TREASURY PROCEDURE

By Treas. Info. Release No. 1288 (April 24, 1974), the Treasury Department announced without a public hearing that Rev. Rul. 74-288, 1974-21 Int. Rev. Bull, would increase the applicable percentage from 5.25% to 6.0% for foundations organized after May 26, 1969, and from 4.375% to 5.50% for foundations

organized before May 27, 1969. This year was the first in which the Treasury increased the applicable percentage.

The method by which the Treasury Department announced the current percentage was doubtful under the guidelines set by the Administrative Procedure Act. Section 553 of that Act requires the Treasury Department to give notice to the public of a proposed change in a substantive rule or regulations and prescribes a period of time during which interested and affected parties may comment upon the proposal. Underlying this requirement is the rationale that the Treasury Department, although acting in accordance with properly delegated authority, is performing essentially a legislative function where substantive rules and regulations are concerned and should be required to follow normal legislative procedures in such cases.

Nevertheless, the Treasury Department disregarded this procedure and set the "applicable percentage" by means of a revenue ruling with no solicitation of comment from the tax bar and foundation community. The establishment of such percentage cannot be included within the realm of the Treasury Department's "interpretative" functions. Case law in the area informs us that rules and regulations subject to the rule-making procedure of section 553 of the Administrative Procedure Act include those which implement existing law. That is the case here.

Moreover, although the Internal Revenue Service normally does not allow comment upon revenue rulings prior to issuance, there is authority for such a procedure in special cases. Rev. Proc. 72–1, 1972–1 Cum. Bull. 693, 695, permits the solicitation of comments on rulings during preparation where such a procedure is "justified by special circumstances." Revenue rulings are normally issued with respect to a stated set of facts, i.e., interpreting the law as applied to a particular case. This is not the case here, where virtually all foundations will be affected regardless of the facts peculiar to each. In view of section 553 of the Administrative Procedure Act and the Service's own Revenue Procedure governing the issuance of revenue rulings, we believe that the Service was obligated in this case to seek out comments on the proposed change from the tax bar and foundation community.

II. THE STANDARD ADOPTED BY THE TREASURY

Regardless of the propriety of the procedure followed in setting the applicable percentage, the Treasury did not use the prescribed standard. The substantial increase in the applicable percentage suggests that the standard used by the Treasury did not reflect the activity of "investment yields" but only the fluctuation of interest rates, despite the fact that the Treasury was compelled to delete the standard based solely on 5-year Treasury bills after a public hearing on the Proposed Regulations. Prop. Regs. § 53.4942(a)–2(c)(3)(i) (which were replaced by Treas. Regs. § 53.4942(a)–2(c)(5)(i)). Such a formula fails to take into account the "equity" side of foundation investment policy. Investment decisions with respect to corporate stocks are based upon market values and dividend expectancy, neither of which seems to have had any influence upon the Treasury's determination of the applicable percentage. Because foundations invest in equity securities, it is appropriate that the formula which sets the minimum investment return for these organizations should reflect activity in this sector of the investment market.

III. FOUNDATION EXPERIENCE

Recently market values of equity securities have declined while interest rates have continued to climb. The net result after the increase in the applicable percentage is that a foundation whose total economic return has decreased is nevertheless required to distribute more than was required in the past. This anomaly is the result of the Treasury Department's failure to use data pertaining to equity yields in determining the applicable percentage. Foundations in many instances are being required to distribute substantial amounts of corpus in order to meet the minimum distribution requirement, even though the conversion of this corpus into liquid form has caused them to incur capital losses. This is certainly not what was intended to occur when Congress enacted the minimum investment return requirement.

IV. CONCLUSION AND PROPOSALS FOR LEGISLATION

The failure of the Treasury Department to solicit public comment during the percentage-setting process might be corrected by litigation. But litigating the

issue would require substantial outlays of time and expense, would cure only the percentage set for a particular year, and would not solve the problem quickly enough. The best course is Congressional action.

We recommend that the following two changes be made in Code section 4942 (e) (3):

(1) The staute should expressly mandate the Treasury to give notice to and solicit comments from organizations which might be affected by a change in the applicable percentage. Such comment is necessary if the Treasury is to have knowledge of the real economic pressures in the foundation investment world and is to apply the proper standard in adjusting the applicable percentage.

(2) Congress should define more explicitly the standard to be relied upon by the Treasury in setting the applicable percentage. We suggest that such a standard might require the Treasury Department to use a specific formula, taking into account rates on Treasury bills, yields on corporate stocks and interest rates on corporate debentures. In such a case, again, foundation representatives should be permitted to comment upon a change in the applicable percentage pursuant to the statutory standard before such change takes effect.

Thank you for this opportunity to submit written comments on behalf of our foundation clients.

Respectfully submitted,

MALCOLM L. STEIN.

STATEMENT OF THE FORD FOUNDATION

COMMENTS REGARDING THE 4 PERCENT EXCISE TAX ON THE INVESTMENT INCOME OF PRIVATE FOUNDATIONS AND MINIMUM DISTRIBUTION REQUIREMENTS

The 4 percent excise tax

Section 4940 of the Internal Revenue Code, which imposes a 4% excise tax on the net investment income of private foundations, was added to the Code by the Tax Reform Act of 1969. That Act also imposed broad restrictions on the programs and financial activities of private foundations.

The legislative history of Section 4940, although not altogether clear, suggests a dual rationale for the tax:

First, both the House Ways and Means Committee and the Senate Finance Committee contemplated increased compliance efforts for the Internal Revenue Service in the exempt organization field and felt that costs associated with such a program should be borne not by tax payers generally but by the organizations whose activities required supervision. See H. Rep. 91–413 (Part I) 91st Cong., 1st Sess. 10 (1969), and S. Rep. 91–552, 91st Cong., 1st Sess. 27 (1969).

Second, the House Ways and Means Committee (but not a majority of the Senate Finance Committee) felt that private foundations should bear a portion of the costs of government. See H. Rep. 91–413 (Part I), 91st Cong., 1st Sess. 19 (1969).

Some may have supported the tax as a penalty because of past abuses of foundation status for tax avoidance or because of some questionable grants, or because of general antipathy to private foundations arising from the fact that particularly in recent years government has extended its own operations into areas previously served mainly by private charities. Nevertheless, the record can fairly be read to mean that most of those who supported the tax regarded it as either as a means of securing reimbursement for the costs of supervision, or as a general revenue measure.

We accept the first rationale, although this is the first time that the Federal Government has sought to recover from charitable organizations the costs of overseeing charitable giving. But we hope that the Congress will specifically reject the concept of a tax on philanthropy to be channeled to the general revenue

We invite attention to the following considerations:

1. The incidence of the tax falls not upon private foundations but upon those organizations that receive fundation support. Section 4942 imposes penalty taxes on private foundations which fail to make qualifying distributions for exempt purposes in the amount and at the time required by the statute. In general, the new law requires foundations to distribute their entire net income less the 4% tax.

The result is to reduce by the amount of the tax the amount which private foundations must distribute (generally by grants to other organizations and to individuals) in furtherance of their exempt purposes. Potential recipients of foundation support—not the foundations themselves—must thus bear the burden of the tax.

The urgent needs of public charities for funds underscore the practical consequences of a general revenue tax on foundations. The plight of schools and colleges in particular was (and is) so serious that many educational leaders felt compelled to testify against the tax in the 1969 Senate hearings. See Hearings before the Senate Committee on Finance, pp. 5857–5871 (October 6, 1969). The problems of virtually all charitable organizations today are even more serious than they were then.

2. Receipts from the tax far exceed the costs necessary for a vigorous compliance program by the Internal Revenue Service and are not earmarked in any way to offset such expenses. Although one principal purpose of the tax was to shift the cost of enforcement from tax payers to foundations, the tax has in fact served as a revenue producing measure. For fiscal 1973, collections of the 4 percent tax were in excess of $76 million, an increase of $20 million over collections reported for fiscal 1972. The Service has estimated its costs of operation for fiscal 1973 (based solely upon salary and benefits, without any allocation for space, equipment, supplies and travel) as $18.6 million for *all* exempt organizations and $12.3 million for private foundations alone. Thus, the costs incurred in administering all exempt organization provisions (and not merely those relating to private foundations) have been substantially less than one-half of the revenue produced by the tax. Since the revenue is not earmarked for the Internal Revenue Service through the use of a trust fund or otherwise, Section 4940 has become a revenue producing measure under which foundation beneficiaries (through loss of funds) are, in effect, subject to tax.

3. Until 1969, the Federal income tax law provided full tax exemption for all charitable organizations that met certain substantive standards of conduct. The four percent tax, viewed as a revenue producing measure which is imposed, ultimately, on charitable and educational organizations, is an unwarranted departure from this established policy. As Assistant Secretary Cohen told the Senate Finance Committee on September 4, 1969:

". . . a tax designed to raise revenue from private foundations cannot be justified once the other restrictions imposed on them by the bill have been enacted to insure that their funds will be used solely for charity. That is, there is no reason to reduce funds available for charitable activities by a tax once their exempt status has been justified in the first instance."

In 1969, Congress enacted a far-ranging series of provisions regulating the activities of private foundations. Since Congress has already acted to eliminate abuses and to insure that foundations will conduct their activities in a manner consistent with the public interest, we see no reason to reduce the funds available for such activities by a general revenue producing tax. We strongly recommend:

That Section 4940 be recast as an "audit fee" or "service charge";

That the amount of the tax be reduced to a level commensurate with its purpose.

Minimum Distribution Requirements

Section 4942 of the Internal Revenue Code, which contains certain minimum distribution requirements for private foundations, was added to the Code by the Tax Reform Act of 1969.

It is widely known that the Ford Foundation has regularly exceeded the statutory percentage payout requirements. The Foundation's Board of Trustees has been continuously determined to make full use of the return on the Foundation's resources for charity, and in recent years the Foundation has paid out sums well in excess of such requirements. We have never thought that payout should be limited to actual cash income on investments which may pay very low current dividends, although their long-run rate of return may be much higher.

At the same time, and in the spirit of constructive suggestion, we should report that there is reason to anticipate some improvement in understanding of the payout question over the next year or so. This improved understanding is much needed because there are serious questions about some of the assumptions concerning attainable long-run rates of return that were current in 1969. Past discussions on this subject have often lacked a hard base in statistical data

about the actual rates of return achieved by all classes of investors over long stretches of time.

Better information than was available during the drafting of the Tax Reform Act five years ago is now being developed by independent and disinterested actuaries and economists. We hope that the Subcommittee on Foundations will avail itself of any such new studies as it continues to consider the payout question.

JAMES G. K. MCCLURE EDUCATIONAL AND DEVELOPMENT FUND, INC.,
Asheville, N.C., July 25, 1974.

Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: As Secretary of the James G. K. McClure Educational and Development Fund, Inc. of Asheville, N.C. I would like to go on record as requesting a reduction in the 4% excise tax imposed on the investment income of private foundations.

Although the official reason given for the imposition of this tax was to cover the cost of auditing private foundations, the actual cost of such auditing as reported by the Internal Revenue Service is far below the 4% figure. The effect of the 4% tax is to reduce the amount of income which foundations are able to distribute to worthy philanthropic causes.

Most of the resources of the James G. K. McClure Educational and Development Fund, Inc. are devoted to college scholarships for young people from the mountain counties of North Carolina. As a consequence of having to pay the 4% excise tax on investment income, the Fund is unable to give scholarships each year to several deserving and needy boys or girls from Western North Carolina who want to get a higher education.

We respectfully request the Committee's approval of a reduction in the 4% excise tax on the investment income of private foundations.

Sincerely,

JAMES MCCLURE CLARKE.

THE BROWN FOUNDATION, INC.,
Houston, Texas, July 25, 1974.

Mr. MICHEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR SIR: In response to the invitation to the public by the Honorable Vance Hartke, Chairman of the Senate Finance Committee's Subcommittee on Foundations to make written public comments for the record on Sections 4940 and 4942 of the Internal Revenue Code, we submit the following brief observations.

Since the 4% excise tax imposed under Section 4940 applies only to those foundations classified as private foundations, the cost of audit and review of all tax exempt organizations is assigned to such private foundations, which we believe comprise some 13% of the total tax exempts. It is therefore heartening to find the Treasury supports reduction of the 4% excise tax to 2% which seems more than adequate to cover the IRS 1974 exempt organization budget of approximately $21.1 million. We trust this will receive the favor of the Subcommittee, the Committee and the Congress.

Though we agree that a private foundation should be expected to disburse all its income in carrying out its exempt purpose, the minimum investment return provision and the expense and problems relative thereto are more difficult to understand. Maintenance of a balanced portfolio in marketable securities providing a modest hedge against inflation and also producing some income is not likely to yield 6% on market value. A move in either direction from such balance has elements of self destruction. It would seem that a minimum investment return of 3% to 4% would be more realistic for those trying to maintain a prudent investment program.

Sincerely,

MERRITT WARNER,
Executive Administrator.

UNITED STATES STEEL FOUNDATION, INC.,
Pittsburgh, Pa., July 23, 1974.

Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: In response to the invitation extended by the Hon. Vance Hartke (D., Ind.), Chairman of the Senate Finance Committee's Subcommittee on Foundations, to submit written comments for the record on Sections 4940 and 4942 of the Internal Revenue Code, the following points are presented for consideration.

The imposition of a 4% excise tax upon net investment income (the substance of Section 4940) in order to generate funds for auditing foundation activities seems inappropriate when applied to corporate foundations. Certainly, corporations and their affiliates are among the most carefully and systematically audited entities in our current society. Not only does Congress require corporations to employ independent public accounting firms for audit purposes but federal and state bodies of all sorts, ranging from the IRS through a veritable network of bureaucracies, are also engaged in this process of public scrutiny. One result of this insistence upon public disclosure, therefore, is an atmosphere of scrupulous attention to the established legal safeguards. The stated objective of IRS audits of corporate foundations therefore is somewhat analagous to the provision for a backup system of a backup system. Not only does it represent managerial overkill, but in the aggregate, it undermines the purpose of the Congress in passing tax legislation designed to encourage corporate voluntary support of private sector activities by skimming off significant sums of money which might otherwise be applied to highly social ends. We have learned that in the most recent fiscal year, the tax produced by Section 4940 aggregated some $76 million (much of it undoubtedly from corporate-related foundations), compared with the $13–19 million needed to administer the program; a social loss of between $57 million to $63 million for a society already burdened by inordinately high tax rates, both direct and indirect.

The flaws apparent to this observer in Section 4942 relate to the fact that by establishing a tax on the undistributed income of a corporate foundation, the Congress violates a basic economic budgetary principle of spending in times of low income and accumulating offsetting deficits during times of high income. Stated differently, adherence to the spirit of Section 4942 would suggest that when society needs corporate or general philanthropic support least, at a time that market conditions and presumably other economic indices such as employment are up, foundations are almost compelled to distribute their earnings. Conversely, when the economy is functioning poorly (low earnings, increased social need) foundations are encouraged to adopt a stance of reducing their level of involvement in support of social needs. It was to counter this reverse mechanism that corporate foundations were organized in the first place.

Hopefully, these comments will be useful.

Sincerely,

JAMES T. HOSEY.

CARRIER CORPORATION,
July 26, 1974.

Attention: Mr. Michael Stern, Staff Director, Subcommittee on Foundations, Room 2227.

Hon. VANCE HARTKE,
U.S. Senate, Dirksen Office Building,
Washington, D.C.

DEAR SENATOR HARTKE: Carrier Corporation, as do many of this country's more enlightened corporations, commits part of its resources annually to worthy charitable causes. Solicitations for such contributions greatly exceed the sums available for this purpose and the Corporation avails itself of its private foundation to accomplish an orderly and level distribution of these funds to causes which Carrier recognizes as its obligations to the community. Carrier Corporation Foundation, Inc., which is of the simple "pass-through" type, enables the corporation to avoid situations with prospective donees by accepting their requests without commitment and referring them to the Foundation.

Chapter 42 of the Internal Revenue Code has placed unnecessary burdensome recordkeeping and reporting requirements on our type of foundation which,

when viewed in light of actual tax cost (and threatened tax costs due to rigid non-compliance rules), threatens the viability of such an organization as a means of carrying out charitable objectives.

More specifically, it appears from a Treasury study that the 4% excise tax on investment income imposed by Section 4940 of the Code exacts from foundations far in excess of the original legislative objective of financing the Internal Revenue Service's cost of supervising the requirements of Chapter 42. It is proposed that this tax be substantially reduced within the prescribed bounds or, more reasonably, be completely eliminated with respect to "pass-through" private foundations.

With respect to the 15% tax imposed by Section 4940 of the Code for failure to distribute income, it is proposed that the rule requiring the distribution of a minimum investment return based on a percentage of fair market value be radically liberalized or completely eliminated to relieve this rule's undue pressure on foundation portfolios already suffering from an extremely adverse securities market. Favorable modification of this rule will enable foundations to maximize their charitable contributions more effectively.

Respectfully submitted,

EDWARD J. FITZSIMMONS,
Director of Taxes.

ECONOMOS & ALEXANDER, LTD.,
Chicago, Ill., July 30, 1974.

HON. VANCE HARTKE,
Chairman, Committee on Finance, U.S. Senate, 2227 Dirksen Senate Office Building, Washington, D.C.

DEAR SENATOR HARTKE: In response to your request for comments on Sections IRC 4940—excise tax and 4942—minimum distribution requirement, we submit the following comments.

With reference to IRC Section 4940, the undersigned believes that it would be desirable to change the classification of any payment in the form of an excise tax to a fee to be known as an "Annual Audit and Examination Fee". The fees paid each year should be accumulated in a trust fund for the purpose of covering the cost of administering the audit program of private foundations. At the end of two years the Congress and its committee should review the balances, if any, in this trust fund. Then adjustments with respect to the fee charged for this service should be revised to cover the cost of this program.

On the basis of present statistics, it is quite conceivable that a fee of 1% may reasonably cover the cost of the audit programs required by the TRA Act of 1969. The sums collected under this program should not be made available for general revenue purposes.

As to IRC Section 4942 and its requirements for a minimum distribution of net investment income, it is suggested that the annual percentage for distribution be reduced for all private foundations to not more than 4% for the next five years. The difficulty in achieving a total return from equity investments will continue for some time. The economists vary in their predictions as to the time when equity investments will yield a reasonable rate of return. Most private foundations with equity investments have suffered a substantial loss in their investment portfolio and this, of course, has reduced the yield. They should not be required to dispose of equity investments at a loss in order to make up a minimum distribution out of principal. The net effect of this will be to postpone the distributions for the charitable purposes contemplated by the IRC and the TRA Act of 1969 to a later period. This obviously is a policy decision and one which requires a careful adjustment of the percentage rates applied to private foundations.

Sincerely,

JAMES P. ECONOMOS.

JAMES C. DUDLEY,
New York, N.Y., July 15, 1974.

HON. VANCE HARTKE,
Chairman, Senate Finance Committee,
Senate Office Building,
Washington, D.C.

MY DEAR SENATOR HARTKE: When your Subcommittee on Foundations considers sections 4940 and 4942 of the Internal Revenue Code, I urge that it consider the plight of the small family foundation resulting from the crippling requirements of the laws promulgated since 1969.

Guilford Foundation was established by members of the Dudley family in the mid-sixties in order that the young members of the family be trained in the management of their affairs and of their lives in such a way so that they would recognize their obligations to their fellow men and accept their responsibilities to their communities. By means of regular conferences and reports, they have participated from a very young age in the decisions to make grants. As they mature their judgment also has been sought in matters pertaining to policy of management of the assets and, in time, it was and remains the intention to vest them with the major over-all responsibilities involved.

I must say that their response to this concept has been extremely rewarding in that they have taken a lively initiative from the start and, after nearly ten years of organized effort to elicit their concern for others, have formed habits and attitudes of citizenship which already are of value to the world in which we all live.

Another purpose in establishing Guilford was to create a fund which would even out the ability of the family to support deserving causes, lessening that dependence upon the state of family finances, and providing assurance that programs once started could be completed.

Guilford Foundation began very modestly, from contributions which I could spare from year to year, and until recently, when it was funded from a legacy, was never as large as $100,000. Now it is about twice that large. Its grants have in most years exceeded its investment income, usually by a very considerable amount. The grants themselves, with one exception, have not been unusual. They include local agencies such as churches, hospitals, youth groups, schools, libraries, community funds, museums, conservation, community service organizations and the like, most of which if not all have no access to Federal financial support but all of which add in their individual ways to the quality of life for the average person in the community. Nationally it has made grants to service and health organizations, colleges, medical research and conservation organizations.

Its one innovative project, and by far the largest undertaking, has been the establishment of The Center for Family Studies in Duluth, Minnesota. The Center is itself an operating foundation under the code and is actively exploring and testing means to strengthen the family unit in America, a unit which the Trustees of Guilford consider is under serious pressure to dissolve and whose further dissolution would be detrimental to the quality of life in this country. The Center has been funded totally from Guilford since its inception two years ago and is now sufficiently advanced so that it will seek shortly participation from much larger foundations and institutions. It is hoped and planned that in another two years time The Center will be largely independent of need of Guilford's support at which time another major project of a different nature is contemplated. Neither effort, up until now, has received attention from Federal agencies although The National Foundation for Mental Health has expressed interest in the work The Center has been accomplishing.

If you will forgive me for describing Guilford's reasons for existence and activities in this detail, I will come to the point of this letter. The changes in the Revenue Act in the last five years have imposed serious burdens on enterprises such as this one. I am sure that your committee is aware of the wholesale going-out-of-business of small foundations, either by merger or dissolution, following the new regulations. Some undoubtedly were intended by Congress to be dissolved because their existence served only personal goals but many, many more have been terminated because they were unable to afford the legal and accounting expenses imposed upon them by the new laws, not to mention the added taxes, and a great many trustees (Guilford's included) have been periodically baffled by the extremely complicated requirements of the laws themselves.

I am a trustee of quite a number of institutions, large and small, which have depended more or less entirely upon private support. The disappearance of the small family foundation has very materially hurt the effectiveness of these by constricting their reliable access to funds. In at least two cases I am aware of, this has resulted in the seeking and obtaining of Federal aid which would otherwise have been unnecessary.

I, for one, am not sympathetic with the contention made by some that government grant is more appropriate and in the better interests of society than private concern, for it is self-evident that no government could be large enough to be able to correctly sense the needs of each individual community and its people.

Private responsibility is therefore vital to do the work that improves the lot of a government's citizens in the degree required and to discourage its citizens from

private concern and private contribution, as the recent regulatory changes have already done on a grand scale, constitutes a huge disservice to those citizens.

Please, therefore, strive to ease the burden Congress has placed upon foundations and private charity and refrain from driving the concept of personal concern for one's fellowman still further from our lives. Your children and mine can ill afford to lose these principles.

Respectfully yours,

JAMES C. DUDLEY,
President.

THE JONSSON FOUNDATION,
Dallas, Tex., July 18, 1974.

Hon. VANCE HARTKE,
Chairman, Senate Finance Committee's Subcommittee on Foundations,
c/o Mr. MICHAEL STERN,
Staff Director, Senate Finance Committee,
Dirksen Senate Office Building,
Washington, D.C.

DEAR SENATOR HARTKE: The Trustees of the Jonsson Foundation, a private foundation in Dallas, Texas, wish to submit their views on Code Sections 4940 and 4942 in response to your invitation to file these for the record and study of the Subcommittee on Foundations.

We believe the 4% tax imposed by Section 4940 is extremely punitive and unnecessary. It has more than doubled this Foundation's costs (for legal, accounting and administrative fees). Presumably the experience of other such foundations duplicates our own. These increased expenses obviously reduce the dollars available for the charitable purposes of the Foundation. Despite the substantial increase in the number of IRS auditors and the breadth of its investigations of such foundations, it is our understanding that the tax collected is six times greater than IRS costs of such audits. There is certainly some argument for abolishing this tax altogether since such foundations are the only entities in the nation which are charged for IRS audit services. If it is not completely abolished, we strongly urge that the tax at least be reduced to ½ of 1% of net investment income and that capital gains be excluded from investment income so funds set aside and required for charitable purposes will not be diverted to noncharitable government use.

The prevention of indefinite deferment of distributions to charities, the thrust of Section 4942, is commendable indeed. However the annual payout requirement of 6% of market value of investment assets is stringent and places too severe a burden on Foundation trustees to secure a sufficiently high rate of return to avoid:

1. Converting all its investment assets into bonds or other fixed income securities (thus dealing a severe blow to the nation's economy as well as to the ability of the foundation to protect itself against inflation).

2. The other alternative of slowly liquidating and terminating the existence of the foundation represents an even more severe blow to the churches, hospitals, and educational, medical and research institutions which depend so heavily on continued support from such foundations. We urge a reduction in the minimum percentage required to be distributed from 6% to 3%. This would permit private foundations to invest at least a part of their assets in equity securities and preserve their existence.

Many of the most vital services which meet public need were developed and inspired as well as made possible through the financial assistance of foundations which became classified as private under the Tax Reform Act of 1969. To continue to and further diminish their roles in our pluralistic society is, we believe, a disservice to the public. The size of foundations' assets and annual giving ability is negligible when compared to Federal Government expenditures in health, education and welfare. Failure to preserve the foundations, in our opinion, will have an unalterably negative impact on our nation's charitable institutions.

We shall appreciate your consideration.

Sincerely,

PHILIP R. JONSSON, *President.*

THE J. E. & L. E. MABEE FOUNDATION, INC.
Tulsa, Okla., July 24, 1974.

Hon. VANCE HARTKE,
Chairman, Subcommittee on Foundations, Senate Committee on Finance, New Senate Office Building, Washington, D.C.

DEAR SENATOR HARTKE: I understand that your Committee is considering the question of the desirability for lowering the 4% tax imposed on private foundations under section 4940 and also some modification of the payout requirements of section 4942.

The J. E. and L. E. Mabee Foundation was established in 1948. Mr. and Mrs. Mabee are both deceased and the current Board of Trustees is endeavoring to fulfill the trust reposed in us to make worthwhile grants from this foundation, particularly in the geographical area of the Southwest. We are not a large foundation by many standards, but neither are we the smallest. At the current rate of tax being imposed, we are paying out annually approximately $200,000 which we would like very much to see going to charitable beneficiaries in this area. I attended the Senate Finance Committee hearings when the Reform Act of 1969 was being considered, at which time it was suggested that 4% rate of tax would be a revenue matter rather than an amount raised to reimburse the Internal Revenue Service for its costs of auditing private foundation returns and activities. I am not one to say that IRS should not be reimbursed for this extra load, but anything over and above that cost is truly taking funds away from those nonprofit organizations which badly need help, particularly in the small private college area in which we are particularly interested.

I know there are many foundations that have problems with the payout requirements under section 4942. We have had a practice in our foundation for quite some time to distribute all of our income, which has always been in excess of the mandatory percentage of assets on hand. We have no intention of changing this pattern. There are foundations, however, wherein this provision has the effect of a gradual liquidation of the foundation itself. I do not think this is healthy for our nation as a whole. Private giving has always had a substantial role in America, and I hope it will continue so to be.

Thanks for taking the time to read this letter.

Sincerely yours,

DONALD P. MOYERS,
Vice Chairman.

MEMORANDUM SUBMITTED BY LILLY ENDOWMENT, INC., OF INDIANAPOLIS THROUGH LANDRUM R. BOLLING, EXECUTIVE VICE PRESIDENT

Section 4940

The four percent tax on the income of foundations, levied under the Tax Reform Act of 1969, was intended, by general agreement, to provide funds with which to enable the Internal Revenue Service to carry out more frequent and more thorough audits of foundations than had been attempted in the past. In the light of the concerns underlying the Act, more frequent and more intensive audits are certainly justified. There is, of course, a good case to be made for having foundations supply directly the funds necessary for these audits. The four percent rate, however, demonstrably collects far more money than is required to perform these auditing services.

In the case of Lilly Endowment, the tax for 1973, paid in 1974, amounted to $766,119. Even if one accepts the principle that the taxes paid by the larger foundations should be expected to help cover the costs of auditing many smaller foundations, it would still appear that the so-called auditing tax paid by Lilly Endowment is many times the cost of its audit, and that the total charge would seem to be excessive. Since the principal interest of the government and of the general public in foundations is to make sure that they maximize their contributions to approved public charity purposes, it becomes a public policy question as to the reasons why foundations should be taxed in amounts beyond what is required to cover the total costs of foundation audits.

On principle, we would state our conviction that at least half of the so-called auditing tax is in effect a tax on charity. All of the moneys collected in excess of the amounts required for the IRS activities connected with foundations con-

stitute what can only be regarded as a punitive tax on foundations. That it is within the power of the Congress to levy such a tax, and to set it at whatever level the Congress may desire, is of course beyond argument. What is ultimately at stake is the basic question of national policy toward foundations—whether their work in behalf of charity is to be encouraged or discouraged, whether foundations are to be accepted as basically beneficial to our nation or are to be regarded as institutions merely to be tolerated until government agencies take over their functions.

Lilly Endowment can and, of course, will live with whatever tax the Congress levies. Our desire would be for the Congress to revise downward this tax from four percent to something like the two percent that, on the basis of present calculations, would seem to cover adequately all the costs related to the IRS oversight of foundations.

Section 4942

The pay-out requirements governing the amount of money distributed by foundations in grants and operating expenses have been stated in the Tax Reform Act of 1969 in terms of a percentage of a foundation's assets or the total income for each year, whichever is greater. The Commissioner of Internal Revenue is granted certain discretion in determining what that percentage shall be. In light of the inescapable fluctuations in stock market values, investment earnings, interest rates and the general health of the economy, some flexibility in the pay-out rate would seem desirable; and it should be understood that the pay-out rate could go down as well as go up.

Just what the pay-out rate prescribed by law should be is a question on which concerned and responsible persons may differ. On the basis of present public policies, it is to be assumed that the total of current income from the holdings of a foundation should be the minimum amount to be distributed. Beyond that it is difficult to establish a formula that will be equitable and prudent in all circumstances, for all foundations, at all times. Some foundations whose holdings may be rapidly increasing in value may actually be able to pay out, *over time*, far more to charity if the mandated percentage rate is set relatively low rather than high. If the purpose of the pay-out requirement is essentially to maximize contributions by foundations to charity, this consideration should be carefully examined, and safeguards should be established against administration of the pay-out requirements in such a way as to erode, and ultimately destroy, the capacity of a foundation to perform its charitable purposes.

Since any figure set is, in some respects, arbitrary and since the annual earnings of most reputable stock market portfolios, mutual funds, and other balanced investment indices have been well below six percent over the past decade, we would support the suggestion that the pay-out requirement be significantly reduced from the present anticipated schedule.

HORACE P. ROWLEY, III,
New York, N.Y., May 20, 1974.

Re: Subcommittee on Foundations: written statement.

MR. MICHAEL STERN,
Staff Director, Committee on Finance, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: I submit this statement and the attached exhibits in accordance with Senator Hartke's invitation dated April 26, 1974.* It is a personal statement on behalf of myself only. The recommendations are based on my observations of the acts of the Suburban Action Institute and its development subsidiary, Garden Cities Development Corporation.

SAI is a New York charitable trust which has received a 501(c)(3) tax exemption. GCDC is a New Jersey not-for-profit corporation which has *not* received a 501(c)(3) tax exemption. Until recently, the trustees of both organizations were Paul Davidoff, Nell Gold, and their wives. SAI's goal is to persuade the courts to implement its political theory of "inclusionary zoning". "Inclusionary zoning" means distribution of housing on the basis of race and economic quotas. Davidoff, "Opening the Suburbs: Toward Inclusionary Land Use Controls", 22 Syracuse Law Review 509 (1971). GCDC's goal is to actually build developments in suburbs where SAI has succeeded in establishing quotas.

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*The exhibits referred to are made a part of the official files of the committee.

Davidoff and Gold direct SAI. There is a 21-member "board of advisors", but its duties are not clear (Exhibit-1). SAI also publishes and distributes its own propaganda (Exhibit-2). SAI has also helped establish the Connecticut Coalition on Exclusionary Zoning in the Suburbs, and the New Jersey Coalition to End All Suburban Exclusion. These are political organizations.

Since 1970 SAI has filed many administrative and judicial actions against both municipalities and corporations in Connecticut, New Jersey and New York. I am attaching 9 separate press releases from SAI and GGDC which describe some of their acts in their own words (Exhibits 3–11). The effects of these acts include not only disruption, but also great expense for legal defense. They have little or no support among the residents. Nevertheless, they claim to know what is good for them.

SAI's acts are financed by many foundations:

Foundation	1970	1971	1972	1973	1974
Taconic	20,000	30,000	20,000	20,000	
Field	30,000	30,000	36,000	35,000	
Schumann		20,000		20,000	
Wallace-Eljabar		50,000	75,000		
Stern		30,000	30,000		
Twentieth Century	111,300				
Rockefeller Bros				35,000	
Ford					50,000
National Endowment Arts					38,000

In a booklet titled, "The Suburban Frontier" by D. Hayunga, which SAI publishes, the author states:

> One (model) identified by one of the Institute's (SAI's) co-directors when he described the Institute's activities as "*stealing from a bank*". Under this image, sophisticated thieves set their sights on a particular bank, study its alarm systems, its type of safe, its possible vulnerabilities, and then move in with the sophisticated tools and knowledge of safe-cracking techniques and alarm-breaking mechanisms. More specifically, the activists model under this image is composed of a group of experts who move into a community, study the functioning systems well, and then with their expertise in city-planning, confrontation politics and law manipulate and maneuver those systems so well that the operating system is forced to produce the desired effects. The power-levers under this model include such tools as law, utilization of the press, and federal intervention—all of which are used to pry open the cache of valuables. (Emphasis added).

Various aspects of SAI's and GCDC's acts are under investigation by IRS, GAO, and the New York Attorney General.

I recommend that Congress make the following changes to the Internal Revenue Code sections which cover foundations and exempt organizations:

1. *Congress ought to limit the capital of all foundations and the amount of money which an exempt organization can receive during its lifetime.* The big foundations are too powerful. Their officers make public policy by allocating huge amounts of money to projects which they approve. These officers did not earn the money and their views are not representative of the public. This is also true of the grantee exempt organizations. They also want to impose their concept of the public interest on the public. There are so many foundations and exempt organizations now that neither IRS nor the entire government could regulate their activities. The proposed limitations will reduce their power and give the public an opportunity to help regulate them.

2. *Congress ought to limit the relationship between foundations and exempt organizations.* The relationship between foundations and exempt organizations has reached the point of Establishment. For example, Rev. H. Carl McCall was a member of the Schumann foundation at the same time that he was a member of SAI's board of advisors. Even though he was Executive Director of the foundation at the time it granted money to SAI, the foundation reported on its 1971 federal tax return that:

> There is *no relationship* between the grantee and any manager, director, trustee or substantial contributor to the Foundation. (Question E(1)(D)) (Emphasis added).

I am enclosing my correspondence with the foundation about this relationship (Exhibits 12–14). I am also enclosing a letter about this general problem of interlocking foundations and exempt organizations from Mr. Robert F. Goheen, Chairman of the Council on Foundations (Exhibit–15). Another problem is exempt organizations and foundations with the same officers. For example, Mr. David R. Hunter is Executive Director of both the Ottinger Foundation and the Stern Fund which share the same office at 21 East 40th Street in Manhattan. Both foundations granted money to SAI (Exhibit–16). Congress ought to limit the number of foundations and exempt organizations to which a single person can be associated to two. It should also prohibit any person from being a member of both the grantor and grantee organizations. I do not believe that "General Principles and Guidelines for Grant-Making Foundations" of the Council on Foundations is enough protection for the public. The rules are vague and not enforceable.

3. *Congress ought to give foundations a duty to give notice and opportunity for hearing to interested parties before granting money to an exempt organization.* Foundations give undivided attentions to "public interest" schemes of exempt organizations who are applying for a grant, but no attention to the people who will be affected by the grant. SAI is a good example. The foundations who granted money to SAI could have no doubt that its acts would cause great changes to the suburbs of metro New York. Nevertheless, none of them ascertained the opinions of the affected people. This is pure Due Process. Denial of Due Process in the SAI case has caused great disruption. Another problem is notice of default. In 1969 the 20th Century Fund granted over $100 thousand to Davidoff and Gold as individuals (apparently) (Exhibits–17–19). Nevertheless, Davidoff and Gold defaulted on the project, and the Fund planned to sue them (Exhibits–20–22). Neither the public nor other foundations knew about this for a few years until the press published the information. Another problem is open records. Foundations ought to have a duty to disclose to the public during all working hours all of its files on a particular exempt organization. This would give to the public an opportunity to insure that the organization is making truthful statements to all foundations.

4. *Congress ought to establish a mandatory limit on the amount of money which a particular exempt organization can receive during its lifetime.* These organizations neither die nor fade away. If they complete a project, the question is not how to dissolve, but how to find a new project. Many of the people associated with these organizations cannot succeed in the market place. They have a vested interest in a perpetual project. These organizations ought to be ends-oriented, not means-oriented. If one cannot achieve the end with $500,000, then it ought to dissolve and let someone else try.

5. *Congress ought to clearly define the political activity which is prohibited.* Foundations and exempt organizations believe that they know what is good for everyone else, and they have the power to force it on us. Books such as the *Ethical Investor* tell foundations how to impose their will on the public. In an article titled, "Suburban Action: Advocate Planning for an Open Society," Davidoff and Gold clearly state that "advocate planners" decide both means and ends;

> Suburban Action represents the institutionalization of a concept concerning one form of advocate planning. This concept emphasizes the role of the planner as a proponent of goals, as an actor concerned with the purposes of the system for which he plans. This view stems from a theory of planing that suggests that at least some planners should more actively espouse purposes than means. It is not a denial of the importance of the planners technical role where he details effective ways to accomplish given goals. But it does rest on the belief that an essential part of the planning process is the determination of appropriate sets of ends for a system.

Their peculiar ideas have presented to the legislatures of Connecticut, New Jersey and New York which have rejected them. Nevertheless, they want to impose these ideas on us against our will. In fact, Davidoff ran for Congress in Westchester County and was overwhelmingly defeated. "Inclusionary zoning" is clearly a political theory. The representatives of the people have rejected it. SAI is not free to lobby for it in the courts and retain its 501(c)(3) tax exemption. Congress ought to make it clear that exempt organizations are free to work only toward goals which the representatives of the people have approved. If they don't like those goals, they can work to change them. But they cannot do so and keep their tax exemption.

6. *Congress ought to prohibit so called "public interest law firms."* These firms are proliferating. In a booklet titled, "The Public Interest Law Firm—New Voices for New Constituencies," the Ford Foundation is lobbying for more of them. These firms tell us what is the "public interest." They use class actions to exploit activists courts in order to obtain court orders which have the same force as a statute. The effect is that these firms have nullified the will of the majority. Now these firms want to add insult to injury. They want to collect not only grants from foundations, but also attorneys fees from the losing parties in their lawsuits. They want to be paid double. But they don't want to be liable for attorneys fees if they lose. And, of course, the foundations don't want to be liable either. SAI claims to be a public interest law firm. It has filed many lawsuits including one which may turn out to be the most important zoning case to reach the U.S. Supreme Court. *Oakwood at Madison* v. *Madison Township*, 283 A.2d 353 (1971). Davidoff was his own expert witness in the case. Also, William Baylis was not only a plaintiff in that case, but also a plaintiff in another SAI case named *Baylis* v. *Franklin Lakes*. Whatever good these firms ever did will be accomplished by the new Legal Services Corporation. The federal and state legislatures are the only public interest law firm which we need. And they alone ought to decide what is in the "public interest." If these law firms want to continue, let them do so without a 501(c)(3) tax exemption.

7. *Congress ought to impose a legal duty on exempt organizations to produce a fair and balanced product.* Generally, exempt organizations "research" for evidence supporting their predetermined views. They don't look for or report conflicting views. They ought to have a duty to do so just as broadcasters have a similar duty under the FCC's Fairness Doctrine. One-sided reports are pure political propaganda.

8. *Congress ought to impose a legal duty on foundations who grant money to exempt organizations which support one view to grant money to another organization which supports a conflicting view.* Generally, foundations and exempt organizations are leftist oriented. As a result, their products are leftist oriented. The other side has no opportunity in the market place of ideas. A kind of Fairness Doctrine ought to apply to the foundations themselves. The competition will cause a higher probability of a good and true product. Foundations will not find such organizations unless they have an incentive to do so.

9. *Congress ought to prohibit an exempt organization from operating a non-exempt subsidiary.* It is common now for an exempt organization to operate in tandem with a non-exempt organization. SAI and GCDC are a good example. SAI breaks down zoning, then GCDC builds "inclusionary developments." SAI is a *de facto* part of GCDC. GCDC gets all the benefits of tax exempt status, but none of the limitations. I am enclosing two newspaper articles about the operations of SAI and GCDC in tandem (Exhibits-23-24).

10. *Congress ought to make a "freedom of information act" for foundations and exempt organizations.* The public needs access to information about both the internal and external operations of them in order to insure that they are operating in the public interest. There is no way that IRS can monitor the operations. It needs the help of the public. Now they give the public the run-a-round if asked for information. I am enclosing correspondence with the Wallace-Eljabar Fund, a SAI grantee, and the attorney for the Regional Plan Association, which consults Davidoff's wife and Rev. McCall (Exhibits 25-26). The Stern Fund is an example of the effects of public monitoring of foundations. In 1972, Stern reported that it granted $25,000 to the Committee for Unified Newark which is directed by black revolutionary Imamu Amiri Baraka (LeRoi Jones). IRS reported that it had *denied* a 501(c)(3) tax exemption to CFUN *before* the grant. Stern protested that the grant was for "tax exempt activities," but its own annual report proves that it protest too much (Exhibits-27-28). IRS probably would never have known about this grant if I had not called it to their attention.

11. *Congress ought to require all foundations and exempt organizations to issue an annual report to both the government and the public which will be keyed to a central computer program.* Now many foundations do not publish an annual report. The public must go to their office and attempt to extract the information from them. Very few exempt organizations publish annual reports, and the public must wait about 1¼ years to see their income tax report. IRS ought to establish a central computer program for all foundations and exempt organizations. This will give IRS and the public an opportunity to retrieve

information about a particular foundation or organization. Now the public must wait for the bi-monthly *Foundation Grants Index* in order to get information which is usually stale.

12. *The Subcommittee on Foundations ought to assume jurisdiction over the National Endowment on the Arts and the National Endowment on the Humanities.* Last December after a great controversy, NEA granted $38,000 to SAI for a study of zoning laws. GAO is investigating the grant because it has nothing to do with "art." I am enclosing a copy of the original and revised project descriptions, and a newspaper article about what caused the change (Exhibits-20–31). This incident and the fact that NEA has about $170 million to spend proves that it is following the path of the private foundations and needs close government regulating.

13. *The Subcommittee on Foundations ought to do an in-depth case study of SAI and GCDC.* SAI/GCDC and the foundations which support them would be a good case to study because it contains many of the qualities which the public has been complaining about. GAO, and maybe IRS and the New York Attorney General will issue a report. The Subcommittee will not have to start from scratch. Now is the time to subpoena SAI and GCDC for an explanation of their acts.

In conclusion, I trust that the Subcommittee will continue to monitor the structure and operations of foundations and exempt organizations.

Respectfully,

HORACE P. ROWLEY, III.

New York, N.Y. May 22, 1974.

Re: Subcommittee on Foundations; supplemental statement.

MR. MICHAEL STERN,

Staff Director, Committee on Finance, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: This is a supplement to my written statement dated May 20 about foundations and exempt organizations.

I am enclosing excerpts from the 1970–71–72 annual reports of the Wallace-Eljabar Fund which clearly show how the Fund and Suburban Action Institute conceived a scheme to change the zoning laws of New Jersey. (Exhibit-32).

I am also enclosing some more newspaper articles about SAI's lawsuits in New Jersey and New York (Exhibits-33-7).

Respectfully,

HORACE P. ROWLEY.

1970.—"One of the major objectives of the Wallace-Eljabar Fund in its giving is to promote public discussion and awareness about New Jersey's neglected problems. The Fund made a number of grants in 1970 which illustrate this concern. * * * b. The Suburban Action Institute received funds to establish a law office in New Jersey to bring legal action against exclusionary land use and zoning practices which constrict the supply of housing. By careful selection of the cases, adequate funds for research, and the preparation of carefully drawn arguments, it is hoped that important court decisions will result. Dennison Ray is directing the project at 745 Park Avenue, East Orange, New Jersey.* * * There is little state consciousness—New Jersey's Constitution contains the *strongest home rule provisions of any state's*, and there are 567 municipalities to exercise them."

1971.—"There were some encouraging results which can be traced directly to grants made by the Wallace-Eljabar Fund in 1970 and 1971. Some of these should be of interest outside New Jersey, even though our major emphasis continues to be the upgrading of public interest representation in the councils and courts of this state. Specifically, Fund contributions led to: a landmark decision in the case of *Oakwood at Madison, Inc.* vs. *Township of Madison*, which was argued by the Suburban Action Institute under the litigation project initiated with the Fund. For the first time in the Nation, a court invalidated a municipal zoning ordinance in its entirety because it had the effect of excluding large segments of the population; and moreover, the court ruled that the general welfare requirement necessitates municipal zoning to fulfill "*its fair proportion*" (that is, "inclusionary zoning", ed.) of the housing needs of its region, not just its own population. Although the litigation route is sometimes torturously slow, it can produce more with one action than a thousand open housing tests or a dozen conferences. Dennison Ray is counsel; Lois Thompson is associate counsel. Project offices are at 715 Park Avenue, East Orange, New Jersey 07107."

1972.—"Suburban Action Institute—S.A.I. operates an education and litigation program in New Jersey, supported by foundation funds. S.A.I. initiated litigation which is now being heard against municipalities which engage in exclusionary zoning and land-use practices which constrict the supply of land for housing and deny access to housing by the overwhelming majority of North Jersey residents. Paul Davidoff and Neil Gold are co-directors at 150 White Plains, Road, Tarrytown, N.Y. 10591."

1973.—Not published yet.

[From the New York Post, Jan. 30, 1974]

MITCHEL FIELD SUIT DISMISSED

(By Irving Lieberman and Steven Marcus)

A federal judge today dismissed a suit that sought to block development of 574 acres of land in Mitchel Field in Nassau County unless low-income housing was also built.

The decision by Judge Mark A. Costantino in Brooklyn, clears the way for the construction of a 52-acre industrial park on the site.

Plans for the park were announced yesterday by Nassau County Executive Ralph G. Caso, who said it would provide 6000 jobs and generate $1.2 million a year in rent and taxes.

The suit had been brought by the NAACP and Suburban Action Institute, a nonprofit urban planning organization that is seeking to create jobs and housing in the suburbs for low-income families.

The two organizations contended that Nassau County officials had been "racially motivated" in opposing plans for building housing at Mitchel Field, which formerly was an Air Force base.

Costantino said in his decision that "unquestionably" the decision not to construct housing "is in large part a result of public opposition" and that "it is clear from all the evidence" that such opposition to low-income housing "has been racially motivated."

RESIDENTS NOT ON TRIAL

But the judge added that the "residents of Nassau County are not on trial. There is no proof," he said "of official conduct which has as its purpose the containment of blacks or which has the effect of denying [to] blacks rights and opportunities available to whites."

Richard F. Bellman, a lawyer for the Suburban Action Institute, said he would have to study the decision before deciding whether to appeal.

[From the New York Times, Jan. 31, 1974]

SUIT ON MITCHEL FIELD HOUSING DISMISSED

(By Morris Kaplan)

A Federal judge in Brooklyn dismissed yesterday a suit by blacks and poor people to force Nassau County officials to build low-income housing at Mitchel Field.

The judge, Mark A. Costantino, ruled that there was no proof during a 12-day trial that ended last July 13 that county officials had denied plaintiffs the rights and opportunities available to more affluent whites.

The judge acknowledged the existence of racial discrimination in Nassau, but this attitude, he said, could not be charged to the county's elected officials in this case. In other instances, he added, proposals for low-income housing predominantly occupied by blacks had been dropped by elected officials because of heated community opposition.

Nassau, Judge Costantino pointed out, has the highest median income level and the lowest percentage of over-crowded housing in the metropolitan area.

U.S. AGENCY ABSOLVED

The defendants in the suit included the Nassau County Executive, Ralph G. Caso, Who announced plans yesterday for a 52-acre industrial park at Mitchel Field that would provide 6,000 jobs, he said, and generate $1.2-million a year in rent and taxes. The suit was filed last March by civil rights and housing groups to prevent Nassau from developing a 630-acre tract in the area unless it provided for public housing on the land.

Judge Costantino also dismissed as "without merit" charges against the General Services Administration that it had failed to comply with Federal site-selection laws. The G.S.A. is proceeding with plans to use 55 acres for a post office and a Federal office building, according to Cyril Hyman, deputy chief of the civil division of the United States Attorney's office.

The plaintiffs, including the Long Island Region of the National Association for the Advancement of Colored People, had brought the class action suit on behalf of all blacks for Spanish-speaking persons who were eligible for low-income housing.

They contended that except for 250 units of housing for the elderly, Nassau officials opposed any housing at Mitchel Field. The plaintiffs maintained that the county's failure to include low-income housing had been motivated by racial bias and that this would perpetuate patterns of racial segregation existing in the county.

They asserted, further, that housing for the elderly would be almost exclusively for whites and low-income housing would be almost exclusively for blacks in violation of the 14th Amendment.

APPEAL IS PLANNED

The plaintiffs, seeking declaratory and injunctive relief, were represented by Richard F. Bellman and Lois D. Thompson of the Suburban Action Institute of Tarrytown, N.Y. Mr. Bellman said that he would move quickly for a stay pending an appeal, to prevent Nassau from carrying out any further development of the acreage, which is in the middle of the county and near Uniondale, East Meadow and Hempstead.

He added that the judge's ruling favored consideration of an appeal, which will be filed in the Second Circuit Court of Appeals.

Expressing "delight" with the decision, Mr. Caso said, "While I question Judge Costantino's contention that 'community opposition to [low income family housing] has been racially motivated,' I also note the court's finding that * * * there is no proof of official conduct * * * which has the effect of denying blacks rights and opportunities available to whites.' "

"It is clear from all the evidence that community opposition to this [low-income] form of housing has been racially motivated," Judge Costantino said, adding:

"Proposals for the construction of this form of housing have incurred immediate and vehement opposition. As can be expected, such heated opposition has not been ignored by the elected officials of Nassau.

"The residents of Nassau, however, are not on trial. If judging the actions of the public officials of Nassau, community reaction to low income family housing—the racial fears and prejudices manifested—is only one of many relevant indices."

The judge found no proof of official conduct aimed at the containment of blacks or of the existence of "fixed patterns" of home ownership in Nassau. No physical boundaries separate whites from blacks and there is considerable movement of blacks into areas formerly occupied exclusively by whites, he said.

The county has 1,428,000 white residents and 275,000 blacks.

[From the Sunday Record, Feb. 10, 1974]

SAI ZONING SUIT DISMISSED

(By Richard Duffy and Paul J. Lieberman)

A Suburban Action Institute suit challenging the zoning of Franklin Lakes, Wayne, and three other New Jersey towns on the ground that the poor and lower-middle classes are unfairly excluded was dismissed Friday in Superior Court in Hackensack.

"The issue raised by the complaint, in my opinion, should be directed to the legislature, and not to the courts," said Judge William R. Morrison, who then invited the Suburban Action Institute, based in Tarrytown, N.Y., to appeal.

Lois Thompson, attorney for the tax-exempt SAI, said it would appeal. She characterized the judge's decision as unusual.

18-MONTH-OLD SUIT

The judge said the issues raised by the suit probably would be resolved ultimately by the state Supreme Court.

Although it names only five communities as defendants, the suit asks for a finding that the zoning in virtually all the state's suburban communities discriminates against the poor. The suit was filed 18 months ago in behalf of six poor persons and four organizations.

Besides Franklin Lakes and Wayne, Holmdel, in Monmouth County; Livingston, in Essex; and East Brunswick, in Middlesex, are the defendants.

Judge Morrison said he did not believe the issues raised by the suit fell within the jurisdiction of the courts.

DEFENSE CONTENTION

The ruling agreed with a defense contention that the suit is too broad. The suit is a general attack on the zoning of the communities, rather than a request for permission to build specific projects on specific tracts. Morrison said the suit had raised no concrete dispute on which the court could rule.

"They're treating it as though the court sets down the groundwork of zoning in the state," Dean A. Gaver, a Newark lawyer representing the five towns, had said.

He continued:

"The issue is whether a developer could build low-income housing in any one of these five towns. I submit the law makes it clear that they can."

"We have no project, no land, no nothing," he said of the broadness of the SAI suit.

The suit notes that there is a housing shortage in the state, and says the shortage is especially acute for poor people.

It argues that ordinances or parts of ordinances that restrict construction of housing within the price range of the lower classes ought to be declared unconstitutional. The suit cites clauses that prohibit multifamily housing, set minimum floor areas, restrict apartment houses to one-family units, prohibit mobile homes, and prohibit similarity of design in adjacent buildings.

The SAI had argued that the trend of court decisions relating to zoning—including the recent decision by Superior Court Judge George B. Gelman ordering the rezoning of a Washington Township tract to permit apartments—had outlined the basic case against suburban zoning codes. In that case, however, the suit was brought by a developer seeking permission to build.

Two other zoning challenges will come before Morrison in the next few months.

As in the challenge against the five towns, both are sponsored directly or indirectly by the SAI. Both, Ms. Thompson said, are more straightforward and common than the suit dismissed Friday.

One suit challenges zoning in Mahwah, Ramsey, Saddle River, and Upper Saddle River on the ground that many workers in those communities cannot afford to live there. Three of the four plaintiffs work at the Ford Motor Company plant in Mahwah.

In the other suit, the Garden Cities Development Corp., an SAI subsidiary, is asking the right to build a 720-acre, 6,000-unit town-house and garden apartment complex off Route 202 in Mahwah.

The State Supreme Court now is considering a zoning case involving Mount Laurel Township, in Burlington County. That decision, said SAI trustee Neil Gold, will give guidance to the lower courts in zoning and related land-use suits.

[From the Ridgewood News, Feb. 14, 1974]

ZONING ANALYSIS—MORRISON RULE—NO LANDMARK

(By Joe King)

There is a tendency by the favored side to hail any court decision on zoning practice as a "landmark" with presumed universial application, but that is hardly

tenable in the rebuff suffered by the Suburban Action Institute in Superior Court in Hackensack, in a suit against Franklin Lakes and three out-county towns.

It would be injudicious to assume that the dismissal of the case set any precedent for the remaining two actions mounted by SAI. One cites Mahwah, Ramsey, Saddle River and Upper Saddle River as defendants on their zoning codes. The other, by SAI satellite Garden Cities Development Corp., challenges Mahwah on the right to build a 6000-unit housing development in the township.

Had judge William R. Morrison ruled in favor of SAI Friday against Franklin Lakes et al, that surely would have been a "landmark" decision, as the jurist implied by referring the issue to the Legislature, and Bergen might well have feared the collapse of state-conferred "home rule" zoning.

Judge Morrison respected the delicate line between judicial interpretation of a law and legislation by the courts, that seems to have been drawn fine in several recent zoning decisions, and, as the jurist said, in need of ultimate adjudication by the state Supreme Court.

* * * * * * *

SAI, the richly funded White Plains, N.Y., organization that is gunning widely against the "home rule" concept of zoning, sought a sweeping, categorical opinion from Judge Morrison that there was a general discrimination against the "poor" in the zoning practice of the defendant towns, and, in extension, all others like them, a package that would include almost all of Bergen and much of the suburban state.

Judge Morrison was given no precise point of law on which to rule; essentially, as he said, the suit involved law-making, not interpretation. Broadly, as the defense saw it, SAI contended that zoning ordinances should be recast to meet the lowest income levels.

It would be naive to think the crack SAI legal corps floated this suit as anything but a trial balloon, to assay the judicial winds and estimate a course for the Mahwah actions, which are in one case based partially on court precedent, and in the other on hardnosed equity in the land.

* * * * * * *

The parent SAI suit against Mahwah et al. maintains zoning has no regard for area needs in the general vicinity of the towns, a point that has gained scattered but growing recognition in court decisions. An absolutely novel contention by SAI, focusing on Mahwah, is that a town has the obligation to provide housing for workers employed there, especially at the giant Ford Co. plant on Route 17.

The later point is a philosophy, or a sociological concept, that the courts are being asked to enforce, apart from law.

The Garden Cities (SAI) suit involves land equity in asking why Mahwah should have the privilege to deny the plaintiff the right to build 6000 housing units on an owned tract.

In a similar case in Washington Township Superior Court Judge George Gelman not only ruled in favor of the land-owning plaintiff, in the Waldy Tract suit, but entered into the specifics of town planning, hitherto sacrosanct by statute.

What seems apparent is a lack of direction on zoning to the judges by the Supreme Court on what law is standing, an abnegation by the Legislature of any intrusion on current statutes, and a stubborn reluctance by most towns in the county, particularly those in court, to review their traditions realistically and eliminate what is unreasonable, unfair and capricious.

[From the Bergen Record, Apr. 30, 1974]

Court Rejects 'Elite' Zoning

(By Adrian Peracchio)

Rendering a decision that would curtail home rule, a Middlesex Superior Court judge has rejected a long-contested Madison Township zoning ordinance.

Judge David D. Furman said it is illegitimate to use the municipal zoning power to create what he described as an elite community of high-income families with few children.

Furman said a municipality has a responsibility to its region to provide land for low- and moderate-income housing.

In Madison Township's case, the region to be considered would extend as far as New York, the judge said.

If the ruling is upheld by the New Jersey Supreme Court, where it is headed for automatic review, it may become a landmark decision profoundly affecting most suburban areas in the state.

The central issue appears to be the question of how far a municipality will have to go to fulfill regional housing needs, and who will dictate where the line is drawn.

In Bergen County, a growing number of wealthy bedroom communities face litigation over alleged exclusionary zoning practices. Among them are Mahwah, Saddle River, Upper Saddle River, Franklin Lakes, and Ramsey.

The original legal issue in Madison Township was whether a municipality had the right to exclude multifamily housing. The town drew up a zoning plan limiting development to two acre lots when, in 1970, developer Nathan Kaplan proposed to build apartments for low- and moderate-income families.

Kaplan fought the ordinance in court, supported by the Suburban Action Institute, a private group based in White Plains, N.Y., which is attacking zoning laws in New Jersey, New York, and Connecticut as tending to keep out poor and nonwhite persons.

CHANGES CALLED MINIMAL

The suit against Madison Township was joined by six white and black, low- and moderate-income families for class action. In 1971, Furman struck down the ordinance.

The township appealed the decision and took it to the state Supreme Court. Before the state's highest court could rule, the town amended its ordinance to provide some zoning for apartments.

Instead of ruling on the original appeal, the court sent the amended ordinance back to Furman for a new trial.

Yesterday, Furman ruled that the changes made in the ordinance had a minimal effect on zoning laws whose effect, he said, still would be exclusionary.

Furman said in his decision:

"The zoning objective in 1970 of an elite community of high-income families with few children is maintained by the 1973 amendments. The advances toward moderate-income housing opportunities are token—toward low-income, opportunities are nil."

He argued that the town had a responsibility to provide housing space not only to meet its present needs, but also to accommodate future population shifts on a regional basis.

DEFINES REGION BROADLY

In this argument, the potentially troublesome issue of defining regional housing needs comes into play. Furman defined the Madison Township region as the area where people would normally come from to seek housing, providing the town had such housing to offer.

The area includes New York, he said, since 15 per cent of the township's residents work there.

"The region the housing needs of which must be reasonably provided for by Madison Township, in the view of this court, is not coextensive with Middlesex County," the judge wrote. "Rather, it is the area from which, in view of available employment and transportation, the population of the township would be drawn, absent invalid exclusionary zoning."

Lois Thompson, counsel to the Suburban Action Institute, said the township argued it had to meet only the needs of Middlesex County. She said:

"We argued that the town has drawn people not only from Middlesex County but from all of Northern New Jersey. We presented a study showing patterns of population growth and migration predictions through 1985, prepared by the Regional Plan Association. Apparently the judge looked at the results of the study and used them."

Richard Plechner bristled at Furman's definition of regional needs. "How is our town going to take care of New York City's housing needs?" he asked. "Personally, I don't think the Supreme Court will go along with it."

"This decision would seem to require things not within the control of this community," Plechner added. "If we are required to build the kind of low-income housing the decision expects of us, it may very well mean an end to all building

in this town. It's extremely difficult to construct low-income housing without some kind of subsidy.

'CANNOT SUBSIDIZE REGION'

"The town cannot afford to subsidize the greater metropolitan region, and I don't think a court will compel us to do it."

Furman argued also that Madison Township must maintain its 1970 percentages of low- and middle-income population.

"Without the rigidity of a mathematical formula," the judge wrote in his decision, "this court holds that Madison Township's obligation to provide its fair share of the housing needs of its region is not met unless its zoning ordinance approximates in additional housing capacity the same proportion of low-income housing as its present low-income population—about 12 percent—and the same proportion of moderate-income housing as its present moderate-income population—about 19 percent."

Currently under review in the state Supreme Court is a lower court decision striking down similar zoning ordinances in Mount Laurel Township, a sparsely populated community in Burlington County.

MAJOR INROAD SEEN

A state Supreme Court ruling is expected to come soon in the Mount Laurel case, certainly earlier than in the Madison Township case, which is likely to be affected by the Mount Laurel decision.

The two cases bear striking similarities. Trial judges in both instances said—for the first time in New Jersey—that a municipality could not ignore housing needs beyond its own boundaries.

Paul Davidoff, executive director of the Suburban Action Institute said Furman's ruling would become, if approved by the high court, a major inroad in the fight to break income barriers in the suburbs.

"It's the most important decision to come down in the whole battle to make it possible for middle- and low-income and nonwhite families to gain access to the growing possibilities of the suburbs," Davidoff said.

The institute is participating in court challenges to zoning in Mahwah, Ramsey, Franklin Lakes, Saddle River and Upper Saddle River.

"It may not affect our case too badly, but it sure won't do us any good," said Franklin Lakes Mayor Thomas Pawelko, commenting on yesterday's Madison Township decision.

[From the Ridgewood (N.J.) News, May 2, 1974]

ZONE OPPONENTS TO DROP APPEAL

(By Jan Rubin)

FRANKLIN LAKE.—Suburban Action Institute will not appeal its case against this borough and four other municipalities which was dismissed in Superior Court in February by Judge William Morrison.

Lois Thompson, counsel for the open-housing group, said Tuesday consultations with some of the plaintiffs in the case of Bayles et al vs. Franklin Lakes, Wayne, Holmdel, East Brunswick and Livingston indicate they feel the broad-based suit they have been pursuing is not viable.

A novel theory was attempted in the class action, but with the current status of the law and the courts in New Jersey, it is better to stick with sure winners, like the Madison case, Mrs. Thompson said.

Monday, Superior Court Judge David Furman overturned Madison Township's zoning ordinance, which had been challenged as exclusionary in a suit brought in 1970 by developer Nathan Kaplan and SAI.

Judge Furman ruled the township's zoning ordinance must provide for a fair share of housing needs for the region—about 12 percent low-income and 19 percent moderate-income housing. He defined Madison's "region" as one that extends to New York.

He rejected the 1973 amendments to the zoning ordinance, whereby smaller lots were created and 150 acres were set aside for apartment development on

land previously zoned for two-acre residential development, charging they made only token advances toward moderate-income housing opportunities and none toward low-income housing.

Mrs. Thompson said she found "remarkable" the judge's clear enunciation of the duty of a municipality to zone for the needs of low- and moderate-income people in the region, as well as his definition of a region and his indication of how much housing he wants.

SAI's suit against Franklin Lakes et al, filed July 1972, was turned into a complainant class action in September 1973, whereby the six low-income and minority plaintiffs represented the entire class of poor and minority residents in the greater New York area. At the same time, Judge Morrison denied SAI's request to have the five defendant municipalities represent the entire class of municipalities having alleged exclusionary zoning practices.

In dismissing the suit in February, Judge Morrison said the complaint was a matter for the legislature rather than the courts and invited SAI to appeal his ruling.

In its suit, SAI had asked the court to strike down seven alleged exclusionary zoning practices, as well as the state's enabling statute, which delegates zoning powers to municipalities. The seven practices, which prohibit or restrict multiple-family housing and ban mobile homes, are found in the zoning codes of virtually every municipality in the state.

Although this particular suit has been dropped, the zoning codes of the municipalities can still come under attack. Buttressed by Furman's Madison decision, groups that feel the codes are exclusionary may still bring suit against the boroughs.

Mayor Thomas Pawelko, who had pledged to defend the borough's zoning to the Supreme Court if necessary, said Tuesday he is pleased to hear SAI will not appeal the Superior Court dismissal of its suit against this borough and five sister communities.

He expressed disappointment with Judge Furman's decision in the Madison case. He said he is interested in studying the decision and having the borough attorney look it over in order to learn more about the specifics of the decision.

"I am strictly in favor of home rule—having each town decide for itself," the mayor said, adding he can foresee complications arising from regional zoning and the body that would administer it, inequities that might occur because a town is a part of a region as well as difficulties in defining a region.

"Fantastic!" was the reaction of Tom Pearson, chairman of the Citizens United for Home Rule, on learning of SAI's decision to drop its suit against this borough. "I'm glad the courts recognize zoning is a legislative prerogative."

He assessed the Madison decision as one that will lead to a quota system, which he described as a "highly obnoxious idea. The courts will have to decide whether the towns keep up with the percentages," he said, adding, "I don't like the idea of a judge making the zoning law."

SHERMAN, CONN.
May 14, 1974.

Mr. MICHAEL STERN,
Staff Director, Committee on Finance,
Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: May I have the opportunity of submitting this statement to be included in the testimony considered by the Subcommittee on Foundations in their present investigation? As a taxpaper, I feel it my duty and my right to present my evidence and my views if they can be of any help in preventing the intent of the laws regulating foundations and tax-exempt organizations benefits from them being misused and abused. As a resident of Sherman, Conn., I have reason to be familiar with some of the activities of Suburban Action Institute, which has been the recipient of sizeable foundation grants, and has engaged in very dubious activities "in the public interest." Although tax-exempt under section 501(c)(3), it formed a development affiliate, not tax-exempt but so-called "not-for-profit," with the same two men, Paul Davidoff and Neil Gold, as key officers of both. This affiliate, Garden Cities Development Corporation, was the proposed builder of several Planned Unit Developments, the permits for which involved court suits to break the zoning of the localities, pursued by SAI. I speak in particular of "Watersedge," in New Fairfield and Sherman, Conn., and enclose (A) a copy of a debate presented in the New York Times Real Estate

Section of Nov. 4, 1973, between Malcolm Cowley, a distinguished Sherman writer, and Paul Davidoff.*

Davidoff was clearly acting in his capacity as a director of GCDC at the same time as he was propounding the particular political theories of SAI. As Mr. Cowley pointed out, the difficulties presented by the lack of drinking water, of sewage facilities, of road access, of employment proximity, and the steep, rocky lakeside terrain, combine to make the proposal for high-density development not feasible physically, and out of the question for low-priced construction. Mr. Davidoff accused opponents of the plan of racism and bigotry, and of deliberately excluding the poor and the blacks by zoning regulations, as though lot size were the only factor in housing costs, and ignoring the facts that down-zoning would inflate land costs, force a sewer where none existed, and in the end benefit only developers. In my letter to the N.Y. Times Editor, Nov. 18, (B) I point out that it is an "integration plan" only on the word of Mr. Davidoff, and that the plan in fact includes no quotas or assurances of any kind as to the future residents, and that surely the units cannot be low in cost.

On Dec. 8, 1973, Channel 7 New York, in a TV program called "Persons, Places & Things" provided a forum for Neil Gold, defending the Watersedge plan, and also presented remarks by Malcolm Cowley, the first selectmen of New Fairfield and Sherman, and a few residents. My review for the local press, enclosed (C), reports a surprising statement by Gold that 40% of the units would be subsidized by the developers for families with incomes below the median level for Conn. This claim had not been made in any official application, Planning and Zoning hearing, or court suit, and how it was to be done was not explained then or since. Planners who testified before the New Fairfield hearings estimated that the housing units would cost a minimum of $30,000 each, exclusive of land requirements for 2 access roads 1 to 1¼ miles long each (which land the owners were unwilling to sell) or profits for each of the two partners, "not-for-profit" GCDC and admittedly for profit Steve Weil, the actual owner of the land in question. It was not clear whether Mr. Gold spoke on this program for SAI or for GCDC.

A 501(c)(3) organization with a "development affiliate" is not separate from that affiliate if they (a) share the same offices, (b) share the same officers, (c) the same telephone numbers, (d) the same office equipment, (e) the same purposes. Yes, even the purposes of the two organizations are the same: SAI's purpose is "research and action," and GCDC's purpose is action and research.

SAI's application papers to IRS (form 990a) state:

> The purposes of the SAI will be to study the appropriate role of the suburbs in metropolitan areas in connection with their contribution toward satisfying public needs for decent housing . . .
>
> An additional purpose will be . . . to help develop low and moderate income housing and to develop techniques for obtaining employment for low and moderate income people in suburban areas . . .

GCDC's incorporation papers filed in New Jersey on August 5, 1971, list the following purposes:

> (*a*) to create a housing sponsorship vehicle to expand housing opportunities . . .
>
> (*b*) To engage in research activities pertaining to the development of housing and related facilities

The meaning of "a housing sponsorship" is spelled out in the 6th paragraph: giving the Corporation powers

> (*a*) To . . . own . . . real . . . property
>
> (*b*) To . . . construct . . . or otherwise participate in the development of housing and related commercial, recreational, . . . facilities

That the purposes of these two organizations are the same is, apparently, not recognized or at least not observed in practice by the Ford Foundation, not by Taconic, not by Stern Foundation, not by Field Foundation, and not by the National Endowment for the Arts.

The National Endowment for the Arts should be included by the Subcommittee on Foundations, I believe, within the meaning of "foundations." No other branch of Congress overseas this organization, which is a large and growing one, though its funds come from Congress and from the people. The law setting up NEA removes this organization from "political influence." By the same token, it removes it from public control, and it was with astonishment that

*The enclosures referred to are made a part of the official files of the committee.

the residents of Sherman and New Fairfield learned that, on April 23, 1973, the NEA had given a grant of $38,000 to SAI, described as follows:

The effect of breaking zoning restrictions in the suburbs, and the development of racially and economically integrated new communities on the fringe of metropolitan areas—these will be the objectives of this project . . . "We are not out to break zoning," David ff had said in an interview in the new Milford Times on April 20, but the NEA thought otherwise, and thought it a goal worthy of grant money. As for the "development of new communities," NEA wrote in a letter on Dec. 6 that these were "ones in which the Institute had been active in seeking changes in residential patterns through modifications of zoning regulations." On further inquiry, NEA admitted that Sherman/New Fairfield, Lewisboro, Mahwah and Readington, and Ridgefield were indeed "among" the five communities to be studied. It was pointed out to NEA that it was not the tax-exempt SAI which was operating in those towns, but its non-tax-exempt Siamese twin, GCDC, to which NEA could not give grants. It was pointed out that zoning was found constitutional by the U.S. Supreme Court, and is public policy, but to no avail. NEA replied: "They have assured the Endowment that the projected study will be objective, and that it will encompass contrasting points of view . . ." But they have repeatedly stated that they are "advocate planners," meaning they have a point of view, their own, and they *advocate* it. NEA further: "Mr. Davidoff has assured this office that designers, environmentalists, and other authorities whose experiences have not paralleled those of the Institute's own core of staff members and consultants will be used for the study."

The studies of this group were presented by themselves at the New Fairfield Zoning Board hearing. They were Peter Kitchell, architect, who showed slides of Heritage Village, Southbury, Conn. retirement development.

Walter Cudnohofsky, landscape architect; Eleanor Steinholtz, economic consultant; Michael Kaplan, architect; Charles Francis, engineer; Robert Conradt, traffic engineer; Kendall Lund, engineering geologist, whose testimony read in part: "At this particular site, I was retained to provide a site description for the architect, planners and engineers. This description would be used as a guide in determining specific sites for building, planning data, the availability of utilities such as ground water and sewage disposal systems, and a bank of information that could enable them to make reasonable cost estimates . . ."

The purpose of this group was obviously to provide data for the construction of apartments. Their "study" was the "study" which any developer is required to do to put up housing, and required to undertake to make his case a zoning board when he demands a down-zoning. The purpose for which the NEA grant was given was to pay these consultants' fees. NEA said that the money could not be used to pay debts already incurred, but what mechanism can they employ to enforce this? Exposes of Garden Cities in the N.Y. Times Real Estate Section March 24, and the Times-Herald Record (Orange County, N.Y.) March 25, make it clear that they have not paid their bills. (See my letter, D, to Danbury News-Times, April 17.) Their attorney, J. Jackson Walter, severed his connection with them in October, and it is widely believed that he left because they failed to pay his fees. Neil Gold said, in the N.Y. Times March 24 article: . . . "You don't have to have resources to build houses. You have to have access to people who have resources. Good plans, sound economic analysis and good people willing to *wait for their fees* until development starts." If SAI has not paid the consultants on behalf of GCDC, then it is likely the bills may be still unpaid, in which case the NEA grant will pay for these long-waiting debts.

To sum up the NEA grant: First, it gave a grant for a purpose which does not qualify. Second, when the errors of the grant were learned and the grant protested, it simply invited the applicant 7 months after the grant was awarded, to rewrite his purpose, thus indicating that it did not care what the purpose is. Thirdly, the rewritten version is so vague that there can be no test of whether the funds will have been appropriately utilized, since almost any use of the funds can qualify.

NEA's attention was called to the fact that the recipients, Davidoff and Gold of SAI, were not scholars. As the Sherman Civic Association wrote, "They are not impartial scholars . . ." Their attacks on zoning show that they have already reached a conclusion on the question they are supposed to be studying. They are known developers, who propose to build apartment houses and commercial facilities in our town and New Fairfield, in Readington and Mahwah, in Lewisboro.

Where purposes of the 501(c)(3) "charitable trust" and its development affiliate, organized under a "not-for-profit" title, are nearly identical, it is perhaps not surprising that the NEA should have accepted from Davidoff a *"verbal assurance"* that those organizations "are now" separated, and required from protesters "solid evidence" of the contrary. It was pointed out that the New Jersey office, referred to in the GCDC incorporation papers as their "clubhouse," apparently in response to some requirement of N.J. Statutes Title 15, was given to SAI by the Wallace-Eljaber Fund, but now, according to Wallace-Elijabar itself, is not used by SAI. One wonders whether the books and records show a purchase by GCDC of this property from SAI, which was paid for by a $25,000 grant by Wallace-Eljabar. Meanwhile, the office telephone is still listed in the names of both SAI and GCDC, and both customarily use the Tarrytown office. Admittedly, these organizations were not separated up to the end of 1973. NEA claims that they are now separate. How, what has changed, we do not know. Undoubtedly there is a large body of case law which shows that organizations so intertwined are not in fact separate organizations. I believe the IRS should make an explicit regulation embodying this case law. Thus, tax-payers would be protected from the ruse of the noble-appearing partner collecting grants, and siphoning them off to the business partner.

I would call to the attention of the Committee the grant of some $111,000 by Twentieth Century Fund to Davidoff and Gold, of SAI and GCDC, made shortly after the N.Y. Times story of June 29, 1969. (On Sept. 12, 1974, the news broke in New Fairfield and Sherman (encl. E_1 and E_2 that the 20th Century Fund was commencing legal action against Davidoff and Gold because they had not produced the study which they had contracted with the foundation to produce. The purpose of the grant, in the 1970 report of the 20th Century Fund, is the following:

> The research directors will be testing whether problems of race and poverty can ever be resolved without taking steps to marshall the resources of the suburbs.

Clearly, the question is rhetorical. If there were any doubt, the 20th Century Fund Newsletter of Dec., 1969 (encl. F) gives a whole page to showing that the aim of the study was not to study whether the urban problems of race and poverty could be resolved, but what measures could be taken to override local zoning, which was and is assumed to be the cause of the problems, or at least the obstacle to their resolution. Says the Newsletter, announcing that the study will commence in 1970,

". . . Mr. Davidoff of Hunter College, one of the originators of 'advocate planning,' and Mr. Gold, a planning consultant, will examine whether the federal government pursues urban policies that work to solidify existing class and racial lines in the country . . . They will seek to demonstrate that these problems cannot be solved *unless* steps are taken to marshall the resources of the suburbs in combating physical and spiritual decay in the cities."

The recent Ford Foundation grant to the Urban Development Corporation to construct "racially and economically-integrated housing" in Buffalo appears to have been unnecessary. The UDC is a quasi-public corporation, with all the financial powers of Government and none of the responsibilities, with power to float its own tax-free bonds, which it has done in such abundance as to be criticized by the State Comptroller of N.Y. last year for floating more than it needed and thus needlessly incurring a high debt service. Yet the Ford Foundation has given $200,000 to UDC. If, as I think, this is the sort of thing that UDC can surely do without the Ford money, the aim of this grant would be to take an "affirmative act" of "commitment." Whatever one may think of the justification or legality of this grant, he should recognize that this goal has been aimed for elsewhere and not achieved. I refer to the planned community of Twin Rivers in East Windsor, N.J., described in the N.Y. Times Real Estate Section of May 13, 1973, (encl. G) where the aims of housing an economic, ethnic and social cross section failed dismally of achievement. Only 18 to 20% of the families are black: most are college educated, white-collar commuters.

I believe some way should be found to make the public's protest of foundation grants to certain organizations more meaningful. Where protest has been recorded, consideration of future grants to the organization in question, by the same foundation or by a new donor, should be publicized by a notice to the protesters, giving them an opportunity to be heard at a stage where reconsideration

is possible. There are foundation centers and directories that collect information of this sort, and might be willing to assist in implementing this sort of program.

Very sincerely yours,

(Mrs.) LILLIAN BLOCH.

CANDLEWOOD LAKE DEFENSE ASSOCIATES,
New Fairfield Conn., May 11, 1974.

Hon. MICHAEL STERN,
Staff Director, Subcommittee on Foundation to Tax Laws, U.S. Senate Committee on Finance, Dirksen Senate Office Building, Washington, D.C.

DEAR DIRECTOR STERN: We address your May 13-14 staff hearing. Were the FORD FOUNDATION a private corporation, this three-billion dollar behemoth would be indicted on anti-trust charges.

In total violation of tax laws against political activity, FORD FOUNDATION is principal funder, not of one, but of ALL significant organizations and activity designed to challenge local and state law providing for local zoning. It has now added challenge to environment to its activity. It specifically funded the dubious Suburban Action Institute (of which more will be said) with $50,000 to challenge environmental considerations in court which block mass housing.

Moreover, Ford Foundation has bent to its will, purchased, and funded activities over a long period of time THAT BASE THEIR CLAIMS UPON GROSSLY EXAGGERATED PROJECTIONS OF POPULATION INCREASE, TO JUSTIFY EXPANSIONS IN PLACES WHERE SUCH NEEDS DO NOT EXIST ANYWHERE NEAR THE EXTENT CLAIMED.

The principal vehicle for the production and dissemination of such statistical falsity is the Regional Plan Association of New York. Ford is the principal funder of all its activity. However, RPA has also received, wasted, and dedicated to false projection, funds from the Dept. of Urban Development—some $650,000—in its "Choices of '76" program.

Regional Plan Association figures ARE AT TOTAL VARIANCE WITH THE UNITED STATES CENSUS, WITH EXAGGERATIONS OF POPULATION INCREASE OF RPA IN THE ORDER OF 100 to 500 or 600%, as compared with the 1970 federal census. YET, the Ford Foundation monopoly of RPA, Suburban Action Institute, and Garden Cities Development Corp. acts as a unified conspiratorial team to overwhelm small and defenseless communities, destroy their ecology, initimidate their citizens in exercise of civil rights of objection with threat of personal suit—to intimidate local law bodies wth similar personal financial threat.

Ford Foundation money is used to misuse the name of minority groups as the excuse for overthrowing local law. Always, minority citizens are presented by this complex as persons whose aspirations can in no way be satisfied, except by mass destruction of all existing value of nature, of history, of the right of towns to exist. Yet, these same minority citizens have the same needs for nature as do others, and this investigation of racial antagonism at a time when towns like ours are more than willing, and freely do, welcome such citizens into their towns on the same terms as anyone else.

At Waters Edge, Lake Candlewood, New Fairfield—now a principal objective of Ford Hatred, the name of a member of your committee, Senator Ribicoff, was grossly perverted. Waters Edge is a joint venture in which Garden Cities Development (offspring of SAI) is partner. The Senator and his brother both repudiated the effort.

At this point of our letter to your Hearing, we shall do two things: First, propose a certain legal curb on these abuses of tax law best exemplified by Ford Foundation—then, cite specific examples of statistical misrepresentation, funded and sponsored by Ford and its funded complex, designed to influence law and legislators.

A PROPOSAL FOR CONTROL OF FOUNDATIONS

Not only shall a Foundation that is tax exempt conduct no political activity in its own name, but it shall not fund, nor contribute in any way to any other organization, tax exempt or not, nor participate in any coalition or contribute to any coalition which has as its purpose the institution of litigation against any political body for the purpose of causing such body to change its laws, or to lobby for a higher body to force such change.

Any litigation, or any advocacy of any change of law, or appropriation by a political body of the People by a tax exempt Foundation shall be solely for matters of its own direct interest, and not for any abstract social concern. (i.e.—we consider it proper, for instance, for the Cancer Foundation to urge an appropriation for cancer research—or for Ford to pursue an action for its own direct financial interest, such as a tax levy upon it). Concentrated tax exempt money must not be used to thwart the will of taxpayers, expressed by elected representatives.

INSTANCES OF DIRECT ABUSE BY BODIES THAT RECEIVE FUNDING FROM FORD FOUNDATION

1. It is a fiction that the Siamese twins, jointly controlled by the Davidoff and Gold families, Suburban Action Institute and Garden Cities Development Corp. are "separate." They are not. Moreover, there is ample reason to believe that SAI has diverted its own funds to speculations of Garden Cities Development Corp. and that these funds have been lost. We enclose exhibits to illustrate.*

There is further reason to believe that Suburban Action, which shares two joint offices with Garden Cities, has assumed a disproportionate part of costs, and we have proof, legal proof, that Suburban Action Institute, at Mahwah, New Jersey, has paid for development activities of Garden Cities.

2. Other foundations, such as Rockefeller Brother Funds, Wallace-Eljabar Fund, Taconic Foundation, and we, as gathered from letters and talks, deduce that Field Foundation, No longer have renewed money to suburban action. Yet Ford has taken it on to challenege environment. All these other foundations were told the same story—that SAI and Garden Cities are "separate". All learned better.

3. The Mahwah, New Jersey, proposal of Garden Cities to add 23,000 people to a town of 14,000 is called Ramapo Mountain. This project, and the president, Neil Gold, were the feature of the 19 station telecast, funded by Ford, as presented by Regional Plan Association of New York in the Spring of 1973—also funded by Ford.

In conjunction with Ramapo mountain, *both SAI and Garden Cities, jointly,* through the mails, with return card permit 289, Tarrytown, over the signature of both Davidoff and Gold, sent out a brochure directed mainly to minority people. We send you a small part of the brochure as an exhibit.

The claims of land acquisition and the assertion of these millions of dollars of assets, designated to install confidence, covering five towns in three states, are false. They are the subject of postal complaint, and inquiry is under way. Documentary proof of falsity is available to you in the zoning testimony in New Fairfield of Jackson Walter, General counsel of Gardens Cities development Corp., Aug. 14, 1973. We submit press articles pertaining to still another development in which the false claim of acquisition was made.

THIS IS THE TYPE OF WATERGATERY THAT FORD FOUNDATION SPONSORS!

Please read the article submitted on the TWENTIETH CENTURY FUND AND DAVIDOFF AND GOLD. Subsequent articles revealed that although Gold and Davidoff, as president and chairman of both SAI and Garden Cities, who certainly had a fiduciary duty to both, ACTUALLY TOOK $92,700 odd dollars *personally,* and that $88,000 is sought for return.

REGIONAL PLAN ASSOCIATION OF NEW YORK

1. This organization proclaims the right to plan for over 300 counties from Virginia to Massachusetts. In 1968, November, barely 18 months before the 1970 Census, Boris Pushkarev, Chief Planner, published the huge SECOND REGIONAL PLAN to cover 22 counties in New York and New Jersey, and eight districts of Connecticut, Fairfield, Litchfield, and New Haven Counties.

RPA PROJECTED AN INCREASE IN POPULATION OF THE METROPOLITAN REGION, as it calls it, of 11.2 million persons between 1970 and 2000.

RPA PROJECTED a 40,000,000 increase in what it calls the Atlantic Seaboard Region in the same period. IN BULLETIN #90 (a not for general sale piece) SIX MONTHS before the CENSUS (bulletin 90 was funded by Ford), Pushkarev repeated the figures.

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*The exhibits referred to are made a part of the official files of the committee.

THESE FIGURES ARE THE BASIS OF ALL LAWSUITS AND TESTIMONY OFFERED AT ZONING HEARINGS BY GARDEN CITY AND SUBURBAN ACTION!

2. WHAT DID THE CENSUS SHOW? Well, Ford in 1971 gave RPA 252,600 dollars to "interpret" the census. In July, 1973, the "interpretation" came out. The 11.2 million increase diminished to 4.8 million!

What happened to the 40,000,000 increase? It is left to us to tote the figures and inform you that the Seaboard figure would drop to 7,000,000!

Only last month, the census released a figure that between 1970 and 1973 (1973) POPULATION IN THE NORTHEAST, THE PRINCIPAL CONCENTRATION POINT OF LAWSUIT AND ACTIVITY BY FORD AND ITS SATELLITES, population *decreased* 1.2 million!

3. How did RPA announce its downward revisions? Certainly not in forthright manner. Pushkarev published a manual stressing that population in the Metropolitan Region would gain by 7 million by year 2020, not 2000, but 2020, and he underlined the figure seven. No reference whatever to the 11.2 million.

It is a feature of RPA statistics that unless one has three or four booklets spread out, one will always gain the impression that an unexpectedly large new increase of stupendous new size has been uncovered. We consider this statistical fakery. IT IS ON SUCH A BASIS THAT ENVIRONMENT IN HUNDREDS OF TOWNS IS PROJECTED FOR ASSAULT IN THE NAME OF "MASS PUBLIC OR MASS LOW INCOME HOUSING", or the profit of unscrupulous speculators in partnership with Garden Cities.

4. The Regional Plan Association of New York projected that the population of Fairfield, New Haven, and Litchfield Counties, Conn., would total 2,900,000 by year 2000.

It had to drop the figure to 2,100,000. I wrote to INTERNATIONAL PAPER COMPANY, listed on the CHOICES of '76 BALLOT as a sponsor, that RPA had exaggerated the projected gain in population by 800,000, and that the figures were the basis of selecting Fairfield County as the main target of FORD-SAI-GARDEN-CITIES-RPA CONCENTRATION to destroy local ecology and law and institute litigation.

RPA DISPUTED ME, and claimed all it did was project a rise to 2,100,000! No reference at all to its oft-repeated figure, which is available to you in black and white, of 2,900,000.

5. I am authorized to state to you that International Paper did not authorize the use of its name as a sponsor, and I am prepared to prove it to any member of your staff.

6. MORE ABOUT THE CHOICES of '76 ballot. You see, from the sample, it is elaborate. It is costly. Over a million were printed by Moore Business Forms, listed as a "sponsor."

Actually, 47,500 responses were received. However, to make it look better, a figure of 140,000 was announced! What they did was to count each page as a separate total, and add them up . . . their population projection methods apparently being used here too. At that rate, if we added up the total of ballots cast by citizens of this country for all offices, our population would exceed China's.

7. As an example of waste of money (and HUD money was involved in the Choices program) separate offices and a large staff were maintained for many months at the premises of the GALLUP organization to "count and analyze" the tiny return. I had 94 ballots myself—none filled in. However, a certain organization did conduct "seminars" to instruct on filling them out.

8. This spurious *choices* affair is used now by FORD FOUNDATION AND ITS BENEFICIARIES as the basis to spread their monopoly of thought control. On September 21, 1973 this imperial-minded complex set up organization in Connecticut, with a full time organizer. IT IS CONCENTRATING ON ATLANTA! Atlanta has shown it can handle its own affairs in most commendable manner. Does it need Ford's RPA, soon to be followed by the SAI-Garden Cities people, to negate their progress and stir antagonism?

9. Suburban Action Institute institutted litigation against Madison Township, N. Jersey. It used RPA figures, originals, to claim exclusionary practice. The figures are wildly exaggerated. Yet, a Superior Court Judge used the RPA figures to rule against the Township, according to S.A.I. attorney who submitted the statistics.

10. JOHN KEITH OF REGIONAL PLAN ASSOCIATION OF NEW YORK, ITS PRESIDENT, recently wrote an article claiming credit for the legislation that created the TriState Regional Planning Agency of NY, NJ and Conn. The Legislature of Connecticut has been compelled to pass resolutions limiting the authority of TRI-STATE to being merely advisory, to give some modicum of protection to its citizens. TriState regularly grants research contracts to RPA, and even sponsors its requests for appropriations from the federal government, recently for over 300,000 dollars. To illustrate the total subservience and bondsmen of Regional Plan Association of New York to Ford Foundation,

ON MAY 23, 1974 THE 45TH ANNUAL CONFERENCE OF RPA WILL BE HELD AT THE HEADQUARTERS OF FORD ON EAST 42 ST., NYC

In conclusion, we question totally the validity of this tax exempt complex being permitted to smother in incompetent octopus tentacles the entire Atlantic Seaboard.

Moreover, it does not stop there. FORD IS ON THE WEST COAST TOO! It is principal funder of the NATIONAL COMMITTEE AGAINST DISCRIMINATION IN HOUSING FUNDING, of which Garden Cities President, Neil Gold, was once program director, and with which intimate, complementary relations may still be revealed if the Senate Banking Committee uses its resources to uncover them.

There are other things . . . At your pleasure, we can illustrate to you how the infiltration by Regional Plan Association itself of incorrect figures into the State of Connecticut Recreation Manual in 1965 has led to an endless chain of harassment and ecological threat to the entire Candlewood Basin and Housatonic Region of Connecticut.

There is more, more, and more, if the falsities of FORD FOUNDATION arrogance and sponsorship of statistical fakery are used in "the end justifies the means" manner.

The Senate has to decide whether the social concerns and ambitions of the entire American People are going to be decided by the Congress of the United States, or by a self-willed abuser of tax privilege on a vast scale, THE FORD FOUNDATION.

We cite the ROCKEFELLER INSTITUTE and its marvelous, non-political, research and human improvement as one extreme, the true purpose of a tax exempt foundation. THE LAW WE ADVOCATE WILL NOT AFFECT ROCKEFELLER INSTITUTE . . . IT WILL SAVE US FROM FORD.

Sincerely,

FREDERICK BENEDIKT,
Executive Secretary.

CANDLEWOOD LAKE DEFENSE ASSOCIATES,
New Fairfield, Conn., May 23, 1974.

Letter No. 2

Hon. MICHAEL STERN,
Staff Director, Subcommittee on Foundations, U.S. Senate Committee on Finance, Dirksen Office Building, Washington, D.C.

DEAR DIRECTOR STERN: Since our letter of May 11, re: FORD FOUNDATION, RPA, ETC., the following items that we believe to be of real importance have developed, or come to our attention:

1. Yesterday, the Port of New York Authority released new figures, to project transportation needs, 1970–1990, which reduce even the U.S. Census-based population-increase projections. They render still more void and self serving the Ford-Regional Plan Association figures, even the revised ones. (We attach the summary to the sheet marked "Some pertinent RPA of New York Figures, as an addenda.) This sheet was not included in our first set of exhibits. It is now important. We learned that the Suburban Action Institute case vs. Madison Township, N.J., leans heavily on original RPA figures, and we, in answer to a letter from Governor Byrne, have supplied this sheet, and others, to him.

2. Yesterday, the paper carried news that Ford Foundation will grant $5.5 million to the public broadcasting system. This is 55% of the combined amount granted by the Corporation for Public Broadcasting, and itself. The added 3.3 million required must be raised from the public.

We do not argue with the grant itself. We do emphasize that this establishes once again FORD control not only of the combine of statistical mis-information of which we wrote, but also the all-important media of mass communication, TV. It proves what we wrote you—Ford control of the spurious "Choices of '76" telecast. Since public TV is now a network, the situation has improved to some extent—but when Channel 13, N.Y., was fully independent, the total subservience to FORD-RPA-SUBURBAN ACTION INSTITUTE objectives was widely criticised. It is by no means eliminated.

This shows the need for addition to the tax law of our proposal—no tax exempt foundation to fund another such group devoted to political activity and litigation against established governments at any level. (please refer to our first letter.)

3. I just read THE SUBURBAN FRONTIER, published jointly in 1971 by SAI and the now inoperative Board of Missions of the United Presbyterian Church. A page of quotes is attached.

However, this book, available for $1 from the Presbyterian Distribution Service, 111 Varick Street, should be with Sub-Committee in full. IT CLEARLY STATES THE DEVOTION AT A NUMBER OF POINTS TO *POLITICAL ACTIVITY* ESPECIALLY OF SAI, BUT OF ALL THE PARTIES WE HAVE WRITTEN OF. I have to use my copy and am unable to give it to you.

Senator Ribicoff has most graciously written us his thanks for material we sent him. If you show him this latest, it would be greatly appreciated.

Sincerely,

FRED BENEDIKT,
Executive Secretary.

RPA arrives at the 31 county figure by subdividing 3 community counties into regions, and subdividing a bit elsewhere.

SOME PERTINENT REGIONAL PLAN ASSOCIATION OF NEW YORK FIGURES

1. The most important one of all is the overriding prediction of the Second Regional Plan of 1968 that population in what they choose to call the "31 County Metropolitan Region" would rise from 18,980,900 (1965, itself an inflated figure—NYC wound up in the 1970 census with fewer than RPA's 1965), to 30,180,000 by year 2000, a jump of 11,199,100.

Included was a jump for Jersey from 5,418,900 to 10,300,000. The total Jersey gain was set at 4,881,100. (we gave you a reprint table)

2. The July newspaper release NOW SETS 4.8 million as the total for all, less than the projected increase of Jersey alone. However, in their articles, RPA likes to refer to the 4.8 as "about five million."

The 1968 plan came out in November, one and one half years before the census. Bulletin 90, (private) of Sept. 1969, six months before the census, repeats the same figures, repeatedly defends the 40,000,000 Atlantic Seaboard increase by yr. 2000, and speaks doggedly of the impossibility of that region's failing to maintain its traditional standards of growth, and in another bulletin, refers to the price as being merely the demolition of some landmarks.

3. Bergen County—predicted a jump from 1965 to 1,450,000 in yr 2000 from 849,300. The new figures (1970 census) showed Bergen with a pop. 897,100. (1940-409,600).

The new RPA projections are: Bergen County, 1985—1,050,000; 2000—1,150,000. Instead of a jump of 600,000, it is now 253,000, and 153,000 by 1985.

4. AT THIS POINT, some of the absurdities of Mahwah become evident . . . They place a "regional" household at 3.19 persons per unit . . . Unlimited households certainly approach 4—by unlimited household I mean no limit to bedrooms, a universal Garden Cities figure . . . In Mahwah, that means 20,000 to 24,000 population increase.

Staying in the 20,000 to 24,000 range for those 6,000 Mahwah units, one sees Garden Cities is asking that 14 to 16% of the entire "projected increase" of Bergen by 1985 fall within a total area of 600 acres, and a built area of only a third or a quarter of even those 600 acres.

Also, the density of New York City overall is some 24,000 per square mile. Mahwah would equal or exceed the average density of NYC.

A similar situation exists in New Fairfield, where on 63 of 253 acres they would load 8,000 to 10,000 of the 157,100 increase predicted for all of Fairfield County, which I believe is much larger in area than Bergen County.

5. They propose an increase in density for Bergen County and that region to 4920 per sq. mile overall, to be exceeded in Mahwah 4 or 5 times over.

These are some of the more obvious figures revealed. Without doubt, a Jersey statistician, with Jersey State figures available, should be able to extend these conclusions. In any case, GARDEN CITIES INVARIABLY GRAVITATES TO THE AREAS OFF WILDES EXAGGERATION BY RPA. The promised opening of a new plan is enough to cause RPA's ally, the Davidoff-Gold complex, scurrying in search of a disgruntled developer, the greedier and more disreputable the better.

MAY 22, 1974.

ADDENDA TO STATISTICS OF RPA—BASED ON PORT OF NEW YORK AUTHORITY

Salient points:

1. Demand for jobs in the 22 County Region of the Metropolitan Area between now and 1990 will outrun the supply, although the supply of jobs will increase.
2. Population increase, 1970 to 1990, is placed at 12.6% over the 1970 census, to reach a total of 20.2 million over the census figure of 18 million.

(RPA originally projected a gain hugely in excess, reaching to 30.2 million by yr. 2000, for the same counties, plus Litchfield and New Haven Counties, Connecticut, which were small factors in the total.)

3. Because of smaller families expected, demand for apartments, plus other type, housing will reach 19%, with a somewhat greater bias toward apartments, owing to small families.
4. The rate of population increase, because of lower birth rates, is now BELOW ZERO INCREASE IN THE TWENTY-TWO COUNTIES.
5. The 12.6% projected increase in population, 1970–1990, compares with 28.5% in the 1950–1970 period.
6. While continuing, the movement toward the suburbs will decline.

* * * * * * *

Analysis of these figures indicates two things:

A. The existing zoning regulations in practically all communities do not deter growth, by the hitherto natural means, AT THE RATES INDICATED BY THE POPULATION INCREASES.

It would be hard to find communities in the Metropolitan Region that fail to grow by rates much greater than prescribed as a necessity by these figures.

B. Such growth, and local planning, does not require the intervention of Ford, or its satellites—

Or, the confessedly insincere suits, deliberately tailored to be radical and unacceptable in their demands, as described in the book, co-published by SAI, entitled, "The Suburban Frontier."

(News note: Yesterday, the Board of Selectmen of New Fairfield felt itself compelled to issue public warning to boatmen to use caution in approaching THE UNLAWFUL DAM OVER LAKE CANDLEWOOD BUILT BY GARDEN CITIES-SAI IN A JOINT VENTURE—and to write urgently to the safety division of the State Boating Commission and the Lake Authority of the hazard. Following that, a near accident on the shoal was witnessed and reported to Candlewood Lake Defense Associates.

Quotations from "The Suburban Frontier", co-published by Suburban Action Institute and (inoperative) Board of Missions of United Presbyterian Church, USA.

Page 25—"another issue at the very heart of the institute will need resolution in the near future. Two models seem to be competing against each other. One was identified by one of the Institute's co-directors as "stealing from a bank." Under this image, sophisticated thieves set the sights on a particular bank, study its alarm systems, the type of safe, its possible vulnerabilities, and then move in with the the sophisticated tools and knowledge of safe-cracking techniques and alarm-breaking mechanisms. More specifically, the activist model under this image is composed of a group of experts who move into a community, study the functioning systems well, and then with their expertise in city-planning, confrontation politics and law manipulate and maneuver those systems so well that the operating system is forced to produce the desired effects. The power-levers under this model include such tools as law, utilization of the press, and federal intervention, to all of which are used to pry open the cache of valuables.

The second model relies more upon educating suburban residents to the need for economically and racially-integrated communities and then moves to organize them to press for structural changes in their own communities to that end.

(Some lines omitted here.) Conclusion of paragraph is: Unlike the first model, which must expect a certain amount of community retaliation, this second model functions on the basis of trust and cooperation."

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(Our note: the frank invocation of politics by SAI would seem to be in violation of laws regarding tax exempt bodies.)

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Page 39—"Confrontation" is primarily a strategy headed up by outsiders who have little to lose in their confrontation venture.

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Page 39—"A second point which the history of confrontation would seem to indicate is that confrontation is primarily for the purpose of raising the issue. As such, confrontation: (1) should be radical in its demands, and (2) other more moderate groups working under different strategies must pick up the pieces and work 'with' the confronted institution to implement the programs which are a response to the confrontation."

* * * * * * *

Page 39—Confrontation efforts by radical organizations often are accused of not being politically realistic in their demands. Such an accusation in itself is politically naive. If confrontation demands and tactics were politically realistic—which means more moderate—they would not be listened to, nor would they be out on the frontiers of social movement.

* * * * * * *

Page 40—a lengthy paragraph describes Suburban Action Institute as having "A particular confrontation approach appears to warrant more attention by social activists than has heretofore been the case. The Suburban Action Institute provides a concrete example of the approach * * *"

Other parts of the booklet state trained organizers, to come in as outsiders are needed—untrained people not satisfactory.

Other important sources—US Census—Bulletin 90 (private) RPA; 2nd Regional Plan of 1968.

PEPPER, HAMILTON & SCHEETZ,
Washington, D.C., July 25, 1974.

Subject: Written comments on sections 4940 and 4942 of the Internal Revenue Code of 1954.

Attention: Michael Stern, Staff Director, Senate Finance Committee, 2227 Dirksen Senate Office Building, Washington, D.C. 20510.

VANCE HARTKE, *Subcommittee Chairman,*
Senate Finance Subcommittee on Foundations,
Dirksen Senate Office Building,
Washington, D.C.

DEAR SENATOR HARTKE: On behalf of the Ad Hoc Committee on Family Foundations (comprised of The Hormel Foundation, The Kellogg Foundation, The Kresge Foundation, Lilly Endowment, Inc., The Maclellan Foundation, The Pew Memorial Trust and The Woodruff Foundation) we thank you for the opportunity to discuss the inequities associated with the minimum investment return as adopted in Section 4942. In particular, we could like to point out that: one, Section 4942 will require divestituture of stock which is not required to be divested under Section 4943; and two, the fair market value of stocks does not reflect the dividend paying capacity of a corporation, and therefore, the minimum investment return is irrational since it is expressed as a percentage of the fair market value of the assets held by a private foundation.

The foregoing problems were presented in detail when the Ad Hoc Committee testified before the Committee on Ways and Means on April 10, 1973. A copy

of that testimony and written statement, along with a study by Dr. Norman Ture, is hereby submitted to your Subcommittee for the record.[1]

At that hearing, the Group endorsed the Congressional action taken in 1969 to eliminate certain abuses previously associated with private foundations but asserted that some of the measures adopted were unduly restrictive. In particular, unless Section 4942 is amended, immediately, the country's existing pattern of charitable grants will be altered to the detriment of the nation. Section 4942 was designed to prevent minimization of current increases by investment in growth stocks—it threatens to operate to produce foundation liquidation.

No specific recommendation for the form of amendment to Section 4942 was presented on April 7, 1973, since it was believed more important, first, to establish the fact that Section 4942 currently is a slow acting death sentence for private foundations and, second, the elimination of foundations has the potential for altering the country's future by eliminating an important portion of its funds available for the private charitable sector. Based upon the reaction of many who heard or have read the testimony, the Group believes it sustained its case.

Subsequent to the presentation before the Committee on Ways and Means, the Committee on Senate Finance determined that Section 4942 should not overrule the divestiture transition rule for the Herndon Foundation in Section 101(1)(4) of the Tax Reform Act of 1969. The Senate adopted the Committee's action in H.R. 6642. Similar relief should be provided for all private foundations to the extent that they too are not required to divest stock under Section 4943.

In regard to general legislation concerning Section 4942, the Committee on Ways and Means previously attempted to alleviate the problems in Section 4942 when it unanimously reported out H.R. 11197 in 1971. Unfortunately, the 92nd Congress was not able to consider H.R. 11197. That bill would have reduced the income equivalent from six to five percent and provided certain transition rules to allow foundations the opportunity to adjust to Section 4942 (a minimum distribution of three and one-half percent for 1972 and 1973, four percent for 1974 and 1975, four and one-half percent for 1976 and 1977 and a five percent ceiling thereafter). Its substantive provisions were the result of coordination with the Treasury. Hopefully, either the Committee on Ways and Means or the Committee on Senate Finance will consider favorably legislation similar to H.R. 11197.

In connection with the overall reduction of the minimum investment return, it should be pointed out that such a reduction would be consistent with the analysis of the Peterson Report to the Committee on Senate Finance. That report recommends a 6 percent to 8 percent figure after examining *total rate* of return of mutual funds and taking into account a rate of inflation of from *1.6 percent to 2 percent*. In the words of the Report.

"Thus, if the objective were that one should permit a reasonable investor to earn enough to maintain the purchasing power of his assets—then one could require an annual payout to charity of from 6% to 8%." (Report, page 84)

The language in Section 4943(e)(3) permits a variation in the rate fixed in the statute. It only mentions ". . . the relationship which the money rates and investment yields for the calendar year 1969 . . ." means to current rates and yields. No reference is made to corpus growth or to inflation although these factors figured in the Peterson analysis.

Based upon Standard & Poor's 500 stock average for the years 1970 through 1972, there has been virtually no net annual return taking into account rates, current yield and inflation. If the years from 1959 through 1973 are taken into account, a net annual rate average of about 4.5 percent is shown. See attached table prepared by The Glenmede Trust Co.

The index at the end of 1973 only begins to suggest the problem private foundations are going to have in the future if there is no change in the statute. The current yield figure for 1969 was 34.3 percent on Standard & Poor's and the present current yield is 4.3 percent. Intermediate governments are at 8.09 percent; short term at 8.44 percent. Thus, the Treasury could ultimately decide upon an index of 8 percent or more in the future which would require a significant corpus invasion even though the corpus has shrunk in dollar value during the year while its purchasing power suffered a 10 percent debasement by inflation. This clearly would be an unintended result by Congress in adopting a minimum investment return which was not to act as a divestiture provision.

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[1] House Ways and Means Committee hearings entitled "General Tax Reforms," pp. 5859.

In summary, it should be clear that the statute has an incomplete standard for determining whether a foundation is distributing an adequate amount and sets forth an excessive percentage based upon experience from 1969 to date. Thus, if the Peterson Report were being currently prepared, it might well call for a 4 percent figure. Moreover, to the extent the money market rates are increased to match inflation, the present statute may require a most unfortunate invasion of corpus even in years in which the purchasing power of the corpus has shrunk—certainly after applying an inflation factor.

Respectfully yours,

H. LAWRENCE FOX.

Enclosures.

Year	Standard & Poor 500 year-end closing price	Percent			Total yearend holding to beginning	Percent		
		Annual growth rate	Standard & Poor 500 current yield	Annual return		Annual inflation rate	Annual loss due to inflation	Net annual return
1958	$55.21							
1959	58.89	6.67	3.06	9.73	$109.73	4.16	4.56	5.17
1960	58.11	−1.32	3.35	2.03	102.03	1.72	1.75	.28
1961	71.55	23.13	2.82	25.95	125.95	1.23	1.55	24.40
1962	63.10	−11.81	3.38	−8.43	91.57	1.14	1.04	−9.47
1963	75.02	18.89	3.04	21.93	121.93	1.28	1.56	20.37
1964	84.74	12.96	2.95	15.91	115.91	1.56	1.81	14.10
1965	92.43	9.07	2.94	12.01	112.01	1.90	2.13	9.88
1966	80.33	−13.09	3.57	−9.52	90.48	2.80	2.53	−12.05
1967	96.47	20.09	3.03	23.12	123.12	3.14	3.87	19.25
1968	103.86	7.66	2.96	10.62	110.62	3.99	4.41	6.21
1969	92.06	−11.36	3.43	−7.93	92.07	4.88	4.49	−12.42
1970	92.15	.09	3.41	3.50	103.50	5.46	5.65	−2.15
1971	102.09	10.77	3.01	13.78	113.78	4.71	5.36	8.42
1972	118.05	15.63	2.67	18.30	118.30	3.15	3.73	14.57
1973	97.55	−17.37	3.46	−13.91	86.09	5.40	4.65	−18.56
Average								4.53

McLEAN, VA., *May 24, 1974.*

Mr. MICHAEL STERN,
Committee on Finance,
Washington, D.C.

DEAR MR. STERN: I am a trustee of several small, tax-exempt organizations: the Phelps-Stokes Fund of New York, the African Student Aid Fund of New York, the Institute of Intercultural Studies of New York, and the Institute for Psychiatry and Foreign Affairs of Washington, D.C. In my capacity as director of seminars at the Smithsonian Institution, I enjoy an unusual vantage point from which to observe the interplay of resources provided through direct federal appropriations and public money managed by corporations and foundations in their philanthropic roles. My comments below, however, do not reflect any "policy position" of the Smithsonian as that unique "private-public mechanism," but paraphrase what I wrote in 1967 as a private citizen in response to a *Washington Post* article (Jan. 23, 1967) by Henry Fairlie, the British journalist, who claimed: ". . . the way in which the great foundations operate in the U.S. is near to a public scandal. They are bodies wielding irresponsible power, subject to no public control, whose power is large, is increasing, and ought to be diminished."

My reply, in a draft of an unpublished article, seems pertinent to some of the points raised by Senator Hartke in his February 8 speech printed in the April 11, 1974 *Congressional Record:*

"The proposition I would like to have considered is that the private nature of foundations is something of a myth, so that if 'public' is better than 'private' from a British point of view, Fairlie might understand that the whole ensemble of foundations, big and small, functions as an American version of a Ministry of Education, Science, and Culture in 'normal' countries. The various foundations might then be interpreted as serving as semi-autonomous bureaus of a

bigger 'ministry.' All his rests on the assumption that tax laws, publicly administered and enforced, make foundations possible.

"A corollary to this point is that to make them conform to our old-fashioned notion of civics, we need to work out a symbiotic relationship between philanthropoids and those who petition for money. That is, we idealize now the notion that public servants have obligations to respond—directly and indirectly—to the suggestions made by taxpayer citizens. Citizens are encouraged to make their views known to elected officials—and appointed ones. Though such civics is imperfectly practiced, the ideal remains. Such an ideal relationship ought to exist between those who hand out money and those who have good ideas about how it should be spent, i.e., those who appeal for tax-exempt funds. The foundation officer need not agree with the suggestions, and can decline the opportunity. But some adult education is needed to make the present stewards of 'public' funds—money foundations can spend because the government lets them—more solicitious of help from people who ought to be perceived as 'idea men,' rather than those begging for alms from the rich. The act of petitioning for such funds in the public interest is an exercise of the obligations of citizenship. The preferred attitude is illustrated by an apochryphal comment attributed to Prof. Kenneth Boulding, the economist, in an exchange with a Ford Foundation officer about a pending grant to support the professor's research: 'If you don't watch out, I might wind up not asking you for a grant at all!'

"Greater public control over foundation resources should come from this direction of citizen participation than from formal government supervision which already has intimidated many foundations to the extent that they are increasingly less effective as creative and innovative sources of initiative. Moreover, those who ask for money should come to realize that they are doing a favor to the foundation officers, and that it is their civic duty to press continually suggestions upon the foundations regardless of whether something is 'in program' or 'out of program' at a given time.

"It is wrong to think that foundations' unique purpose is to distribute money. Along with the transmission of cash for the public good, foundations provide many other services in a kind of secular ministry: listening to citizens' problems, providing referrals, serving as a web or network of clearinghouses through which money, ideas, and human talent can find the right combinations leading to action. Complex, industrial civilizations need such combinations of linkages between the parts to make society function. Even the most monolithic state structures such as the U.S.S.R. have to depend on informal communications and some entrepreneurial initiative of smaller units to function. Not all 'interlocking directorships' are pernicious or elitist. For example, the tax laws which allow the Rockefeller Foundation (among others) to operate provide the legal, if not the fiscal, basis for a number of civic actions by its officers. I refer to the frequent use the National Academy of Sciences has made of Rockefeller scientists on its various braintrusts dealing, say, with problems of developing countries and health and agriculture in our own society."

Sincerely yours,

WILTON S. DILLON.

BRADLEY, ARANT, ROSE & WHITE,
Birmingham, Ala., May 7, 1974.

Re: Hearings on IRS Administration of Private Foundation Rules.

SUBCOMMITTEE ON FOUNDATIONS FINANCE COMMITTEE,
U.S. Senate, Washington, D.C.

DEAR SIR: In connection with the hearings on the administration of tax laws pertaining to private foundations by the Internal Revenue Service, this firm wishes to point out the most significant administrative problem encountered by our foundation clients. The basic problem is that the amount of the tax imposed under Chapter 42 of the Code is generally so modest that the foundation against which a deficiency is asserted cannot hire counsel to defend against the deficiency without spending more than the amount of the tax. Consequently, even if the tax is not due, the foundation is placed in the position of paying the tax or paying as much or more to a lawyer to contest the tax. Two effects have ensued from

these circumstances. First, the foundations have generally been inclined to simply pay the tax as a kind of extortion payment. Second, the IRS personnel administering the foundation rules appear to have taken a very narrow and restrictive approach to the provisions because the foundations are unable to contest their actions.

To illustrate, we requested during the latter part of 1973 permission on behalf of the E. T. Comer trust to set aside income earned in 1972 pursuant to the provisions of Section 4942(g)(2). The reason given for the proposed set-aside was that the foundation had originally had three charitable beneficiaries, a county road, a public cemetery, and a general category described as the education of poor children in a certain county. It was inappropriate to spend the income from 1972 on the road because the road had become a state highway; likewise, it was inappropriate to spend the money on the cemetery because adequate funds had already been provided for its maintenance. However, the foundation had not received its permission under Section 4945(g) to make education grants until the latter part of 1973 and, therefore, did not have time to spend the 1972 income pursuant to the scholarship program.

In response to the request for set-aside, the IRS ruled that the set-aside was not appropriate because the facts did not show that a "specific project" was involved or that the project was one which could better be accomplished by a set-aside than by an immediate payment of the funds. In spite of the fact that the amount of the tax under Section 4942 would only amount to $800, we nevertheless proceeded to protest the denial of the set-aside. However, the exempt organizations branch in Atlanta was wholly unmoved by our contention that the set-aside provision certainly must have been intended to apply in the circumstances simply because it was not possible to distribute the income within the time required by Section 4942. The national office has now requested a brief from the foundation in support of its protest of the decision of the Atlanta office. The difficulty faced by the foundation is that a further brief will cause the foundation to expend a substantial part of the amount of tax involved.

Although it may be that no solution to the problem exists, it would be appropriate for the subcommittee to consider the circumstances.

Sincerely yours,

JAMES WILLIAM LEWIS.

THE ZELLERBACH FAMILY FUND,
San Francisco, Calif., June 10, 1974.

Senator RUSSELL B. LONG,
U.S. Senate,
Washington, D.C.

DEAR SENATOR LONG: The enclosed copy of the 1973 Annual Report of The Zellerbach Family Fund may be of interest as demonstrating the work of one medium sized private foundation.

The report is brief and presented in a modest fashion because our primary purpose is to use funds for needed programs.

We recognize that primary funding for essential services in society must come from broadly based community and federal sources. Foundations such as ours can, however, initiate and sustain programs that are innovative and experimental, and provide experience that can be used by others.

I would be pleased to respond to any questions that you have about the operation and policies of the Fund.

Cordially and sincerely,

HAROLD L. ZELLERBACH,
President.

Enclosure.

ANNUAL REPORT—FOR THE YEAR ENDED DECEMBER 31, 1973

OFFICERS—1973

Harold L. Zellerbach	President
William J. Zellerbach	Vice President
Louis Saroni, II	Treasurer
Rosemarie Zilka	Secretary
Edward Nathan	Executive Director

DIRECTORS—1973

Philip S. Boone	Louis Saroni, II
R. Stanley Dollar, Jr.	Harold L. Zellerbach
Philip S. Ehrlich, Sr.	William J. Zellerbach

The Zellerbach Family Fund along with other modest sized foundations formerly used its funds primarily to launch new, useful community organizations. In the 1960s it was possible to start day care centers, outreach neighborhood service programs, specialty counseling services and small performing art groups with confidence that these programs would then receive continuing support from traditional government or community funding agencies after the seed money phase had run its course. Unfortunately, the seed money concept grew but the sources of steady nourishment did not keep pace in the seventies.

Tight money, the rediscovery of basic unmet human needs, and government spending ceilings have forced a reshaping of granting policy in the direction of sustaining and contributing to new developments in established organizations.

In 1973 the Board of The Zellerbach Family Fund supported many innovative demonstration projects but did not establish new organizations. Funds were used to permit talented staff of existing institutions to develop and demonstrate new programs in education, mental health and in the performing arts.

The following examples include some projects supported by the Fund in 1973:

Project and organization

Children of Divorce, Marin Community Mental Health Service.
New Family Project, San Francisco Unified School District.
Children's Trauma Center, Children's Hospital of the East Bay.
Neighborhood Arts Program, San Francisco City and County Art Commission.
Institute on Human Sexuality, University of California School of Medicine.

These demonstration projects have value beyond San Francisco because they develop theory and provide technical information on specific ways to deal with problems that face all communities.

The Zellerbach Family Fund has also maintained its support of cultural activities in San Francisco. Grants have given encouragement and recognition to dance and instrumental groups who help to create a rewarding community environment. New talent is offered an opportunity for expression. Experimental theater and dance is supported by grants to:

Western Opera, Spring Opera, Xoregos Dance Co., Stanze Peterson Dance Co., Performing Arts Workshop.

In 1973 in response to an extraordinary crisis in the public funding of urgently needed services The Zellerbach Family Fund along with three other foundations established an emergency fund in cooperation with the United Bay Area Crusade. These funds have been used to help child care, rehabilitation services, after hours care, and programs directed toward the developmentally disabled. Without this emergency funding these programs would have been shut down or dramatically curtailed. The joint funding that The Zellerbach Family Fund helped make available permitted services to continue uninterrupted, and made possible consultation and joint planning efforts of long-term benefit to the community.

The following list indicates grants made by The Zellerbach Family Fund during 1973, as grouped in these categories; Art and Performing Arts; Building Funds; Education; Federated Funds, Health and Community Welfare.

Each recipient of funds prepared a grant request and provided fiscal and progress information required by the Fund.

The "Instructions For Submitting Applications" and "Conditions Governing Grant Acceptance" have been included as the last pages of this report.

Responsible grantmaking in the interest of the community has required many hours of study on the part of the Board. We believe that this annual report reflects our attempt to meet a high standard of responsive and responsible foundation management.

Arts and Performing Arts

Organization and program description

African Peoples Theatre—Workshops and repertory theater offering original productions concerned with Black culture and the experience of the Black community.

American Conservatory Theatre—Drama training, student matinees and general operating expense of repertory theatre.

American Institute for Cultural Development—Introduction of cultural resources into school curriculum. Enables low income families to attend major cultural events through ticket purchase and transportation.

Berkeley Promenade Orchestra—Classical music in museum setting that provides multiple aesthetic experiences at modest prices to an expanded listening audience.

Berkeley Repertory Theatre—Emergency grant to meet operating expenses of resident professional theatre company in Berkeley.

California Palace of the Legion of Honor—To catalog and preserve the prints and drawings of the Achenbach Collection of Graphic Arts.

Chinese Cultural Foundation—Emergency grant toward finishing construction. An attempt to improve understanding, and link East and West through cultural exchange.

City and County of San Francisco Neighborhood Arts Program—Expansion and development of workshops, festivals and performances in neighborhoods throughout San Francisco.

Performing Arts Building—Development and study costs for proposed Performing Arts Building.

East Bay Music Center—To promote quality music learning opportunities for East Bay residents.

Heirs Inc.—To enable young Bay Area Poets and authors to publish creative works.

Mother Goose—Music, threatre, craft and dance programs for institutionalized youth and adults.

Performing Arts Workshop—To support creative dance program and teaching effort in dance and theater production with adolescents and adults.

San Francisco Art Institute—Operating expenses for fine arts school with emphasis on drawing, sculpture, ceramics, printmaking, photography and film.

San Francisco Ballet Association—Toward maintenance of the San Francisco Ballet Company.

San Francisco Conservatory of Music—Initiating three-year grant for staff stabilization and faculty development.

San Francisco Dancers Forum—San Francisco Dancers Forum High School Dance Project—a performing company, selected from dancers from scholarship program for limited income youth, appearing in schools and community.

San Francisco Symphony Association—General maintenance support of Symphony Orchestra.

Spring Opera of San Francisco—Toward production costs of opera season.

Stanze Peterson Dance Theatre—To support fully integrated contemporary dance company known for excellent repertoire.

Talent Bank Foundation—Reserve funds for development of opera presentation and opera workshops within public schools.

Western Opera Theatre—To permit continued opera performances in Bay Area Schools and the development of talented young artists.

Xoregos Dance Company—To support outstanding contemporary dance company with varied program and creative choreography.

THE ZELLERBACH FAMILY FUND

ARTS AND PERFORMING ARTS GRANTS
for the year ended December 31, 1973

	Commitments Unpaid 12/31/72	Commitments Authorized 1973	Paid 1973	Unpaid 12/31/73
African Peoples Theatre	$	$ 2,000	$ 2,000	$
American Conservatory Theatre		5,000	5,000	
American Institute for Cultural Development		5,000		5,000
Berkeley Promenade Orchestra		3,000	3,000	
Berkeley Repertory Theatre		1,000	1,000	
California Palace of the Legion of Honor	13,340		13,340	
Chinese Culture Foundation		1,000	1,000	
C & C of San Francisco - Performing Arts Building		3,750	3,750	
East Bay Music Center	2,500		2,500	
Festival of Dance		500		500
Heirs Inc.		1,000	1,000	
Mother Goose		5,000	5,000	
National Endowment for the Arts (NAP)		30,000	30,000	
Performing Arts Workshop		5,000	5,000	
S. F. Art Institute		5,000	5,000	
S. F. Ballet Association		75,000	50,000	25,000
S. F. Conservatory of Music	10,000		5,000	5,000
S. F. Dancers Forum		1,985	1,985	
S. F. Symphony Association	5,000	5,000	5,000	5,000
Spring Opera of San Francisco		6,000	4,000	2,000
Stanze Peterson Dance Theatre		2,000	2,000	
Talent Bank Foundation		3,000		3,000
Western Opera Theatre	5,000		5,000	
Xoregos Dance Company		7,000	2,000	5,000
Total - Arts & Performing Arts	$ 35,840	$167,235	$152,575	$ 50,500

FEDERATED FUNDS

Organization and program description

Jewish Welfare Federation of San Francisco, Marin County and the Peninsula—Local program services and overseas support of philanthropic activities.

Foundations—UBAC Emergency Fund—To meet emergency financing needs of UBAC agencies whose programs are endangered through sudden governmental policy changes.

Agencies supported include: Chinese Newcomers Service, Travelers Aid, Aid to Retarded Children, Watoto Weusi School, S. F. Community Rehabilitation Workshop.

United Bay Area Crusade—To support a variety of social services and specialized programs in the San Francisco Bay Area.

	Unpaid 12/31/72	Authorized 1973	Paid 1973	Unpaid 12/31/73
Branson School	$	$ 2,000	$ 2,000	$
Pacific Medical Center	5,000		5,000	
Paramount Theatre of the Arts		2,500		2,500
St. Luke's Hospital	5,000		5,000	
S. F. Museum of Art	15,000		5,000	10,000
S.F. University High School		5,000		5,000
University of Pennsylvania	120,000		30,000	90,000
University of Southern California	25,000		25,000	
Total Building Funds	$170,000	$ 9,500	$ 72,000	$107,500

EDUCATION

Organization and program description

Alvarado School Art Workshop—Continued support of art projects in public schools under direction of Ruth Asawa.

Bay Area Engineering Society's Committee for Manpower Training—To provide opportunities for minority workers to develop skills and to gain knowledge to establish careers in engineering.

Community Council for Mutual Education—To improve education and learning for students through improved understanding of concerns of teachers; to improve communication between teachers; between parents and teachers and teachers and students.

Council on Foundations—Educational, informational and organizational materials to promote efficient and useful foundation administration.

Encounter Theater—Resolution of conflict in school and between parents and children through drama, role playing difficult living situations, and through humor.

Foundation Center—To make foundation grant information available in libraries throughout the United States.

Golden Gate University—To support management in the Arts Curriculum.

La Raza En Accion Local—Program dealing with economic and social problems of Spanish speaking community.

Multi-Culture Institute—Specialized school program that preserves cultural and ethnic identity while developing appreciation for unique contribution of various peoples.

Pacific University—Scholarship program for students in financial need.

Public Advocates—Law student intern program in non-profit community law firm.

San Francisco African American Historical Society—To preserve culture, to develop programs and to support museum under sponsorship Black Community.

San Francisco Foundation—To publish Bay Area Foundation Directory.

San Francisco Unified School District New Family Project—Outreach service program to children and parents new to San Francisco.

Strybing Arboretum Society—In support of expanded educational program for elementary school students.

University of California, Berkeley—Bancroft Library—To conduct oral interview series "Arts in the Community".

University of California School of Law—Operating expense of Ecology Law Quarterly under management of law students.

University of California School of Medicine—San Francisco—To support clinical and educational program of Institute on Human Sexuality.

University of California—Santa Cruz—Toward equipment for marine research vessel.

Women's History Research Center—Support of librarian to classify and catalogue unique collection of books, pamphlets and clippings about women and their concerns and contributions.

Yosemite Institute—To develop a curriculum and plan for Yosemite National Park to be used as an environmental teaching center.

YWCA—Berkeley Black Women's Unit—Leadership development and community action program for Black women on campus.

THE ZELLERBACH FAMILY FUND

EDUCATION GRANTS
for the year ended December 31, 1973

	Commitments Unpaid 12/31/72	Commitments Authorized 1973	Paid 1973	Unpaid 12/31/73
Alvarado School Art Workshop	$	$ 5,000	$ 5,000	$
Bay Area Engineering Society's Cmte. for Manpower Training		5,000	5,000	
Community Council for Mutual Education		7,500		7,500
Council on Foundations	10,000		2,000	8,000
Encounter Theater	3,000	7,500	10,500	
Foundation Center		4,500	1,500	3,000
Golden Gate University		1,000	1,000	
La Raza En Accion Local	3,750	7,500	7,500	3,750
Multi-Culture Institute		10,000	10,000	
Pacific University		10,000		10,000
Public Advocates		10,000	10,000	
San Francisco African American Historical Society		5,000	2,500	2,500
San Francisco Foundation	500	750	1,250	
San Francisco Unified School District		27,000	6,750	20,250
Strybing Arboretum Society		7,125	7,125	
University of California - Bancroft Library		14,489		14,489
Ecology Law Quarterly		2.500		2,500
San Francisco-School of Medicine		16,000	8,000	8,000
Santa Cruz	5,000		5,000	
Women's History Research Center	5,000	5,000	10,000	
Yosemite Institute		7,500	7,500	
YWCA - Black Women's Unit		10,000	5,000	5,000
Total Education	$ 27,250	$163,364	$105,625	$ 84,989

BUILDING FUNDS

Art

Paramount Theater of Arts, Oakland—Building purchase and remodeling.
San Francisco Museum of Art—Expansion and remodeling.
University of Pennsylvania—Towards Performing Arts complex.

Education

Branson School—Library complex.
San Francisco University High—School building.

Health

Pacific Medical Center—Hospital improvement.
St. Lukes Hospital—Hospital improvement.
University of Southern California—Student Health Center.

	Unpaid 12/31/72	Authorized 1973	Paid 1973	Unpaid 12/31/73
Jewish Welfare Federation	$ 25,000	$ 30,000	$ 35,000	$ 20,000
United Bay Area Crusade Foundations Emergency Fund		75,000	37,500	37,500
Regular	20,000	20,000	20,000	20,000
Total Federated Funds	$ 45,000	$125,000	$ 92,500	$ 77,500

HEALTH AND COMMUNITY WELFARE

Organization and program description

Advocates for Women—Support women's economic development center to secure industry contracts and to offer apprenticeship positions, training and counseling for women in the job market.

American Hospital of Istanbul, New York—Toward support of a program of nurses' training and general hospital operation.

Berkeley Runaway Center—Youth Alternatives Program—Crisis Intervention and coordinated care effort on behalf of troubled and transient youth.

Center for Independent Living—Program support to enable handicapped youth to live independently and to encourage city planners to consider the needs of the handicapped.

Children's Hospital Medical Center of the East Bay—Children's Trauma Center—Comprehensive community coordination and direct service program to prevent child abuse, to offer protection to children and counsel to parents who are concerned about harm to their children.

Chinatown Northbeach Youth Services and Coordinating Center—Local match to secure federal funds to prevent delinquency among youth in Chinatown. To enable community resources to help youth in own neighborhood in preference to institutionalization.

Community Streetwork Center—Community outreach program for youth considered susceptible to delinquent behavior.

Contra Costa County—Y.W.C.A.—Transportation project for poverty clients in need of community services.

County of San Mateo—Community Youth Responsibility Program—Community involvement program to prevent juvenile crime and to offer rehabilitation alternatives in preference to incarceration.

Earl Paltenghi Youth Center—Community center and vocational counseling effort directed toward minority youth.

Friends of the San Francisco Deputies and Inmates—Start-up costs for organization to improve conditions and services in San Francisco county jail.

Marin Community Mental Health Service—Children of Divorce Project—To initiate a counselling service and research study directed toward children of parents in the process of divorce.

Marin Open House—Wilderness Project—Drug treatment program incorporating "Outward Bound" principles intended to promote self-reliance, trust and personality growth.

Mission Childcare Consortium—Local match for federally funded day care and treatment center for abused children and their parents. To evaluate the effectiveness of a variety of treatment methods.

Mount Zion Hospital and Medical Center—Harold Brunn Institute—To support research relating to personality type and stress management to coronary disease.

Mount Zion Hospital and Medical Center—Family and Child Crisis Project—An outreach preventive and corrective mental health service.

National Association of Social Workers, Golden Gate Chapter—To improve demonstration project concerned with institutional racism and social welfare agencies. Study and consultation effort to improve access and quality of service to consumer groups.

Potrero Hill Youth Legal Center—Alternative rehabilitation program for youth involved with probation department.

Resource One—Community computer project for social needs.

San Francisco Citizens League—To support summer activities determined useful by participating youth groups.

San Francisco Lawyer's Committee for Urban Affairs—To enable the legal profession to use their skill and to direct their competence to solve the legal problems of San Francisco's poor and minority communities.

University of California, San Francisco School of Medicine, Alcoholism Project—To determine constitutional reaction to alcohol and to develop treatment program to prevent destructive response.

Volunteer Bureau—San Francisco—To develop and evaluate planned volunteer service opportunities for population likely to need hospitalization for emotional problems and to provide opportunity for residents recently returned from state hospitals.

Westside Community Mental Health Center—Audrey L. Smith Developmental Center, Inc.—Start-up costs and essential equipment for innovative developmental center serving minority community.

Westside Community Mental Health Center—City College of San Francisco—Development and maintenance support of a health and counselling service at City College of San Francisco.

Westside Community Mental Health Center—Progress Foundation—To bring residential facility to building code standard in order to accommodate persons who formerly would be sent to a state hospital or less desirable setting.

Youth for Service—Operating funds for skill training, job development, street work and remedial education program for youth with limited opportunities.

THE ZELLERBACH FAMILY FUND

HEALTH AND COMMUNITY WELFARE GRANTS
for the year ended December 31, 1973

	Commitments Unpaid 12/31/72	Commitments Authorized 1973	Paid 1973	Unpaid 12/31/73
Advocates for Women	$	$ 7,500	$ 7,500	$
American Hospital of Istanbul		2,500	2,500	
Berkeley Runaway Center Youth Alternatives Program	8,500		8,500	
Center for Independent Living	5,590		5,590	
Childrens Hospital Medical Center of the East Bay		12,000	6,000	6,000
Chinatown Northbeach Youth Svc.		6,000	6,000	
Community Streetwork Center	5,000		5,000	
Contra Costa County - YWCA	5,000		5,000	
County of San Mateo Community Youth Responsibility		5,000	5,000	
Earl Paltenghi Youth Center		4,000	4,000	
Friends of San Francisco Deputies and Inmates	2,000		2,000	
County of Marin - Children of Divorce	21,205	1,890	15,696	7,399
Marin Open House	7,500	3,800	7,500	3,800
Mission Childcare Consortium		8,000	8,000	
Mount Zion Hospital - Harold Brunn Institute		15,000	7,500	7,500
Family & Child Crisis Project		22,000	22,000	
National Association of Social Workers		2,000	2,000	
Potrero Hill Youth Legal Center	4,250	10,000	9,250	5,000
Resource One	5,000		5,000	
San Francisco Citizens League		4,000	4,000	
San Francisco Lawyers Committee for Urban Affairs		2,500		2,500
University of California S. F.		12,000	6,000	6,000
Volunteer Bureau		4,000		4,000
Westside Community Mental Health Center				
Child Advocacy	7,500		7,500	
City College	5,000			5,000
Progress Foundation		12,400	12,400	
Youth for Service		5,000	5,000	
Total Health & Community Welfare	$ 76,545	$139,590	$168,936	$ 47,199

THE ZELLERBACH FAMILY FUND

Schedule of grants for the year ended December 31,1973

	Unpaid 12/31/72	Authorized 1973	Total	Paid 1973	Unpaid 12/31/73
Arts & Performing Arts	$ 35,840	$167,235	$203,075	$152,575	$ 50,500
Building Funds	170,000	9,500	179,500	72,000	107,500
Education	27,250	163,364	190,614	105,625	84,989
Federated Funds	45,000	125,000	170,000	92,500	77,500
Health and Community Welfare	76,545	139,590	216,135	168,936	47,199
Total Grants	$354,635	$604,689	$959,324	$591,636	$367,688

The Zellerbach Family Fund was established in December 1956 under the laws of the State of California. Between its inception and December 31, 1973, the Fund has distributed $5,228,594.00 in support of various programs. Principal funds unencumbered as of December 31, 1973 amount to $14,188,962.47.

INSTRUCTIONS FOR SUBMITTING APPLICATIONS

Grant applications are addressed to the Director of the Fund and should include the following information:

(1) A half-page summary of the purpose of the proposed project. A more detailed presentation may accompany the summary.

(2) An itemized budget with clear indication of the source of income and a listing of specific support from federations, foundations, community efforts, and public and governmental sources.

(3) A listing of those persons and foundations to whom the project request has been directed and a statement of anticipated sources of current and future income.

(4) A statement indicating community support and identifying the project's leadership. This statement should also present evidence of the competence and the preparation of the leadership to direct the proposed project.

(5) Evidence that the applying organization is a tax exempt *non-profit* organization, contributions to which are deductible.

(6) If the project has been in existence for six months or longer, include an evaluation of the project, its progress and its problems.

Grants made by The Zellerbach Family Fund are directed primarily to projects in the San Francisco Bay Area. Direct service projects in arts, education, and health and welfare that strive to improve the quality of life for all people in the urban community receive funding priority.

CONDITIONS GOVERNING GRANT ACCEPTANCE

If your project is approved for funding by the Board of Directors, you will be required to meet the following conditions:

(1) Provide a financial statement of your expenditure of the grant funds at conclusion of your project or for fiscal year in which the funds were expended.

(2) Submit a progress report for each six months of the project supported by The Zellerbach Family Fund or provide a final evaluation statement if the program supported is for less than six months duration.

(3) Submit a final program evaluation for those projects of more than six months duration.

NEW FAIRFIELD, CONN.,
May 14, 1974.

Mr. MICHAEL STERN,
Staff Director, Committee of Finance, Subcommittee on Foundations, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: My name is Martha A. Halas. I am a resident of New Fairfield, Connecticut. I wish to present the following information to your Committee.

Please show the Committee Members the first column in the attached editorial item from the New Milford Times of April 4, 1974. Notice that below the editorial is a news item from the NEWS TIMES of Danbury, Conn., of March 30, 1974—"Candlewood Developer, Suburban Action, receives grant."

To you, SAI may be a tax-exempt foundation. Around here, it is a developer, trying to make money for itself and its partner, Steve Weil.

I think that the tax laws should be changed to make it difficult if not impossible for foundations to make our life here in the countryside unbearable. I will talk about the SAI, the Ford Foundation, and the Regional Plan Association.

1. SAI is run by men who are trying to build WATERS EDGE, a 2500 unit development on Lake Candlewood. Please show your Committee Members the headlines of March 24, 1974, NEW YORK TIMES, "ACTIVISTS IN SUBURBS UNDER FIRE AS LANDLORDS.":

(a) Candlewood Lake is an intensely developed area right now, with mass public recreation, traffic problems, overuse, right now. It is a hydro-electric

project. The Sierra Club warned against any added heavy usage. It calls it a "fragile resource."

(*b*) At zoning hearings, their own experts testified they could not supply adequate water, that they had no sewer plans. New decisions of the State, leaving New Fairfield out of sewer plans, makes the development unable to have any plan whatever.

(*c*) In property that they bought, the NY Times article notes there is neither low-income, nor integrated housing, nor any intent to make it so—just plain gambling for profit in land speculation with money that comes from tax-exempt sources.

2. FORD FOUNDATION—In plain English, what does the grant to SAI mean? They say it is to help combat environmental objects against huge development. Look at this: The conservation commission of our neighboring town, Sherman, received $1,950 from the Ford Foundation to PROTECT AND CONSERVE THE LAND FROM WRONG USAGE—then Ford gives $50,000 to SAI to undermine and intensely develop the very same land—selected on the Conn. Land Use Map as an "area of scenic ridge, vacationland, and wetlands.".

The SAI grant is wrong! A public trust is misused. The terms under which these foundations are formed, and operate, is wrong. The public's own money is used to force the public to accept the private ideas of these people.

You should set up a board of license, that would have to hold public hearings, to re-license every foundation with assets of over one million dollars every five years, or to order it to liquidate. Money given foundations should be subject to gift tax and estate tax.

3. REGIONAL PLAN ASSOCIATION OF NEW YORK interferes with legislation. RPA aim is to deprive us of home rule in zoning and planning. In the name of open space it wants to fill in all the space of the enormous triangle of the Mid-Hudson Region. (Ford gave it $150,000 for this purpose.)

Please note letter enclosed from Regional Plan Assn. They are not supposed to be affecting legislation. But why then did it meet with legislators if that was not clearly its motive.

I ask that they be deprived of their 501(c)3 status. Please note that this New York organization, with Ford money, is trying to branch out and interfere and dictate in many states.

Please note also enclosure of a letter I sent to the Danbury News Times, which they printed

Yours truly,

MARTHA H. CARSELLO HALAS.

ACTIVISTS IN SUBURBS UNDER FIRE AS LANDLORDS

(By Ernest Dickinson)

TARRYTOWN, N.Y.—Neil Gold hopes to reshape America's traditional housing patterns. His dream is to provide an alternative to all-white suburban enclaves of single-family homes.

On the drawing boards he already has plans for more than 15,000 units of housing in five mixed-income, racially integrated communities in New York State, New Jersey and Connecticut. They would cost an estimated half a billion dollars to build.

The vehicle established to fulfill this vision—Garden Cities Development Corporation—has submited plans for 3,675 townhouses and apartments at Waccabue Hills, a project that would triple the population of the town of Lewisboro, N.Y., in 10 years. Also on paper are 6,000 housing units at Ramapo Mountain in Mahwah, N.J.; 2,570 at Candlewood Lake in New Fairfield, Conn.; 2,200 at Readington Village in Hunterdon County, N.J., 850 at Fairfax County, Va.

These projects have stirred considerable local controversy, and some are in litigation. But while the debates swirl over Garden Cities' brochures, presentations and claims for the future, the corporation in the last year has been quietly picking up existing garden-apartment complexes. And as an owner it has drawn considerable fire from local officials.

At the development known as Chateau Le Mans on the outskirts of Indianapolis, Mayor Morris Settles of the town of Lawrence said that he had to threaten to shut off water to all 524 units to collect a long-overdue water bill of almost $10,000.

At Lancer Courts in Depew, near Buffalo, the Erie County Water Authority is petitioning in Federal Court to have portions of the rents assigned to cover a back water bill of about $3,000. At Katrine Apartments, just outside Kingston, N.Y., Central Hudson Gas and Electric Corporation has threatened to shut off utilities to collect a bill of about $20,000. There, also, the Ulster County Health commissioner, Dr. B. J. Dutton, said that his office had received an inordinate number of tenant complaints since Garden Cities took over.

He has been trying since July, he said, to get the company to put in pumps and remedy other violations in its sewage treatment plant. The company has a poor record of maintenance, he said, with many promises but no major improvement.

In Hilton, N.Y., a residential Lake Ontario community west of Rochester, Robert Elliott, the village administrator, said that he had been getting numerous complaints from tenants since Garden Cities bought the 111-unit Hilton Heights apartments.

"They are leaving the place like flies," he said. "Things go wrong. You can't get them fixed. Even simple little things."

Garden Cities' problems in Hilton involve management, street dedication and complaints for nonpayment of bills, Mr. Elliott said. "There hasn't been a water or utility bill paid in almost a year, since they have owned it," he said. He said that a lien would be placed on the property "if things aren't straightened out."

Garden Cities Development Corporation occupies a suite in an office building at 150 White Plains Road here in Tarrytown. That suite is also the headquarters for subsidiaries that Mr. Gold has established—Garden Park Realty Company and Garden Park Management Company. He also foresees setting up an engineering company.

Mr. Gold, a man of medium stature who is in his mid-30's, declined in an initial interview to discuss for the record any of Garden Cities' properties, or even to identify them. Later he relented when it developed that there was criticism of the company's management.

He made two principal points. "Garden Cities is a not-for-profit membership company in which nobody has put a dime of capital," he said. "We have no investors. We have no stock. We are all here on rather modest salaries. Therefore, what Garden Cities has to work with is the money that it gets in.

"There are times—sometimes for months—when we are very cash poor. This is so for normal companies operating for profit, but for us it is particularly so. The result is that in those periods we defer payment of bills. But, all the time, our first concern is to upgrade the properties. That is what we have been doing."

Moreover, Mr. Gold said, "it is not as though we bought projects that were viable and they went to hell. We bought projects that were going to hell and we are making them viable." Garden Cities' theory, he said, is to acquire properties with problems and gradually upgrade them.

A native New Yorker who graduated from Columbia University in 1959 and took a master's degree in history, Mr. Gold was relaxed, and articulate as he discussed the social theories that led to his present activities.

Early in his career, he said, he reached the conclusion that racial problems in the United States could not be solved before an attack was mounted on the basic problems—the separation of families residentially by race and income.

In 1966, while he was program director of the National Committee Against Discrimination in Housing, he met Paul Davidoff, a Yale Law School graduate who has taught planning and urban affairs at the University of Pennsylvania and Hunter College. "We realized that we had a lot in common and have been close ever since," he said.

Two years later the two created the Suburban Action Institute as a New York State charitable trust to fight exclusionary land use controls. It received foundation grants and is tax exempt.

Garden Cities was organized in 1971 under New Jersey law as a not-for-profit corporation, and while Mr. Davidoff was its board chairman until last September and Suburban Action's offices are on the same floor of the same building as Garden Cities', the two organizations are now totally separate, according to both Mr. Davidoff and Mr. Gold.

The most critical part of the housing crisis, in Mr. Gold's view, is not its shelter aspect. It is the emplacement of homes—where they are located—that determines one's basic outlook on the world, he said.

It is necessary, he maintained, to provide an alternative environment—one less isolating, less antisocial than the present "monuments to American affluence"—the one-class, single-family suburb.

Hence the large, mixed-income planned communities that Garden Cities proposes. Typically they consist of townhouses and garden apartments, with schools, shopping centers, sewage plants, libraries, recreational facilities and a network of pedestrian walkways.

In order to bring in lower income families, Mr. Gold said, Garden Cities has been devising a system of private subsidies for the poor—subsidies completely independent of Federal and state grants. In effect, the corporation would be setting up its own welfare program.

Discussing the specific complaints raised about the quality of Garden Cities' present management, Mr. Gold and the corporation's special counsel, Allen Zerkin, made several observations.

Lake Katrine and Hilton, Mr. Gold said, were "suffering when we bought them." The former he described as a "first-rate rescue job," adding that it would be "one of the most beautiful garden apartments in the region when we finish improving it."

It will take time, he said. Contracts have been let but work cannot start until the ground softens.

About the sewer plant violations at Lake Katrine, Mr. Zerkin contended that the problems were the result of sabotage done in a "very sophisticated way," allegedly by a former employe. "But the sewer plant is running fine now," he said. Taking issue with that statement, the health agency reiterated its charge of improper maintenance.

At Hilton Heights, according to Mr. Gold, Garden Cities must have invested "almost $100,000," including $40,000 worth of trees, a $20,000 pool and $10,000 worth of play equipment. Mr. Elliott, the Hilton administrator, conceded that improvements had been made.

A visitor to Hilton Heights last week observed that many new trees had been planted. But he was informed by one tenant, Mrs. Beverly Wing, that "quite a few people are breaking their lease and moving out."

"One of our windows blew out the other day and we couldn't get the kid who's in charge to replace it," she said. "Finally my husband took a window from the model apartment."

Another tenant, Mrs. Pamela de Baker, said: "These places are falling apart. They're not being kept up. We've lived all over the United States and I've never dealt with a place like this. My husband's company pays our rent and they've held back payment for two months until some things get taken care of."

She complained of water in the basement, leaking windows and a large crack in the bathtub.

A third tenant, however, was milder in her comments. "It's a place to live," said Mrs. Louis Scuderi. "I'm not wild about it but I don't have that much against it either."

According to Mr. Gold, Garden Cities bought Hilton Heights at a low price after being informed that all bills had been paid. "Apparently we were informed incorrectly because a few months ago we were told that the water bill was still outstanding," he said.

Agreeing with Mr. Gold, Mr. Zerkin insisted that Garden Cities had not been bad managers. But there have been times when the inability to pay a bill has made it hard to get work done.

"Everything traces back to the financing," he said, "the fact that we have been 'boot-strapping'—building something from nothing, literally nothing."

In the Lake Katrine purchase, for example, Garden Cities bought 152 units plus adjacent property on which permits for additional construction had already been granted. A wealthy, unidentified partner took a 50 per cent interest in this second, or construction, phase of the deal, Mr. Zerkin said. The partner's signature was sufficient to obtain an institutional loan of approximately $200,000 to help finance the purchase. In addition, the seller provided a $65,000 loan, or purchase money mortgage. The loans covered more than 100 per cent of the purchase price, so that Garden Cities did not have to invest any of its own cash.

Mr. Zerkin said that by personally guaranteeing institutional loans and also by supplying some cash, two wealthy individuals had greatly assisted Garden Cities in its purchases.

Garden Cities is moving toward construction both at Lake Katrine and at Hilton, Mr. Zerkin said. There are also plans to build 135 condominium units in the so-called Rose Garden on the south side of the village of Newark, N.Y., 30 miles east of Rochester.

Although Garden Cities put in none of its own cash at first, Mr. Zerkin said, its object is to "turn the property around" fairly rapidly and syndicate it, and then lease it back from the syndicate. So far this has occurred on one investment, he said—a 132-unit project known as Sherwood Manor on Dodge Street in Rochester.

In that instance, Garden Cities came away with a $200,000 profit after a sale to a syndicate, which consists of Garden Cities as general partner and about a dozen limited partners. Limited partners in such a syndicate are normally high-income investors seeking the benefit of tax shelter.

The profit from that sale has been used in part to support the staff of about 15 or 16 persons in Tarrytown. In addition, the unnamed benefactors have on occasion supplied cash.

"But it's been rough," Mr. Zerkin acknowledged, as he said it would be in any such operation with a social purpose. The procedure of upgrading and then syndicating is more difficult than had been anticipated, he said.

"We had to go into the hole at various times," he said. "We've fallen behind, and we've been bailed out."

Most if not all of the properties have a smattering of black tenants, though the Garden Cities officials indicated that no affirmative action program had been adopted to change the racial or economic composition of the developments.

Mr. Gold indicated that he was eager to move forward with the construction projects. "We have our staff of accountants and controllers that run our projects," he said. "We are geared up. We are ready to move."

If construction has not yet started, it is not because Garden Cities lacks the means to do it but because it has been blocked by municipal zoning and planning bodies, he said.

"We are not litigating for its own sake," he said, "but where we feel the basic reason for denying Garden Cities the right to build is racial or economic, we intend to litigate and are so doing."

The $200-million Ramapo Mountain project is in the courts. So, too, is the 2,570-unit WatersEdge project proposed for Candlewood Lake. Waccabuc Hills is before the Lewisboro Planning Board. Mr. Gold anticipates that a suit will be filed soon in the application for Readington Village in Hunterdown County, N.J.

This leaves only one of the five big planned communities with no procedural hurdles to clear—the 950-unit project in Fairfax County, Va. But there a sewer moratorium blocks construction and may do so for as long as a year.

Asked where the money would come from to finance the half-billion dollars worth of new construction, Mr. Gold said: "What money? It doesn't cost any money to do this that won't be provided by mortgage loans. You don't have to have resources to build houses. You have to have access to people who have resources. Good plans, sound economic analysis and good people willing to wait for their fees until development starts."

Opinions of the People

The News-Times welcomes letters to the editor from readers. Please sign them and give your address. Letters exceeding 300 words will be returned to the writer for condensation.

HITS GRANT FOR SUBURBAN ACTION

To The Editor:

I am distressed to learn of the $50,000 grant from the Ford Foundation to Suburban Action Institute to do development planning for housing in the rural and suburban area. At the moment when their Waters Edge partner, Steve Weil, has told a reporter that he is kicking them out, at the moment when they stand exposed by the New York Times as suburban slum lords, the Ford Foundation rescues them from ignominy with a $50,000 grant. Think of it. SAI is trying to break down zoning in Connecticut, New York and New Jersey, and ultimately in the entire United States, in order to build "racially—and economically—integrated housing," they say. But apparently there are no poor and no, or few blacks in the four garden-apartment developments which they have bought (N.Y. Times, Mar. 24).

We know, if the Ford Foundation does not, that there is no physical shortage of housing in this country, for we have built 1.5 housing units per new household for the past two decades. We know, if the Ford Foundation does not, that there is a shortage of fuel, and that additional housing in the countryside is wasteful and is contrary to public policy. We know, if the Ford Foundation does not, that

there are very few farms left, and at the present rate at which agricultural land is being paved over and turned into PUDs and new towns, we shall soon be eating hydroponic food (food grown in chemicals). Grants should be not for "social change" but for "social improvement." We agree with Fred Benedikt's remark, that Ford is "the most irresponsible of all foundations."

We urge the Ford Foundation to rescind this grant. We urged it, instead, to make grants to communities in order to keep the few remaining farms as farms, following the policy now started by John Klein, county supervisor of Suffolk County, L.I.

In New Fairfield we have only a couple of farms left; in Sherman, they have only six; in the whole western part of this state, we have only one egg farmer left, and only a couple of dairy farms still remain. Klein's policy is to buy up the farms and lease them back to the farmers, to keep the land out of the hands of the developers, and to keep up food production on Long Island.

MARTHA H. CORSELLO.

[From the New Milford Times, Apr. 4, 1974]

CANDLEWOOD DEVELOPER—SUBURBAN ACTION RECEIVES GRANT

NEW FAIRFIELD.—Suburban Action Institute (SAI), waging a court battle to reverse a local zoning board denial to build a low and moderate income community on the shores of Lake Candlewood, has received a $50,000 Ford Foundation grant, a foundation spokesman said Friday.

The grant will go "to help SAI in its research and planning for low and moderate income housing versus the claims of the environment."

SAI of White Plains, N.Y., was denied permission to build the 2,500 unit community last fall partly because of environmental restrictions.

Frederick Benedikt, secretary of the Lake Candlewood Defense Associates, a citizen group which opposed the project, termed the Ford Foundation "the most irresponsible of all foundations" for making the grant.

PEOPLE IN GLASS HOUSES

News of the Ford Foundation's $50,000 grant to Suburban Action Institute was received in these parts with less than enthusiasm, a reaction that extends to this office.

SAI and its affiliate Garden Cities Development Corp. have not exactly won friends hereabouts with their preposterously inept proposal (setting the background for anti-zoning litigation) to build a 2,500 PUD at Lake Candlewood on a site without redeeming social importance, or even rudimentary facilities such as drinking water, drainage, or the means to provide livelihoods for the low-income group envisioned as living there.

In addition to the "insult" to the environment offered by the WatersEdge project was the overtly stated insult to those who opposed the proposal, labeling them as racists and exclusionists: a probably unique experience for such life-long liberals as Malcolm Cowley and Matthew Josephson, and the thoroughly decent group of people who live in Sherman and New Fairfield.

We did a little homework on the exact nature of the Ford grant, and while we could find nobody at home in the glasshouse on East 43rd Street, * * *

REGIONAL PLAN ASSOCIATION,
New York, N.Y., Dec. 18, 1973.

MRS. MARTHA HALAS,
Bogus Hill,
New Fairfield, Conn.

DEAR MRS. HALAS: David Doniger passed on your correspondence with him. I thought you might like to know which of the Senators' aides we have met with about CHOICES: Ted Leary in Senator Ribicoff's office, and Bob Herrima in Senator Weicker's office. They have been supportive of the project since its inception—helping RPA get a federal grant to pay for part of CHOICES.

I have also enclosed a summary of our activities in Connecticut to follow up on CHOICES, plus a form which you may use to suggest people who might serve on a Connecticut Committee we are helping to create.

Thank you for the interest you've shown.

Regards,

MICHAEL J. MCMANUS.

(Regional Plan Association is a 501(c)(3) organization, and is thus barred from propagandizing to affect legislation. Yet they met with all 6 Senators and 40 Representatives of N.Y., N.J., and Conn., in Washington, according to the statement of the then-Connecticut Coordinator, Dave Doniger, at a meeting on Sept. 5, 1973, in Danbury.)

BIOLOGICAL HUMANICS FOUNDATION,
Dallas, Tex.

Hon. VANCE HARTKE,
Chairman, Senate Finance Committee's Subcommittee on Foundations, % Mr. Michael Stern, Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR SENATOR HARTKE: The Trustees of the Biological Humanics Foundation, a private foundation in Dallas, Texas, wish to submit their views on Code Sections 4940 and 4942 in response to your invitation to file these for the record and study of the Subcommittee on Foundations.

We believe the 4% tax imposed by Secton 4940 is extremely punitive and unnecessary. It has more than doubled this Foundation's costs (for legal, accounting and administrative fees). Presumably the experience of other such foundations duplicates our own. These increased expenses obviously reduce the dollars available for the charitable purposes of the Foundation. Despite the substantial increase in the number of IRS auditors and the breadth of its investigations of such foundations, it is our understanding that the tax collected is six times greater than IRS costs of such audits. There is certainly some argument for abolishing this tax altogether since such foundations are the only entities in the nation which are charged for IRS audit services. If it is not completely abolished, we strongly urge that the tax at least be reduced to ½ of 1% of net investment income and that capital gains be excluded from investment income so funds set aside and required for charitable purposes will not be diverted to noncharitable government use.

The prevention of indefinite deferment of distributions to charities, the thrust of Section 4942, is commendable indeed. However the annual payout requirement of 6% of market value of investment assets is stringent and places too severe a burden on Foundation trustees to secure a sufficiently high rate of return to avoid:

1. Converting all its investment assets into bonds or other fixed income securities (thus dealing a severe blow to the nation's economy as well as to the ability of the foundation to protect itself against inflation).

2. The other alternative of slowly liquidating and terminating the existence of the foundation represents an even more severe blow to the churches, hospitals, and educational, medical and research institutions which depend so heavily on continued support from such foundations. We urge a reduction in the minimum percentage required to be distributed from 6% to 3%. This would permit private foundations to invest at least a part of their assets in equity securities and preserve their existence.

Many of the most vital services which meet public need were developed and inspired as well as made possible through the financial assistance of foundations which became classified as private under the Tax Reform Act of 1969. To continue to and further diminish their roles in our pluralistic society is, we believe, a disservice to the public. The size of foundations' assets and annual giving ability is negligible when compared to Federal Government expenditures in health, education and welfare. Failure to preserve the foundations, in our opinion, will have an unalterably negative impact on our nation's charitable institutions.

We shall appreciate your consideration.

Sincerely,

P. O'B. MONTGOMERY, M.D.,
President.

ELSA U. PARDEE FOUNDATION,
Midland, Mich.

Hon. VANCE HARTKE,
Chairman, The Senate Finance Subcommittee on Foundations, Care of Michael Stern, Staff Director, Senate Finance Committee, Dirksen Senate Office Building, Washington, D.C.

DEAR SENATOR HARTKE: The Trustees of the Elsa U. Pardee Foundation appreciate your invitation to comment on Sections 4940 and 4942 of the Internal Revenue Code.

The 4% excise tax has proven to be excessive and should be adjusted to reflect the actual requirements for auditing foundations. Perhaps the rate should fluctuate with the financial requirements for the purpose of Section 4940. Some have suggested a 2% excise tax as adequate and if a flat rate is more desirable than a fluctuating rate, we recommend a 2% excise tax.

The minimum distribution of net investment income requirements for private foundations should be changed to lower the rate to reflect the actual yearly income of nearly all foundations.

The present rate requires foundations to sell their assets every year in order to meet the pay out requirement. The other choice is to invest the assets in higher paying bonds or Treasury bills which at the present rate of inflation lowers the true value of the assets year after year.

Either choice means over a period of time—foundations are eliminated or severely impaired in their charitable activities.

We do not believe this was the intent of the Tax Reform Act of 1969 as passed by Congress. At least all Congressmen and Senators we have communicated with did not intend the destruction of foundations.

The Tax Reform Act of 1969 and other legislation pertaining to foundations are well constructed and help correct many actual and potential abuses of administering funds for charitable purposes.

After almost four years of experience under the Tax Reform Act of 1969 it is necessary to change the requirements that are excessive and harmful to the long term health of private charity.

Sincerely,

WILLIAM W. ALLEN,
Vice President and Secretary.

SHERMAN, CONN., *May 10, 1974.*

Re Investigation of problems concerning the relation between tax laws and foundations.

Mr. MICHAEL STERN,
Staff Director, Committee on Finance, Subcommittee on Foundations, U.S. Senate, Dirksen Senate Office Building, Washington, D.C.

DEAR MR. STERN: I understand that this Committee is holding an investigation of private foundations in connection with tax laws, on May 13–14. Kindly include the following statement in the public record.[1]

I live in a little town, population around 1500, 65 miles from the nearest sizable employment center, which is New York City. I come to this question from an unfortunate experience on Candlewood Lake, situated in our town and in the Town of New Fairfield (and bordering three other Connecticut towns as well).

Several of us in these towns have given all or most of the past year to defending ourselves against a "Foundation" which is trying to build apartments on our Lake. This Foundation, or, more correctly, its directors, doing business under another name, is now suing New Fairfield—having failed, as it knew it would, to convince the zoning authorities to down-zone a single-family, one-acre area in order to allow it to construct apartments on the Lake. The apartments would cause high-density development which would double the population of that Town and ours combined, which occupy fifty square miles, though the development would cover something less than 200 acres. The Foundation's directors have brought similar proceedings against the zoning authorities of our town, and we have every reason to believe that we shall be sued next, because the zoning authorities of our town are also prevented by the ordinance of the Town from granting developer's petition.

I. *Should foundations interested in housing and zoning be allowed to form "development affiliates" even though they are not tax-exempt? Should foundations in any field—to widen the question—be allowed to form subsidiaries in the same field?*

Suggested change in tax laws: Where a 501(c)(3) organization has a wholly or partially-owned or controlled company in the same field, it shall be presumed that the 501(c)(3) organization exists to serve the non-tax-exempt company.

[1] Note: Suggestions are summarized at p. 31; appendixes are listed at 32–33.

The 501(c)(3) organization in question is Suburban Action Institute (SAI), organized in 1969 as a charitable trust. SAI's purpose was indicated in an article in the *New York Times*: to challenge the constitutionality of zoning.

> Mr. Gold and Mr. Davidoff [the founders and directors] are now choosing two or three towns as targets for their suits. The intention is to get a builder to file plans that would be *rejected* and then go directly to the state and Federal courts. (Emphasis added; David K. Shipler, "Law Suit to Challenge Suburban Zoning as Discriminatory Against the Poor," 6/29/69.

As it was possible to know Hitler's views and plans by reading his book, so it is possible to know this Foundation's views and plans by reading the articles of the founder-directors. In the January, 1970, issue of the *Journal* of the American Institute of Planners, Messrs. Davidoff and Gold describe exactly how they intend to set about the task of reversing the Supreme Court's decision that zoning is constitutional, and of getting state zoning—enabling statutes declared unconstitutional:

> The test case we seek to initiate will be based on a set of assumptions about where an attack on zoning can be most successfully made and on a set of arguments regarding the deleterious consequences of certain forms of zoning. The case will be brought in a jurisdiction that excludes all forms of multifamily housing. It will be brought by a nonprofit developer who has gone to the expense of preparing building plans for substantial numbers of multifamily housing units and who has attempted to have plans approved by the municipal planning agency and by the municipal building department. To file such plans the developer must own, or have an option on land suitable for development within the municipality. Since the municipality prohibits all multifamily housing, the developer's plans *must* be rejected. It is this rejection which will set the stage for judicial examination of the constitutionality of zoning ordinances prohibiting all multifamily units. [p. 19]

Before going further, we should perhaps make clear that the "nonprofit developer" who is to play a role in the "Zoning Test Case" is "nonprofit" in name only. Clearly, investors would not flock to this banner if it were true. Nor would they flock to the banner of "limited-dividend" corporations operating under Section 236 of the Housing Act, were yields from their investments truly limited. The real income to investors from such investments may be approximately measured by the fact that, according to the computations provided by former HUD Secretary Romney, $17,000 apartment costs the American taxpayers $141,854 over forty years.[2]

SAI's own "nonprofit developer," which is discussed in the next section, is not a charitable institution, as indicated by the second paragraph of a letter from the Division of Public Welfare of the Department of Institutions and Agencies of New Jersey, written on May 8, 1973, to SAI's Neil N. Gold, and forming a part of the incorporation papers mentioned above (Appendix B):

> In our opinion, this is not the type of corporation that is contemplated by R.S. 15:1-15 as requiring the affirmative approval of the Commissioner of Institutions and Agencies. Although described and structured as a nonprofit corporation, it does not appear to be essentially charitable or eleemosynary within the purpose and meaning of the cited statute.

There are some who think the implication that SAI's "nonprofit" developer," acting in its private interest, is only the handmaiden of SAI, acting in the "public interest," to be "deliberate deception." There are some who think that those are deceived who suppose that this "nonprofit developer" will be acting in the public interest. Lee V. Blum of South Salem, New York, writes to the editor of the *Patent Trader* (May 17, 1973, p. 11):

> At the Suburban Action Institute conference held on January 17 of this year, Mr. Gold stated that only 50 percent of the stock shares are under the control of this corporation. The other 50 percent are private investors . . . [;] he hoped they would realize a handsome profit.

Deliberate Deception?

In an interview in the *Fairfield County Magazine* of September, 1971, Mr. Davidoff distinguished between a wholesale attack on all zoning laws, such as his 501(c)(3) organization, SAI, was effecting, and a "bonanza accruing to

[2] Letter to the editor, *New York Times*, Nov. 28, 1972, taken from *Fortune* of February 1972.

land developers . . . of a single parcel. But I might add," he said, "we are not in business to create that kind of bonanza [pp. 37–38]."

But they were. Even as Mr. Davidoff was distinguishing himself from ordinary developers seeking bonanzas, he and his partner were engaged in setting up a Siamese-twin organization which would serve as that bonanza-seeking developer. At the very moment when he was disclaiming private interest and proclaiming public interest, the incorporation papers of these two gentlemen doing business as "Garden Cities Development Corporation", were being accepted by the State of New Jersey—on September 7, 1971. (The papers of incorporation are attached and marked "B.") Five towns were "targeted" soon after: Mahwah and Readington, N.J., in April, 1972; Lewisboro, N.Y., in November, 1972; and Sherman and New Fairfield on April 11, 1973. In all cases except one, where Davidoff and Gold joined with the developer who owned the land, their GCDC was named as developer. And in all cases, it was SAI that put out the news releases for GCDC.

On the very day when the Foundation-developers' proposal to build a Pud ("Planned unit development") on Candlewood Lake was announced in New Fairfield, my article, "Catchbasins for a disintegrating New York," about "social consciousness' in developers, was published. Three of the five developers or developer-types mentioned in that article, are discussed in this paper: New York State's Urban Development Corporation; Regional Plan Association; SAI. (The article is appended and marked "C.") SAI's activities on Candlewood Lake need not further detain us. They have been publicized on TV, in the *New York Times* Sunday real estate section, and in the local, bi-weekly, mimeographed *Sherman Sentinel.* In all three, the Town's view is given by author Malcolm Cowley, a resident of the Town of Sherman, and former Chairman of the Planning and Zoning Commission. Mr. Cowley's doubt about the sincerity of the professed aims of Developers Davidoff and Gold, to build "racially- and economically-integrated" housing for the poor and the blacks, will be taken very seriously by all who are familiar with his long record of concern for the poor. Wrote Mr. Cowley on August 1, 1973, protesting a $38,000 grant to the developers:

> Messrs. Davidoff and Gold profess to be acting for the public good. But one notes in every development with which their Institute has been associated that there is also present a land speculator bent on making the largest possible profit. . . .
>
> WatersEdge [the name of the proposed development] is our local example of the sort of activity now to be encouraged by a grant of $38,000 from the National Endowment for, my God! *the Arts.* . . . Oh, yes, the grant to them is "for study," but with their background and announced purposes, everybody knows what the results of the study will be. In this great country eager for the arts, aren't there projects and artists that the Endowment can sponsor without diverting $38,000 to confrontation politics and an undertaking that is essentially short-sighted and destructive?" [The column is appended and marked "D."]

Protesting this same grant, the Sherman Civic Association fired a shot heard round the Tri-State area [see Appendix E]:

> What is happening is that our Federal Government is taxing us for funds being used to attack us. We townspeople who are being besieged must now dig into our pockets to raise more money to defend ourselves.
>
> We believe this situation to be illiberal, unfair, and unjust. We believe that the grants by the foundations and by the National Endowment for the Arts [to Davidoff and Gold] significantly thwart the intentions of the United States Congress. We believe that this misuse of funds should be made the subject of an investigation by the Congress. [See Appendix F.]

Ironically, this grant was announced by National Endowment for the Arts as related, in some vague way, to the bicentennial celebration.[8]

The fact that Mr. Davidoff and Mr. Gold organized their "development affiliate," as they themselves call it, under the "not-for-profit" title of the New Jersey Statutes, immediately that Title was amended to allow them to do so, raises the question of whether this long-rang plan did not call for the Foundation, SAI,

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[8] This grant was investigated by the General Accounting Office. Its 17-paged report dated September 5, 1974, has just arrived, entitled, "Propriety of the City Edge Grant Awarded to Suburban Action Institute [by] National Endowment for the Arts," B–158811. The Report quibbles over the manner in which SAI has reported its expenses to NEArts, but contains not a hint of wrongdoing by NEArts. Questions provoked by some extraordinary evidence of wrongdoing by NEArts available to GAO, have not been raised, far less settled. The Report is a whitewash of NEArts.

in effect to be the subsidiary affiliate, and the GCDC the chief vehicle of their housing and zoning activity. The SAI came first, fortuitous or not; it was essential to establishing good-will among the do-gooders who honestly believed that it was the "vice of exclusionary zonging" that kept out "the poor and the black; essential to getting the attention of the foundations, the civil rights and community leaders, and influential people at all levels of Government and in the media. It is notable that all important zoning case reported in the *New York Times* from 1969 on, contained quotations from Mr. Gold and Mr. Davidoff, even where those gentlemen were apparently quite unconnected with the case being reported. Questions of public relations and of finance were handled with remarkable efficiency by SAI. Dun & Bradstreet reported that SAI had amassed an income in 1973 of $350,000.

So good a public relations job have they done that it has been impossible for us to get our case before the public, though (as we think) their economic case is poor, and ours, good. The B'nai B'rith, the Hartford Archdiocese, the League of Women Voters—SAI's allies in a new "Connecticut Coalition for Open Suburbs"—have been appealed to:

> . . . you have taken a strong position on a controversial issue without (we believe) having first considered both sides of the question. The result is that you are committing the same type error which the Anti-Defamation League was created to oppose—blind prejudice.
>
> Breaking down zoning does not and cannot result in low-cost housing. Zoning is not discriminatory, in the sense of discriminating against people of particular races or income groups. It is not "exclusionary." Breaking down zoning will not result in benefits to the poor or to minority groups. It will not result in integration. All these assertions, we are in a position to substantiate.
>
> The organizations devoted to breaking down zoning are, in our view, engaged in a gigantic fraud, by which they enlist the conscience of well-meaning people in a campaign to yield to themselves great profits through the rise of land-values. [See Appendix H, I.]

Nor were letters to each of the directors of the Stern Foundation, the Field Foundation, the Martin Peretz Foundation, all SAI benefactors, any more successful: Would they give notice and opportunity to us to argue against future grants to SAI? Would they give grants to organizations with an opposite political ideology from SAI's? None said he would. Indeed, almost without exception, none troubled to respond.—would the Ford Foundation be interested to see the admissions we have found, from "their side," that down-zoning does not lower the cost of housing, and may raise it? The Ford Foundation was not interested.

Whether or not GCDC was intended from the very beginning to be the prime vehicle, is unimportant. The important point is that Mr. Davidoff and Mr. Gold are not unique. There are others, who started out as civil-rights activists, graduated to becoming "property-rights activists," and, attracted by the great gains, then went into businness for themselves, as developers. The following is an example of this marriage of convenience:

> The National Housing Partnership, a private corporation established by Congress to attract new money into subsidized housing, has a social mission and thus is promoting some inner city projects. But an examination of its projects shows that only a small percentage is in troubled inner city neighborhoods. [John Herbers, "Subsidized Housing Rise in Suburbs Alarms Cities," *New York Times*, January 24, 1972.[4]]

The essential question is, should they continue to exist?

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[4] The National Housing Partnership was a recommendation of the Kaiser Commission: The Report of the President's Committee on Urban Housing, *A Decent Home* [1969]. Gold and Davidoff were "contractors." Amongst the Committee Members were two men whose names also appear as Directors of National Housing Partnership—Leon N. Weiner, a past President of the National Association for Home Builders who "has given strong impetus to the acceptance of cluster zoning [p. 277]," and John H. Wheeler, prominent in civil rights and in the construction of low-income housing. Also on the Board of Directors is I. H. Hammerman, II. Mr. Hammerman is one of the alleged bribe-collectors for former Vice President Agnew whose testimony helped remove Mr. Agnew from that office. Mr. Hammerman is designated as "Presidential appointee confirmed by the Senate." (See p. 15, 1972 report, *National Corporation for Housing Partnerships* and *The National Housing Partnership.*)

This organization benefits its Partners who "are allowed the benefits to be derived from offsetting their distributive shares of the Partnership's tax losses against taxable income derived from other sources [p. 14]." Tax losses are the principal form of real income to the partners. They have increased from 7.6% in 1970, to 24.9% in 1971, to 51.8% in 1972, of cash invested. Such tax shelters do not help the system of private free enterprise in these days when it is under attack by the vindictive egalitarians.

II. *Foundations should not be permitted to make grants to 501(c)(3) organizations which are affiliated with non-501(c)(3) organizations in the same field.*

". . . [T]he only contribution which the Rockefeller Brothers Fund has made to Suburban Action Institute . . . [was] $85,000 last August. This grant has been used in connection with . . . migrant worker housing in Delray Beach, Florida. . . . The Fund has made no contribution to Garden Cities Development Corporation, nor has one been requested," wrote the Rockefeller Brothers Fund to Dr. and Mrs. Alfred Vagts of Sherman, Connecticut. (See "K.") The same statement has been made by all foundations which have both made grants to SAI and responded to our inquiries. John G. Simon, President of Taconic Foundation, Inc., a long-time donor to SAI, writes:

> 'GCDC maintains fiscal independence from SAI, and we have been assured that no part of any grants we have made to SAI have been used to defray any of the expenses incurred by GCDC in connection with the project in Sherman, Connecticut.

How are the salaries of Directors Davidoff and Gold apportioned between SAI and GCDC? How is the cost of the office equipment apportioned between them? Does GCDC pay rent to SAI for the use of the "clubhouse" in East Orange, N.J., which was given to SAI by Wallace-Eljabar Fund, Inc., as a $25,000 grant for a law office? If so, how much? How does Mr. Simon know that he can rely on the "assurance" of SAI? Does he really care?

The Ford Foundation's Robert W. Chandler, who is in charge of a very recent grant of $50,000 to SAI, relied upon the same fiction of legal separation, when I telephoned him on March 28 to ask how the Ford Foundation could have given this grant to men who had just been exposed in the press as "suburbanslumlandlords." Mr. Chandler twice took me to task for insufficiently distinguishing between SAI and GCDC. Ford had given to the former. It was the latter which had been exposed in the press, said Mr. Chandler. Were GCDC's officers not the same as SAI's officers? Was not GCDC presumably implementing the social and political theories of SAI? If poor maintenance, nonpayment of utility bills of tenants, nonpayment of other bills, and the passing of bad checks [5] were implementing SAI's theories, what was one to think of SAI's theories? Mr. Chandler was unimpressed with my arguments. Had Mr. Chandler not seen the exposé in the *New York Times*, published five days earlier? He had not. It was unnecessary, he said, as he had seen it all before. (GCDC had acquired four garden-apartment complexes. To the best of our knowledge, the *New York Times* exposé of March 24 was the first. There was a second on the following day, by the *Times Herald Record*. If Mr. Chandler had in fact seen an exposé unknown to us and had still given the grant to SAI, Ford was all the more culpable, in our view. See my column in the *Sherman Sentinel*, "L," attached.)

The Foundation and other donors to SAI—National Endowment for the Arts is one such—choose to hide behind the fiction of the legal separation of SAI and GCDC. The Ford Foundation writes me on April 29, " . . . [T]he Foundation declined, over a period of years, to make any grants to the Suburban Action Institute until there occurred a legal separation from Garden Cities." See p. 22. In fact there were only two years separating the existence of 501(c)(3) SAI from GCDC, and they have been "separate" since September, 1971. Paul Davidoff told a New Jersey newspaper in early December, 1973, that he did not know what the National Endowment for the Arts meant by saying that the two organizations were to be severed. They are legally separate, he maintained.

Until the IRS regulations specifically bar foundations from giving grants to 501(c)(3) organizations which have affiliates in the same field, it seems quite likely that foundations will continue to behave in this manner, thus circumventing the intent of the Congress.

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[5] One bum check passed to the utility company in the sum of $3,500 is reported in the *Times Herald Record* account. From two people I have heard that in the Indianapolis garden-apartment complex owned by Davidoff and Gold, more than 10 such checks were passed. This development is known as "Chateau Le Mans," and is apparently in the Town of Lawrence, on the outskirts of Indianapolis. See the *Times Herald Record* account and the *New York Times* account of GCDC's management at "M" and "N."

In the event that your Honorable Committee is unwilling or unable to recommend the suggestions made above, would you be willing to recommend defining "separation" in a manner which will preclude the situation described? The National Endowment for the Arts, which has given a $38,000 grant to these foundation-developers, accepts a "verbal assurance" from Mr. Davidoff that no tie exists between the two organizations, and requires of critics of that grant "solid evidence" of the contray. When given solid evidence, the NEArts further narrows its requirement to "operational" separation. In a letter defending this grant, written to many people in Connecticut, New York, and New Jersey, on December 6, 1973, the NEArts said:

> At the time the application was submitted [by SAI, which was in December 1972, we later discovered], a close relationship existed between the Suburban Action Institute and its "development affiliate," the Garden Cities Development Corporation . . . [but GCDC] severed its connection with the Suburban Action Institute between the time when the grant was first announced and the time when it was once again reviewed . . . on December 1, 1973. Mr. Paul Davidoff, Director of the Suburban Action Institute and Project Director of the study [being financed by NEArts], has assured this office that there is no longer a tie between the two organizations.

They still have the same address, the same officers, the same purposes, as nearly as we can make out.[6] We think NEArts will always choose to accept the foundation-developer's verbal assurance until Congress requires it to adopt higher standards. The purpose of this grant, by the way, was twofold, as announced by the NEArts on April 23, 1973: to break down zoning and to develop racially- and economically-integrated communities in five towns in New Jersey, New York, and Connecticut. These, said NEArts in its letter of December 6, were the five towns in which SAI had already commenced to have the zoning modified accordingly. Such action had indeed been commenced, in this town as in the other four, but not by SAI; by GCDC. NEArts, upon learning of its error, had allowed, permitted, or encouraged the foundation-developer to rewrite the purpose of the grant. This was seven months after the grant had been awarded.[7] The purpose of the grant is now very general, general enough to encompass the earlier-stated purpose, and too general ever to allow misuse to be charged, in our view.

III. *Foundation should not be allowed to make grants for a "study" where grantee is not a true scholar. A grantee is not a true scholar where he has announced that he has reached a particular conclusion and he advocates that conclusion.*

It is clear to the critics of the NEArts grant that that "study" was to be a series of "studies" by "experts" to be presented to the zoning authorities to convince them to down-zone the area in question in order to allow developer's proposal. NEArts has insisted that the foundation-developer has stated that the "study" would be "objective." The four hundred people who attended the New Fairfield Zoning Board hearings on August 14, 15, 16, and 28, 1974 and heard the developer's attorney and his consultants present their "studies" in advocating his position, know that the "study" was quite as unobjective as might be expected.

An urban planner who has announced that he advocates his own ideology is simply not capable of doing a "study." Mr. Davidoff is such an urban planner. In the section quoted below from the Davidoff-Gold article of 1970 in *Journal* of the American Institute of Planners, the authors give us first a quick survey of

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[6] Some changes took place during June 1974. But as of Sept. 5, 1974, Gold is still a trustee of SAI, though Mr. and Mrs. Davidoff are no longer Directors of GCDC. See Report B158811 of Comptroller General, p. 13.

[7] This is one of the disturbing indications of insincerity which the Comptroller General failed to notice. See penultimate paragraph, p. 10, *Report* B158811. Seven months after NEArts had eliminated all SAI's competition for this grant, it permitted SAI to reenter the "race" without opening up the race to competitors. SAI's revised statement of purpose is dated November 29, 1973, one day before the second reconsideration of the propriety of this award by the National Council on the Arts. NEArts deleted the date from copies of this application later made public.

the growth of the idea that the planner should be an advocate, imposing his own views upon society:

THE WHITE ADVOCATE IN SUBURBIA

> Early discussions of the advocate planner's role stressed efforts on behalf of the black and the poor in central cities.[7] Later variations on this theme included the discussion of the advocate role every planner plays in speaking for the interests of a client. Lisa Peattie and others have noted that only a narrow line exists between representation of a client's interests and attempted imposition of the planner's values on his client when he acts as organizer as well as technican in advocate projects in the ghetto.[8] [p. 20]

The authors continue by pointing out that their organization, SAI, represents only itself, speaks only for itself, and promotes its own ideology.

> In Suburban Action's efforts, we assume the role of advocate for an interest that is otherwise unrepresented in suburban planning debates—unrepresented not because it is unorganized, fearful, or voiceless, but unrepresented because it is not there. Consequently, we are speaking for what we regard as our clients interests—in fact, we are speaking for ourselves as white planners who want to see changes in suburban economic, political, social, and physical structure.
>
> Suburban Action represents the institutionalization of a concept concerning one form of advocate planning. This concept emphasizes the role of the planner as a proponent of goals, as an actor concerned with the purposes of the system for which he plans. This view stems from a theory of planning that suggests that at least some planners should more actively espouse purposes than means. It is not a denial of the importance of the planner's technical role where he details effective ways to accomplish given goals. But it does rest on the belief that an essential part of the planning process is the determination of appropriate sets of ends for a system.

The planner *may* seek to represent a client, continue the authors. But they take an alternate view:

> An alternate view of a planner concerned with formulation of goals is one that shows the planner presenting his own ideas in regard to goals. Here the planner is acting to see that a certain social situation is achieved. He does this because he believes it important for one or more reasons, but he does not propose goals in order to satisfy a client. In fact, in this case he has no client other than his own ideology.

They see their role as one which "threatens to tear apart the fabric of society . . ." Consequently, in any given community, they are likely to have a difficult time trying to find allies, but among the allies are, they find, the foundations.

To suppose that such gentlemen are scholars, willing to, wanting to, do an objective study of the role of zoning in curing urban problems, is to suppose that the Arabs are willing to, wanting to, do an objective study of the role of Israel in the Middle East.

Any yet the President's Committee on Urban Housing hired them as "contractors" for its "study," *A Decent Home*.

And yet the Twentieth Century Fund hired them just after they had announced their goal of breaking down zoning, to do a study on "whether problems of race and poverty can ever be resolved without taking steps to marshall the resources of the suburbs," according to its 1970 annual report.

And yet many foundations have given them money for studies.

And yet the National Endowment for the Arts gave them a grant to study the effect of breaking down zoning.[8] Their want of scholarly qualifications for this

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[8] And yet the Comptroller General naively assumes that their "study" will be objective." See *Report*, B158811, p. 14.

study has been noticed. The Sherman Civic Association remarked that they "are not impartial scholars. Their attacks on zoning show that they have already reached a conclusion on the question they are supposed to be studying." Town Supervisor George F. Oettinger of New Castle, New York, said:

> Suburban Action is so bold as to publicize that the same architect, Peter Kitchell, who designs the commercial and residential developments will head the research project financed by the grant. [*Patent Trader*, May 17, 1973]

(Peter Kitchell presented the Davidoff/Gold brief to the zoning authorities in New Fairfield, in Ridgefield, in Lewisboro.) Mrs. Lee V. Blum of Lewisboro wrote:

> I am dismayed, because any researcher or statistician worth his salt knows that statistics can be slanted in direction and are only as objective as the researcher handling and interpreting those figures. . . .
>
> At the Suburban Action Institute conference held on January 17 of this year [1973] . . . which I attended, the majority of the speakers addressed themselves to the primary task of "breaking the zoning in the suburbs."
>
> What kind of objectivity can be expected from researchers such as Suburban Action Institute? [*ibid.*] See "Q."

I have already adverted to the fact that our side of this controversy, the case in favor of retention of local control of zoning and planning, has strong economic justification, and the other side, the Davidoff/Gold/foundation side, correspondingly weak. I may further mention that as between a single-family house and a multifamily unit of equivalent amenities and size, there is no significant difference in cost of construction. Figures provided to us by the Hartford Area Office of HUD, which is the best source, as I am informed by competent authority, are these:

	Single family	Multifamily
Replacement cost of improvements	$17,594	$16,660
Market price of equivalent site	5,500	[1] 2,000
Miscellaneous allowable costs	600	1,800
Marketing expense	1,180	600
Total replacement cost	24,874	21,000

[1] No write down.

The unit in question includes four bedrooms, one-and-a-half baths, 1154 square feet for the single-family house and 1,350 square feet for the multifamily unit. Deducting the site cost, the reader will see that there is a difference of only $372 between the two units. (Full particulars are in the HUD letter, "R–1" attached.) But in fact the difference is far smaller than $374, for in a letter written a month later (January 2, 1973), HUD states:

> In reference to your letter of December 12, 1972, your conclusion that there is only a slight difference between the cost of construction of a single-family house and of a multifamily dwelling unit is correct. Your assumption about the quality being comparable is also correct.
>
> Discussing land costs, we know that land costs have increased in the past and expect them to continue so in the future. *Wherever the land has been down zoned to permit multifamily housing, the land cost rise has automatically followed.* (Emphasis added. See R–2, attached.)

This proposition—that down-zoning raises the cost of land, and that there is no significant difference between the cost of a single-family dwelling and a multifamily dwelling of equal size and amenities, is disputed by Messrs. Davidoff and Gold. Their case illustrates the fact that they are "advocate planners," and, therefore, not capable of scholarship:

THE ADVOCATES' NEW MATH—BY DAVIDOFF AND GOLD

The column at the left is part of their article on "Exclusionary Zoning," published by the Yale Review of Law and Social Action (1970). They assume an identical house, first on a one-acre lot, and then the land down-zoned to one-quarter of an acre. They find that the total cost of land, land-development, and construction is $45,000 in the first instance and $24,500 in the second, and, thus, that a seventy-five percent down-zoning leads to a forty-six percent saving in cost.

(The inference may be made—but it will be erroneous[9]—that all this saving will be passed on the the buyer of the house.) In fact, the saving is not forty-six percent, but only thirteen; and the example fails to take account of the fact that with down-zoning from one acre to one-quarter acre, a sewer, not needed before the down-zoning, will be needed, in all probability. The sewer will wipe out all conceivable savings, both at the time of installation, and annually thereafter to pay the maintenance cost; and, further, through permitting high-density development, which will further raise all costs in the municipality.

The errors by which they postulate that a seventy-five percent down-zoning will effect a forty-six percent saving are the following: (a) an error in addition; (b) an unwarranted assumption that after the down-zoning, the *lineal* cost of development will fall (*i.e.*, a smaller cost on a smaller frontage; (c) a departure in the text and in the computations from the assumption of *a given house*, of 1500 sq. ft. (as it says in the column captions of both columns). They are actually comparing a house of 1500 sq. ft. with a house of 1000 sq. ft., thus effecting a one-third saving on the cost of "the" house!

This Davidoff/Gold article was given as testimony before the New York State Division on Human Rights, "Hearings on Exclusionary Zoning." It may be supposed that this numerical example, coming from urban planners with a reputation for competence and action, was influential with the Committee, which itself was probably predisposed to believe that zoning "excludes" "the poor and the blacks."

The Column below is from Davidoff & Gold, "Exclusionary Zoning,"[10] Yale Review of *Law and Social Action*, vol. 1, No. 2 & 3, Winter, 1970.

TABLE II.—COMPARISON OF COSTS OF LAND, LAND DEVELOPMENT AND CONSTRUCTION FOR SINGLE-FAMILY HOMES IN EXCLUSIONARY AND NONEXCLUSIONARY SUBURBS

Item	1 acre lot [a] 200 ft frontage 1,500 ft² house	¼ acre lot [b] 100 ft frontage 1,500 ft² house
Land	$10,000	$5,000
Land development	9,000	3,500
Construction	[c] 24,000	[c] 16,000
Total (exclusive of financing)	45,000	24,500

[a] Assumes frontage costs of $45 per lineal foot.
[b] Assumes frontage costs of $35 per lineal foot.
[c] Assumes construction costs of $16 per square foot.

According to the Davidoff/Gold assumptions, a house built on a one-acre lot compared with on a quarter-acre lot will lower the cost, not from $45,000 to $24,500 as in their Table II, as they say (in the left-hand column), but from $37,500 to $32,500.

1. Note that in adding up the costs of the one-acre-lot house, they come out with $45,000, whereas any unbiased first-grader would see that this adds up to $43,000.

[9] Indeed, the opposite appears to be the case. The builder apparently pockets it. The following statement is my authority, and it is remarkable because it was written by the builders and other friends of the construction industry, themselves:

". . . [M]any builders set out to build under the Section 235 program but found that if they could produce a unit anywhere near the cost limit, they could easily market the house for much more."

The source is, *The Report of the Governor's Task Force on Housing, A Housing Strategy for the State of Connecticut* (1972, technical ed.), p. 25. By the Governor's Executive Order, only "persons with a proven record in housing" were to be on this Task Force. The Governor instructed them not to study whether or not there was a housing shortage, but to commit themselves to producing housing. There had been enough studies of the housing shortage, the Governor said. In fact, there is no physical shortage of housing justifying the massive down-zoning recommended by this *Report*. The statement just quoted is followed by, "There is [therefore] a large moderate income market not being served." Perhaps. But it is hard to see how builders can be induced to redistribute their profits to home buyers in a democratic society, and the *Report* does not pretend to find a solution.

[10] "Major portions of this article were originally presented as testimony at the New York State Division on Human Rights Hearings on Exclusionary Zoning. The authors also draw in part on their article entitled "Suburban Action: Advocate Planning for an Open Society," 26 Journal of the American Institute of Planners 12 (1970), co-authored with Linda Davidoff."

2. The D/G figures on land development are patently fishy. There is no reasonable basis for assuming that the frontage-cost per lineal foot of a larger lot should be higher than of a smaller lot. Assuming, then, land-development costs of $35 per lineal foot, the land-development cost of the larger lot is not $9,000 but $7,000 (200' × $35). This brings the total cost of the larger-lot house to $37,500 ($10,000 + 3,500 + 24,000).

3. The heading on the second column implies that the house is identical (1500 sq. ft.) before and after the down-zoning. But, in fact, D/G have used a 1,000 square-foot house to arrive at the figure of $16,000 for "construction" of the small-lot house. (See text just below table.) If the house is identical—as it must be for a comparison—and we use the larger size house, the smaller-lot house gives a total cost of $32,500 ($5,000 + 3,500 + 24,000), rather than the $24,500 which they come up with.

4. Thus a 75% down-zoning in lot size, which they postulate, gives, not a 45.6% fall in cost of land, land development, and construction, but only a 13% saving.

5. That saving does not take account of the fact that houses on quarter-acre lots will probably require sewers, and houses on one-acre lots will not. The installation cost of the sewer for the smaller house will further narrow the difference, and that difference will be more than wiped out by the annual maintenance cost for the sewer.

Down-zoning does not lower the cost of housing and may raise it.

Presumably, the foundations' reason for giving grants to SAI is their belief that SAI may be able to break down zoning, which they call "exclusionary" zoning, and (thus) lower the cost of housing "for the poor and the blacks." This is not the case, though most people may think it is. The authorities who support our view are those whom SAI accepts, for example:

1. The American Society of Planning Officials, in a study of the zoning of Connecticut in 1967, said:

> Reducing the lot-size limit that could be imposed by zoning would not prevent developers from building expensive houses on smaller lots—a practice that exists even now.[11]

2. At SAI's own "third annual conference" held on January 17, 1973, Bernard Friedan, director of the Joint Center for Urban Studies of MIT/Harvard, who has written a booklet aimed at breaking down zoning, said, "Even without exclusionary zoning it is not possible to build low-cost housing in the suburbs."

3. At a conference attended by SAI's Davidoff and Gold at the Potomac Institute, a review of which was published in March, 1973, it is stated:

> The presence of zoning districts for multifamily housing . . . does not assure that low income households will have access to a community. . . . This is not because higher densities necessarily decrease per-unit land and construction costs—in many cases this may not be the case. . . .[12]

This Conference was also attended by a representative of the Rockefeller Brothers Fund, Portia Smith, and by others associated with home-building and zone-breaking organizations.

4. In the "Introduction" to the *Syracuse Law Review* volume on "exclusionary zoning" to which Mr. and Mrs. Davidoff have contributed an article, Robert M. Anderson, reviewing the articles, states:

> As suggested in the Williams article, there can be no assurance that the elimination of land use controls [*i.e.*, zoning] would result in a solution of the housing problem. The lack of housing for minorities and the poor is a product of rising costs, high interest rates, the fiscal problems of local governments, and a broad spectrum of other factors. All of these obstacles must be surmounted before the basic problem can be solved . . . [p. 473, vol. 22, 1971]

In addition to these generalizations by authorities acceptable to those who are engaged in breaking down zoning on the ground that it will bring housing "for the poor and the blacks," there are empirical data: Land constitutes only two percent of the monthly maintenance cost of a $16,000 house. Thus if the cost of the land could be cut down by half, which would require a down-zoning of

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[11] *New Directions in Connecticut Planning Legislation: A Summary Report*, p. 31.

[12] Herbert M. Franklin, *Controlling Urban Growth—But For Whom?* (Washington, D.C., The Potomac Institute, Inc., 1973, p. 25.) The conferees are listed at pp. 1 and 2.

very much more than that proportion, the saving effected would be only one percent.[19]

Indeed, the Davidoffs and Mr. Gold say the same thing in effect in their article in the *New York Times Magazine* of November 7, 1971. "The Suburbs Have to Open Their Gates." Their statement appears in a useful analysis of that article, by a resident of our Town, and I give it in full because I think it offers illumination on how our tax laws are being abused by 501(c)(3) organizations. (The statement in question is italicized.)

[From the Sherman (Conn.) Sentinel, May 9, 1973]

ON SECOND THOUGHT

(By Philip Smith)

At the last Sherman Civic Association meeting the audience was urged to read an article entitled "The Suburbs Have to Open Their Gates," published in the magazine section of the New York Times of November 7, 1971. It was written by three urban planners in the Suburban Action Institute (SAI), one of the organizations involved in the projected Sherman-New Fairfield housing development.

I want to add my endorsement, but warn readers to keep their wits about them when reading the article. You can't skim it or read it casually and get wise to its purpose.

When the article was published I clipped it and filed it with other examples of the public relations (P.R.) art, thinking some day to use them in an article to be entitled "How to Con the Public."

Perhaps, because in my wayward life I have been public relations counsel and investigative reporter, I am unduly sensitive to publicity, but my suspicions are aroused whenever zoning is damned out of hand and said to be designed to keep out the poor and the blacks. On the other hand I may not be too biased. I loaned the article to a knowledgeable Shermanite who returned it with the comment "a P.R. mish-mash."

It makes a very persuasive case for abolishing zoning by mixing fact with assumptions and straight statements with distortions characteristic of slanted articles. It takes real writing skill to grind an axe without the axe showing. Fortunately, the SAI has not yet fully developed that skill.

In view of the statement made to Harry Hansen that the threatened project would not be subsidized by state or federal funds, the following paragraph from the SAI article is worth quoting. It says:

"Even if the vise (sic) of exclusionary zoning is removed, government subsidies and control will be required to see to it that the combined public-private market actually produces the needed housing . . . needed to eliminate the slums and ghettos of the central cities . . ."

If the threatened project is to be privately financed how can it provide housing for the poor and the blacks? Will it be under government control?

There is great need for honest information about housing, for articles that don't try to arouse our emotions and distract us by misusing the word "ghetto" and talking about people being "trapped in the inner cities." We need, for example, to be told why it is necessary and desirable to let the inner cities decay and build new cities in the rural areas; why construction of office buildings, auditoriums, and highways should be permitted to destroy about 700,000 housing units every year. What we don't need and should be on our guard against is slanted articles which seek to guide us.

SUGGESTED REMEDY: GRANTS SHOULD BE REVIEWABLE

A council should be set up to determine whether the grantee is a qualified scholar competent to do an objective study. The council should not be made up of foundation men or experts in the field, except that it should have the right to avail itself of the assistance of experts in evaluating the evidence. If the council finds the foundation guilty of giving a grant to a nonqualified grantee, the

[19] B. Bruce-Briggs, "The Cost of Housing," *The Public Interest*, No. 32, Summer 1973, p. 38. This page is appended and marked "S."

foundation should be required to pay a penalty, an amount equal to the amount of the grant. The penalty should be paid to the Internal Revenue Service, with a certain percentage of the penalty going to critic or critics of the grant who have materially contributed to information leading to the adverse finding, in the manner now customary in Internal Revenue cases.

THE FORD FOUNDATION: GRANT TO SUBURBAN ACTION INSTITUTE

The Ford Foundation recently gave a grant of $50,000 to SAI. We have made many attempts to find out precisely the purpose of the grant, but all in vain, and there are indications that it would be useless to address any further inquiries to the Foundation. It is a legitimate question, whether this money is for a "study," or, like the National Endowment for the Arts grant, for briefs by consultants done to facilitate actual construction of apartments, and for presentation before a municipal zoning authority in connection with a petition to downgrade the existing zoning ordinance.

On March 28, 1974, the fifth day after the grantee had been exposed by the *New York Times* for preaching "racially- and economically-integrated housing" but practising something closer to suburban-slumlandlordism, I telephoned the Ford Foundation and spoke with Mr. Robert W. Chandler, who was in charge of the grant. The purpose of the grant, said Mr. Chandler (who informed me, part way through the conversation, that he had more important work than to continue speaking about this grant) is "to help SAI in its research and planning for claims of low- and moderate-income housing versus claims of the environment."

I said, "What does that mean?"

Mr. Chandler answered, "Demands." There was a long pause. He did not further elucidate, and the impression was conveyed that I had been given all the information that, as a member of the public, I deserved.

In my letter to Vice President Marshall Robinson of March 30, I wrote, "Kindly advise (a) precisely what this[14] means—referring to the announcement of the purpose by the Foundation in its Letter of March 15—and (b) whether this is to be a study, or something more; and, if the latter, exactly what more." This inquiry was answered by Mr. Chandler who wrote, "The grant to SAI is for an expansion of its research and planning activities concerning housing needs and environmental quality as factors in the use of suburban land." My request for more precise information, got me an answer in still more general terms. *The more we ask, the less we learn. Is it not the duty of Foundations to release this sort of information?*

It would appear from additional information that either this grant is not for a "study" but is a grant to build, or, that the Ford Foundation does not care at all what SAI does with the money. The additional information leading to this conclusion is Mr. Chandler's remark to me over the telephone, "SAI doesn't have all the answers. If we saw the towns making provision to build housing, we wouldn't give to SAI. We haven't seen evidence of initiative by suburban communities to accept responsibility for helping to solve urban problems by building low- and moderate-housing." *Does the Ford Foundation have the right to impose its views on a democratic society in this fashion?* In addition to Mr. Chandler's remark, there is the remark by now Deputy-Vice President Winnick, published in a Ford Foundation booklet in 1965, suggesting that despite lip-service paid to

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[14] Ford Foundation *Letter*, March 15, 1974, states: "Suburban Action Institute, $50,000 over one year, to expand research and planning activities that seek to demonstrate that equal access to housing is not inconsistent with preserving the environment." By "equal access," SAI may be supposed to mean redistribution of property. SAI's news releases show that it has already decided that apartments in the countryside do *not* conflict with the environment. Indeed, the impression is given that with more apartments, the environment will *improve*. See for example, the SAI news release of November 14, 1972, "New Community in Westchester Will Be Environmental Landmark," attached and marked "T." (SAI's name has been lost from the top of the first sheet in reducing the size of the original.) There are additional questions which should be asked, after the apparent conflict between the environment and "equal access" is settled; for instance, what will be the effect of "equal access" on freedom—freedom of the property owner to use his property as he sees fit, which will be taken away from him if, in the name of "need for equal access," it is determinedthat the zoning ordinance in his town shall be substantially down-graded. And: what will be the effect of down-zoning in the name of "equal access" on low-cost housing?

the contrary, Ford really does think it "knows the answer" and intends to implement it.

> "Mr. Winnick asked how a foundation could help a profit-making organization. Mr. Norton [executive of a "private profit-making real estate foundation"] replied that there will have to be a companion nonprofit organization to take over the public education and service functions of Fair Housing as well as to conduct *what little research needs to be done.*[15]

When I asked Mr. Chandler whether he had read the *New York Times* exposé of SAI, the grantee, he said that he had not, and he admonished me that Ford's grant had been to SAI, and that it was GCDC (the wholly-controlled development affiliate of SAI) which had been exposed. He said, further, that he had read "all that" elsewhere, earlier. If so, Ford is the more to be blamed. Messrs. Davidoff and Gold are the founders, directors, trustees, of both organizations, and are not bound by any outside board. (SAI has a "Board of Advisers," but the information we have is that it does not meet.) It must be supposed that GCDC is implementing the peculiar political theories of SAI, the grantee of the Ford Foundation, and that it would behoove Ford to pay attention to published exposés.

In effect, Ford is using public funds—public, in the sense that Ford is but a steward of the money of others, distributing it in a manner which ought to be for "social improvement," and instead Ford gives grants to developers to implement its own theories. Such grants are irreconcilable with social responsibility.

In my letter to Mr. Chandler, dated March 30, enclosing a copy of notes of our telephone conversation for him to correct, if he found errors in it (but which he did not do, perhaps finding no errors), I asked:

> 9. If [there is no possibility of revoking the grant], before the grant is renewed or another one given, will you give those who desire it, notice and opportunity to speak against it?
>
> 10. If, before you decided to award this grant, a member of the public had inquired into whether or not you had made any grant or intended to make any grant, would you have invited him to give his opinion on it, before making it?

To these questions Mr. Chandler, in his letter of April 16, did not directly advert, and speaking generally, he remarked,

> The Foundation welcomes comments and criticisms pertaining to its work. We try to give all points of view a fair hearing, recognizing that some activities we support are by their nature controversial. However, it is not practical for us to hold public hearings before reaching decisions on the proposals we receive, of which there are tens of thousands annually.

This is not an adequate answer. No doubt, when critics write the Foundation, it files their letters in the file of the grantee. No doubt it would be a simple matter to give notice to those who had written, upon consideration of a new grant to that grantee. I once wrote the FPC about a question relating to Candlewood Lake, and now, everytime there is action in the matter of granting the license to the Connecticut Light & Power Company, which is related to Candlewood Lake, FPC sends me a notice of it. It would be no hardship for the Foundations, whose business is not to maximize profits, and who therefore do not have to keep

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[15] Emphasis added. Louis Winnick, *Housing and Urban Development: The Private Foundation's Role* (New York: Ford Foundation, 1965), p. 17.

McGeorge Bundy, president of the Ford Foundation, paid the same lip-service to objectivity—"We do not have all the answers."—in his contribution to the recent education supplement of the *New York Times*. As far as zoning is concerned, and housing, the contrary is the case, and Ford even employs the same "p.r. mish-mash" terminology as SAI. It, too, speaks of "minority families trapped in the Hartford ghetto" in a pamphlet called *A Decent Place To Live*, without author, without date.

Ford is not searching for the truth, or the answer. Ford is searching for implementation of its truth, and its answer, and forways to impose them upon society. In a democratic society, the people, through their elected representatives, make the decisions which this elitist group is now making for us and attempting to impose upon us, by grants like this one to SAI. Twenty years ago, foundations were impelled to conceal their objective of imposing their views of desirable societal changes. (See *Tax-Exempt Foundations: Hearings before the Special Committee to Investigate Tax-Exempt Foundations and Comparable Organizations*, House of Representatives, 83d Cong., 2d sess. on H. Res. 217, Washington, D.C., 1954, p. 671.) It might be a step in the right direction if foundations, instead of being forced to conceal their views, were encouraged to make them public. *The Public has a right to know. Recommended: a freedom-of-information act to apply to the foundations.*

an eye on minimizing costs, to alert all who have made themselves known, to a pending grant which concerns them. *Indeed, a central information bureau might be set up by the council on foundations of names of grantees and names and addresses of critics, that this information might be given to all foundations contemplating making their first grant to an applicant.* Some foundations may not want this information, and may not want to listen to critics. Others may not want this information with respect to some grantees, and may want it with respect to others. How little it would improve grant-giving to compel foundations to have it, and to hear it, perhaps can be guessed. It is at least a step in the "right direction," which is to avoid imposing harming the general welfare while attempting to help some particular class.

My letter to the President of Ford [See p. 226] was passed to the Deputy Vice President, who wrote me the following answer:

THE FORD FOUNDATION,
DIVISION OF NATIONAL AFFAIRS,
New York, N.Y., April 29, 1974.

Mrs. GERALD SIRKIN,
Sherman, Conn.

DEAR MRS. SIRKIN: Mr. Bundy has passed along to me your letter of April 23rd for reply. I have reviewed your correspondence with the Foundation and regard Mr. Chandler's letter of April 16th as a wholly adequate response. May I remind you of his key sentence: "The Ford Foundation has not invested in any of the developments of the Garden Cities Development Corporation and has no plans to do so in the future."? And as a further historical fact, the Foundation declined, over a period of years, to make any grants to the Suburban Action Institute until there occurred a legal separation from Garden Cities. Moreover, the Suburban Action Institute grant, like others of its kind, is regularly monitored to make certain that the agreed upon grant terms are faithfully adhered to.

I doubt whether further correspondence would add anything to change either of our views on this matter.

Sincerely,

LOUIS WINNICK,
Deputy Vice President.

SHERMAN, CONN., *April 23, 1974.*

Mr. MCGEORGE BUNDY,
President, Ford Foundation, New York, N.Y.

DEAR MR. BUNDY: I have read your contribution to the *New York Times*, education section, and am interested to know that the Ford Foundation believes it does not know the "answer" but seeks to promote its grantees to find the "answer."

Your recent grant of $50,000 to Suburban Action Institute interests us. By the same token, you will, we think, be interested to have an evaluation of the directors of the grantee organization as scholars, inasmuch as you have granted them a large sum for a "study." Such an evaluation is suggested by what appears on the reverse page.

May I ask in return that you kindly explain to me exactly what the Ford Foundation means by the phraseology in which the grant to SAI was given, in your March 15 *Newsletter*. I cannot understand the answer which has been given me by Mr. Chandler, and hope, therefore, that you will not ask him to answer this question again.

Yours sincerely,

MRS. G. SIRKIN.

Enclosure verso.

P.S. I should also appreciate your answering this question: Does the Foundation have a right to give money to a non-tax-exempt organization?

Notes [added 5/16/74]:

(1) Probably the "reverse page" was Appendix L.

(2) Mr. Winnick does not answer this question either.

(3) Nor this one.

Four points in Dr. Winnick's letter are worth commenting on.

1. His distinguishing between the time when SAI and GCDC were not legally separate, and the time when they became separte, is worth noting, as it implies that there was a period during which both organizations were not separate. This is contrary to the view claimed by other SAI-foundation-donors. However, it might be pointed out that GCDC first made its own news announcement, in contrast to its news announcements' being made always by SAI, only in October, 1973. And that announcement gives, as the address of the organization, the SAI address. Details elude us which apparently are available to the Ford Foundation to convince them that the real nature of the relationship has significantly changed.

2. With respect to his final paragraph, as he does not know that we have evidence that down-zoning will not lower the cost of housing and may raise it; as he does not know our evidence that zoning does not keep out "the poor and the blacks," his assertion, which implies that even if he did know it, he would not change his mind, is worth noting. It suggests that Ford is not interested in the truth, but in what *it* thinks is the truth, and that Ford is not interested in objectivity of its grantees.

3. Though he characterizes Mr. Chandler's letter of April 16th as a "wholly adequate response," Mr. Chandler omits to answer six specific factual questions. The public has a right to know the answers to these questions, but the Foundation will not tell. The *New Milford Times* reporter writes in an editorial that she could not get anyone to speak with here about this grant!

4. My letter of Mar. 29 sought assurance that there was no conflict of interest between giving this grant, which amounts to investing in the prospect of grantee's success in breaking down local control of zoning, and the recent large switch in portfolio of the Ford Foundation to land-development-company investments. I have been assured only that they have not invested in any GCDC projects. (Neither, apparently, has anyone else!) The question remains:

IV. *Should foundations be discouraged from both investing heavily in land and housing and giving grants to applicants whose activities, if successful, will have the effect of greatly increasing the value of those investments?*

Soon after the Ford Foundation gave $50,000 to SAI, whose goal is to break down zoning, the news broke that Ford has switched its portfolio significantly into land-development. The Taconic Foundation, one of the first grantors to SAI and still a grantor, is heavily in land-development and housing.[16] The Field Foundation, another generous grantor to SAI, has eighty percent of its portfolio in three trailer companies. One of SAI's goals in its court suits in New Jersey is to get the court to force municipalities to allow trailer camps.

Other organizations besides foundations, which have investments in land-development and in breaking down zoning, and which are obviously in a position to "affect legislation" by propagandizing, are radio and TV stations. CBS owns forty-nine percent of Klingbell, a builder of multifamily housing (that is, apartments). Westinghouse Electric owns Station WINS in New York City and has investments in land, and both Westinghouse Electric and Station WINS are presently being sued along with Westchester-County's largest developer, for two million dollars by the author of a book on zoning,[16a] whom they depicted as motivated by a desire to "keep out people"—the charge always made by the developers and vindictive egalitarians. These people, posing as benefactors of "people," or benefactors of the poor, aim to increase the value of their property by forcing the zoning authority to down-grade its zoning.

It is significant that editorials on WCBS and WINS always take the position of the developers and vindictive egalitarians. A recent editorial on Station WCBS-TV which attacked the zoning of the Town of New Canaan, Connecticut, was written—as WCBS-TV has admitted to me in a letter—with the assistance of SAI's Neil N. Gold. [See Appendixes X–3 and X–4.]

How the causual relationship runs between making grants to zone-breakers and investing in land which will rise in value once the zoning is broken, or whether there is a significant causal relationship at all, I do not know. But, as foundations are trustees of quasi-public money, they should, like Caesar's wife, be above suspicion.

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[16] See Taconic's list of stocks held as of 1971, appended and labeled "X–1" and "X–2."
[16a] *Property Power*, by Mary Ann Guitar (Garden City: Doubleday, 1972).

V. *Responsible legislators have for some years been concerned to insure that foundation grants are not used to influence political campaigns or present one-sided arguments for legislation. What can be done to encourage more conformity with this goal?*

EXAMPLES OF ONE-SIDED ARGUMENTS AND ORGANIZATIONS GIVING THEM

The example of the Suburban Action Institute has already been cited. There are two additional cases that come to mind, both concerning the propagandizing of a point of view concerning land-use, to the end that legislation be affected, or new legislation effected.

1. Regional Plan Association, "Choices for '76"

This 501(c)(3) organization presented a TV series last spring, "Choices for '76," and is repeating some of the "shows" this spring. They purport to be a "town meeting." But the presentation on land-use was one-sided, sales campaign being made for "cluster" zoning;[17] complicated economic questions were presented in a few seconds which need hours or months to properly explain, like replacing local property taxes for education with statewide taxes (type, not mentioned), or replacing local property taxes for all purposes with a property tax at the State level; like Federal housing-production subsidies versus Federal-housing-rent supplements to income. Ballots for the "voting" lay in great number in various places and there was admittedly no attempt to prevent a stuffing of the ballot box; group leaders were chosen selectively from groups known to favor RPA's pro-developer housing policies (like the League of Women Voters and church groups), to hold viewing and balloting sessions in their houses; and the results of the poll have been misused by the Regional Plan Association. For example, viewers by a wide margin voted to restore the cities; RPA says it now favors doing this, but an examination of RPA's program indicates that all it wants to put in the cities are institutions. It still does not want to put any housing in the cities. The housing, it wishes to put in clusters and in new towns out in the countryside, and all in the name of "saving open space" and "avoiding scatteration." As one critic wrote:

> The R.P.A. cannot be prevented from calling its series "town meeting" if it so chooses. But where only one party has access to the platform, where indoctrination is carried on by cell leaders and where no one knows who votes or how often, it looks as if the town it has in mind is Peking.[18]

This $1.6 million program was financed by many foundations, four or five of them being also benefactors of SAI, whose housing policies are identical with RPA's. (See Appendix C.) The Ford Foundation gave $95,000 to support these Peking Town Meetings, and another $130,000 "to promote citizen involvement in regional planning" in 1970. Altogether, the Ford Foundation has given the Regional Plan Association nearly $1.4 million since 1964, the effect of which, in so far as it has an effect, is to disintegrate home-rule and, concomitantly, good-government.

RPA reports that HUD gave approximately $800,000 to this Peking Town Meeting. *Should it have?* The purpose was to affect legislation, whether directly or indirectly. The means was propaganda—a one-sided presentation. There is a threat to our safety and welfare where the Government finances propaganda. With its enormous resources, it can overwhelm us.

Suggested remedy: HUD and other subdivisions and agencies of the U.S. Government which behave like foundations should be treated by your Honorable Committee as foundations.

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[17] "Clustering" is the placement of dwellings, whether single-family houses, townhouses, or garden apartments, on a plot of land in such away as to move them closer together than normally allowed by the zoning regulations. Supposedly, the land thus saved from building will be set aside as "open space." Frequently, however, there is no open space, or the open space gets built upon, or the open space is unbuildable anyway. Developers favor cluster because it allows them to build at higher than the allowed density, and it lowers their costs. Conservationists are sometimes attracted to it in the belief that it saves "open space." Developers often pose as conservationists in promoting it. William H. Whyte, of the American Conservation Association, is the chief publicist for it. The American Conservation Association is Laurance S. Rockefeller's, and Mr. Rockefeller is a developer. Another early publicist for cluster is Leon N. Wheeler, a past President of the National Association for Home Builders; see p. 6, note, above.

[18] Letter to the *New York Times*, June 5, 1973, from Natalie Sirkin.

HUD and the National Endowment for the Arts should come within the jurisdiction of your Committee in so far as they make grants.

2. Governor Rockefeller's Commission on Critical Choices for Americans

This Commission includes leaders in the anti-home-rule movement. They are Laurance S. Rockefeller: Edward J. Logue, head of New York State's Urban Development Corporation (who refused to take the job unless the State legislature would give him the power to override local zoning); Nancy Hanks, Chairman of National Endowment for the Arts, who has given a grant to SAI. The Executive Director is Henry L. Diamond, a man who advocated abolition of home-rule when he was Commissioner of the Department of Environmental Conservation for the State of New York.[19] Governor Rockefeller fathered a number of anti-home rule measures, and all of them were rejected by the citizenry: a Hudson River superhighway; referenda for bond issues for highways; the Rye-Oyster Bay Bridge; Logue's power to override local zoning (which the State legislature voted to rescind twice, the second time being necessitated by the Governor's having vetoed the measure the first time).

We have addressed a letter to all the members of this Commission, one-third of whom are Rockefeller-family, -institution, or -government associates, telling them why we think their Commission is a "stacked deck" on the subject of land use, a copy of which, as it was published in *The Yorktowner* of January 16, 1974, is appended and labeled "V."

It is difficult to get information on what is going on in this Commission. I have many times requested to be put on their mailing list for releases, been graciously assured that I have been, but have never received any releases without renewing my request. Nonetheless, the following information has been learned as to procedure:

The Commission is divided into panels, and each panel is deciding different issues. Very little money, relatively speaking, is to go into original research. Reliance will be put on research which is already done. In the matter of land-use, the only research which is generally known has been done by the anti-home-rulers, which effectively bars Panel No. 6, the Panel that will be considering questions of land-use, from getting more than a one-sided view of the question.

Panel No. 6 has twelve members, and among them are national leaders in the anti-home-rulers movement; L. S. Rockefeller, Edward J. Logue, Nancy Hanks. It is likely that few members who are not anti-home-rulers have ever before been exposed to this question. The Panel has no known pro-home-rulers.

It is apperently the approach to submit certain "critical questions" to the panels, but my request for the questions to Panel No. 6 has gone ignored. (A copy of my letter requesting this information is appended at "W.")

The lobby against home-rule is large and powerful, and includes a foundation set up by the Builders Institute of Westchester and Putnam Counties, for the purpose of educating the public in the "desirability" (to the builders) of "orderly" development, and the "dangers" of "haphazard growth." Laurance S. Rockefeller's "Task Force on Land Use and Urban Growth" includes people like Henry L. Diamond, James W. Rouse (entrepreneur of the "new town" of Columbia, Maryland), the League of Women Voters' National Land Use Committee Chairman, the Executive Director of the National Urban League, and Paul Ylvisaker. Ylvisaker was one of the "expert witnesses" in the case of Oakwood at Madison, at which SAI's Paul Davidoff was another "expert witness," concerning "exclusionary" zoning. It is not surprising that this Task Force recommends that every State adopt a UDC to take land by eminent domain and override local zoning, equating, "development" with the "public interest." (Our view is: What is good for the developers is not necessarily good for the country.) It is not surprising that the Task Force recommends that:

> *Existing non-profit organizations should be supported* [,] *and appropriate additional organizations established* [,] *that will provide government attorneys with the expert testimony, research assistance, and skilled tactical advice needed to prepare for important land-use cases.* Foundations could support one or more institutions of this type. . . . Eventually, after such organizations are established, they should be financed by voluntary contributions from state and local governments in small annual amounts.[20] [Emphasis in the original.]

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[19] See my article analyzing Diamond's "Preliminary Edition" of the Environmental Plan for New York State, "An Egg Facial for the Governor," *The Yorktowner*, Aug. 8, 1973, p. 13, attached and labeled "U."

[20] *The Use of Land: A Citizens' Policy Guide to Urban Growth*, A Task Force Report Sponsored by The Rockefeller Brothers Fund (New York: Crowell, 1973, p. 173.

The SAI is just such an organization, and the Rockefeller Brothers Fund, which financed that "study," is just such a Foundation which has given SAI support. In these controversial land-use cases, where the public has no financial support but must defend itself against the developer, the developer now has the expert assistance of "non-profit" tax-exempt organizations like SAI, who are financed by foundations like Rockefeller Brothers Fund; and to this powerful combine, Messrs. Rockefeller, Ylvisaker, Diamond, Rouse et als propose that state and local governments make contributions.[21]

Governor Rockefeller's Commission on Critical Choices for Americans should be recognized as the most recent, and the most prestigious, of the anti-home-rule organizations, and one more elite body to tell us what we should want, with a small budget for study and a huge budget for spreading the results around.[22]

Remedy: To expect foundations to police themselves is not likely to be efficacious, since so many of them are committed to "affecting legislation" through the courts, as the Internal Revenue Code disallows them from doing so directly through the legislature.[23] Should not "affecting legislation" be precisely defined to include the indirect means of the courts? Ends which are achievable through the courts, are no less effectual than where achieved directly through the legislature. Going through the courts, instead of through the legislature, is a means of defying the will of the voters and imposing upon them the will of an elite. If the anti-home-rulers' proposal is good, if their proposal will improve the general welfare, let them bring it forward through the legislature, and not sneak it in through the backdoor of the courts. Let the tax laws not avoid fulfilling their purpose by closing their eyes to the end, and concentrating their attention on the means—"affecting legislation" solely through the legislature—since it is not the sole means.

I am assured that the Tax Reform Act of 1969 reflect a concern on the part of responsible Congressional Committees to insure that foundation grants are not used to influence any political campaigns *or to present one-sided arguments for legislation.* I have tried to show that one-sided arguments are presently being put forth, under the sanction of the tax laws. I have suggested means for closing this gap which I hope will be helpful.

(Mrs.) NATALIE SIRKIN.

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[21] *The Use of Land* is written entirely from the point of view of the developer, which an occasional sentence noticing undesirable "overdevelopment" should not be allowed to cloud. "[D]evelopment initiated by private developers and builders, confers essential public benefits [p. 192]." "Orderly development" is equated with "the protection of natural, cultural, or aesthetic resources" for which the U.S. Supreme Court is exhorted to rule against zoning [p. 175], thus *affecting (adversely) legislation already declared "constitutional."*

[22] The results will be a scattering of the cities over the countryside in clusters, new towns, Puds ("Planned unit developments")—all to "avoid scatteration"; additional highway- and sewer-construction, allegedly to lower the cost of development by building them before an area is developed, but actually encouraging dispersion from existing cities, of industry and of population. Their view of what public policy should be, will deprive all municipalities of the right to control their own zoning, will put all municipalities through the state's Dull Homogenizing Machine, like dough through a noodle machine, depriving American consumers of the great range of places to live in, to suit all tastes and all pocketbooks, and making all municipalities look alike. If we are to outlaw the right of a municipality to decide its own zoning, and the right of a municipality to zone for large lots, because there are some people who cannot afford to live in other than a trailer, by the same reasoning we would have to outlaw mink coats because some people cannot afford them, and outlaw cloth coats because some people cannot afford them; and in the end we shall all be wearing Chinese blue pyjamas.

[23] Additional examples of grants that indicate commitment to a point of view include the Ford grants to the UDC and to TWO. The UDC does not need Ford's money. It has the power to float tax-free bonds. The Ford grant, of $200,000, is to promote "racially- and economically integrated housing," which is the aim of the Davidoff/Gold "new community" projects. By giving UDC $200,000, Ford is doing nothing more than demonstrating its "commitment" to what UDC stands for. Another questionable Ford grant is for almost $800,000 to The Woodlawn Organization, for "support of real estate, social services, and commercial activities." Woodlawn was described by sympathetic observers as the "underclass" of criminals who engaged in drug-pushing, murder, and other crimes, and who were the recipients of a one-million-dollar grant from OEO. This study points out that "This underclass is not something brought into the city by rural-to-urban migration or an indigenous black culture; it is instead largely the product of urban welfare policies, which institutionalize poverty . . ." ("Woodlawn; the Zone of Destruction," by Winston Moore, Charles P. Livermore & George F. Galland, Jr., *The Public Interest*, No. 30, Winter 1973, p. 42.) There is nothing in this up-to-date article to suggest that conditions have changed. One hopes that Ford has found some conditions changed, or its grant may further serve to institutionalize poverty.

This organization was thoroughly investigated by the Permanent Subcommittee on Investigations of the Committee on Government Operations in 1968; see parts 9, 10, 11 of *Riots, Civil and Criminal Disorders, Hearings*, 90th Congress, 2d Session.

SUMMARY OF SUGGESTIONS

I. Should foundations interested in housing and zoning be allowed to form "development affiliates" which are not tax-exempt? Should foundations in any field—to widen the question—be allowed to form subsidiaries in the same field?

II. Foundations should not be permitted to make grants to 501(c)(3) organizations which are affiliated with non-501(c)(3) organizations in the same field. Alternative: Define "separation" of the tax- and the non-tax-exempt organizations explicitly to prevent circumventing the law.

III. Foundations should not be allowed to make grants for a "study" where grantee is not a true scholar. A grantee is not a true scholar where he has announced that he has reached a particular conclusion and he advocates that conclusion. *Remedy*: Grants should be reviewable. A council should be set up to determine whether the grantee is a qualified scholar . . . not made up of foundation men or experts in the field . . . with a penalty amounting to the amount of the grant in cases of grants not permitted.

[IV.] A freedom-of-information act to apply to foundations. The public has a right to know—but without such an act, the more we ask, the less we are told by the foundations.

[V.] A central information bureau might be set up by the Council on Foundations . . of names of interested parties who might want to testify against the giving of a proposed grant.

IV. Should foundations be discouraged from both investing heavily in land and housing and giving grants to applicants whose activities, if successful, will have the effect of greatly increasing those investments?

V. What more can be done to induce foundations to present more than one-sided arguments for legislation?

[VI.] "Affecting legislation" should be broadened to include not only direct recourse to the legislature but indirect recourse through the courts. (This suggestion is discussed especially at pp. 29–30.)

LIST OF APPENDIXES

*Not included.

B

Filed and recorded, September 7, 1971.

PAUL J. SHERWIN,
Secretary of State.

License fee	None
Filing fee	$5.00
Recording	
Certifying copy	
Secretary of State	
Cert Relto	5.00
Total	10.00

CERTIFICATE OF INCORPORATION OF GARDEN CITIES DEVELOPMENT CORP.

First.—The name of this Corporation is Garden Cities Development Corporation. It is to be incorporated pursuant to New Jersey Statutes Annotated Title 15, chapter 1.

Second.—Whereas, the Governor and Legislature of the State of New Jersey declared the existence of a statewide housing shortage; and

Whereas, the impact of this shortage has been particularly severe with respect to the development of decent, safe, and sanitary housing projects for occupancy by families and individuals of low and moderate income and by non-white and minority group families; and

Whereas, this shortage is often aggravated by restrictive applications of local land use controls resulting in exclusion from many localities within the state of housing for occupancy by families and individuals of low and moderate income and by non-white and minority group families;

Therefore, the purposes for which this Corporation is formed are:

(a) To create a housing sponsorship vehicle to expand housing opportunities in the State of New Jersey for all income groups, but with particular attention to making decent, safe, and sanitary housing available to families and individuals of low and moderate income and non-white and minority group families in those localities from which it has been excluded, in whole or in part, heretofore.

(b) To engage in research activities pertaining to the development of housing and related facilities, on its own behalf, and on behalf of all other organizations involved in the production of housing and new communities.

Third.—The location of the principal office of this Corporation is at No. 715 Park Avenue, in the City of East Orange, County of Essex, and the name of the agent therein and in charge thereof, upon whom process against the Corporation may be served, is Neil N. Gold

Fourth.—The number of Trustees of this Corporation is four.

Fifth.—The names and addresses of the Trustees selected for the first year of existence of this Corporation are:

Paul Davidorff, 18 Forest Park Avenue, Larchmont, New York 10583.

Linda Davidoff, 18 Forest Park Avenue, Larchmont, New York 10583.

Neil N. Gold, 1174 Sussex Road, Teaneck, New Jersey 07666.

Martha B. Gold, 1174 Sussex Road, Teaneck, New Jersey 07666.

Sixth.—In extension and not in limitation of common law and statutory powers, this Corporation, acting through its Trustees, shall have the powers:

(a) To acquire, own, use, sell, lease, encumber assign, or otherwise transfer, dispose of, or deal in real or personal property or any interest therein.

(b) To own, operate, construct, acquire rehabilitate, or otherwise participate in the development of housing and related commercial, recreational, educational, and public facilities without limitation, either by itself or in association with other organizations or individuals, and to engage in research in aid thereof.

(c) To join in any and all forms of business relationships including the holding of stock in other corporations, and participation in joint ventures, general or limited partnerships, or associations formed to develop housing and related facilities.

(d) To accept loans, advances, loan insurance, guarantees, or other types of aid or grants from the Federal Government or any agency or instrumentality thereof, the State of New York or any agency or instrumentality or political subdivision thereof, or a private organization in furtherance of the Corporation's purposes.

(e) To invest and reinvest the principal and income of the Corporation in such property, real, personal, or mixed, and in such manner as they shall deem proper, and from time to time to change investments as they shall deem advisable; to invest in or retain any stocks, shares, bonds, notes, obligations, or personal or real property (including without limitation any interests in or obligations of any corporation, association, business trust, investment trust, common trust fund, or investment company) although some or all of the property so acquired or retained is of a kind or size which but for this express authority would not be considered proper and although all of the Corporation funds are invested in the securities of one company. No principal, however, shall be loaned, directly or indirectly, to any Trustee or to anyone else, corporate or otherwise who has at any time made a contribution to this Corporation, nor to anyone except on the basis of an adequate interest charge and with adequate security.

(f) To sell, lease, or exchange any personal, mixed, or real property, at public auction or by private contract, for such consideration and on such terms as to credit or otherwise, and to make such contracts and enter into such undertakings, relating to the Corporation's property, as they consider advisable, whether or not such leases or contracts may extend beyond the duration of the Corporation.

(g) To borrow money for such periods, at such rates of interest, and upon such terms as the Trustees consider advisable, and as security for such loans to mortgage or pledge any real or personal property with or without power of sale; to acquire or hold any real or personal property subject to any mortgage or pledge; and to assume any mortgage or pledge on or of property acquired or held by this Corporation in furtherance of the Corporation's purposes.

(h) To vote, to give proxies, to participate in the reorganization, merger or consolidation of any concern, or in the sale, lease, disposition, or distribution of its assets; to join with other security holders in acting through a committee depositary, voting Trustees, or otherwise, and in connection to delegate authority to such committee, depositary or Trustees and to deposit securities to them; to pay assessments levied on securities or to exercise subscription rights in respect of securities.

(i) To employ a bank or trust company as custodian of any funds or securities and to delegate to it such powers as they deem appropriate; to keep any or all of the Corporation property or funds in any place or places in the United States of America; to employ clerks, accountants, attorneys investment counsel, investment agents, and any special services, and to pay the reasonable compensation and expenses of all such services in addition to the compensation of the Trustees.

(j) To borrow money, and to issue evidence of indebtedness, whether secured or unsecured, and if secured to secure same by mortgage, deed of trust, pledge, or other means in furtherance of the Corporation's purposes.

(k) To elect officers, appoint agents, engage employees, define their duties, and fix their compensation.

(l) To execute and deliver deeds, assignments, transfers, mortgages, pledges, leases, covenants, contractual agreements, promissory notes, releases, and other instruments, sealed or unsealed, incident to any transaction in which the Corporation becomes involved.

(m) To have and exercise all powers necessary and conventional to the fulfillment of the purposes and objectives of this Corporation.

Seventh.—This Corporation shall exist in perpetuity unless dissolved by its Trustees in accordance with the laws of the State of New Jersey. In the event of such dissolution, all assets of the Corporation after payment of debts, shall be disturbed by the Trustees, provided that such distribution of assets upon dissolution of the Corporation may only be made to corporations, trusts, funds, foundations, or community chests created or organized under the laws of the United States, or any State or territory thereof, or the District of Columbia, or any possession of the United States organized and operated exclusively for civic, scientific, educational, religious, or otherwise public purposes, no part of the net earning of which inures or is payable to or for the benefit of any private shareholder or individual, and no substantial part of the activities of which is carrying on propaganda or otherwise attempting to influence legislation or intervene in any political campaign on behalf of any candidate for public office.

Eighth.—The Corporation is irrevocably dedicated to and shall be operated exclusively for its purpose on a nonprofit basis such that the income and assets of the Corporation shall be used only for Corporate purposes and shall not inure to the benefit of any individual, provided that nothing contained herein shall be construed as prohibiting payments to the Trustees, officers, agents or employees of the Corporation for reasonable expenses incurred and reasonable compensation for services rendered in the furtherance of the purposes of the Corporation.

Ninth.—The names and addresses of the incorporators of this Corporation are:

Paul Davidoff, 18 Forest Park Avenue, Larchmont, New York 10538.
Linda Davidoff, 18 Forest Park Avenue, Larchmont, New York 10538.
Neil N. Gold, 1174 Sussex Road, Teaneck, New Jersey, 07666.
Martha B. Gold, 1174 Sussex Road, Teaneck, New Jersey 07666.
Dorothy M. Finlay, 484 Elizabeth Rd., Yorktown Heights, New York.

Tenth.—Any person may rely on a copy, certified by a notary public, of the executed original of this Certificate held by the Trustees, and of any of the notations on it and writings attached to it, as fully as he might rely on the original documents themselves. Any such person may rely fully on any statements of fact certified by anyone who appears from such original documents or from such certified copy to be a Trustee under this Agreement. No one dealing with the Trustees need inquire concerning the validity of anything the Trustee purport to do. No one dealing with the Trustees need see to the application of anything paid or transferred to or upon the order of the Trustees or the Corporation.

No. 1123

STATE OF NEW YORK
County of Westchester, ss.:

I, Edward N. Vetrano, *Clerk of the County of Westchester and Clerk of the Supreme Court and County Court in and for said County, the same being courts of record having a seal,*
DO HEREBY CERTIFY, That D. Sheldon Goldman whose name is subscribed to the deposition, certificate of acknowledgment or proof of the annexed instrument, was at the time of taking the same a NOTARY PUBLIC in and for the State of New York, duly commissioned and sworn and qualified to act as such in Westchester County and throughout said State; that pursuant to a law a commission, or a certificate of official character, and an autograph signature of said NOTARY PUBLIC, have been filed in my office; that said NOTARY PUBLIC was duly authorized by the laws of the State of New York to administer oaths and affirmations, to certify that the acknowledgement or proof of deeds and other written instruments for lands, tenements and hereditaments to be read in evidence or recorded in said State, to protest notes and to take and certify

depositions; and that I am well acquainted with the handwriting of such Notary Public, or have compared the signature of said Notary Public on the annexed instrument with such Notary Public's autograph signature deposited in my office and believe that the signature on the annexed instrument is genuine.

No notary seal required by the laws of the State of New York.

In Witness Whereof, *I have hereunto set my hand and affixed by official seal this 30th day of July 1971.*

EDWARD N. VETRANO,
County Clerk and Clerk of the Supreme Court and County Court,
Westchester, NY.

Eleventh.—This Incorporation is to be governed in all respects by the laws of the State of New Jersey.

In witness whereof, we have hereunto set our hands and seals this thirteenth day of July, A.D., 1971.

Witnesses:

CHARLES LEE,	PAUL DAVIDOFF,
CHARLES LEE,	NEIL M. GOLD,
CHARLES LEE,	LINDA DAVIDOFF,
CHARLES LEE,	MARTHA B. GOLD,
CHARLES LEE,	DOROTHY M. FINLAY.

State of New York
County of Westchester

On the 13th day of July 1971, before me personally came Paul Davidoff, Neil M. Gold, Linda Davidoff, Martha B. Gold, Dorothy M. Finlay to me known to be the individuals described in and who executed the foregoing instrument and acknowledged that they executed the same

State of New York
County of Westchester

On the 13th day of July 1971, before me personally came Charles Lee the suscribing witness to the foregoing instrument, with whom I am personally acquainted, who, being by me duly sworn, did depose and say that he resides at 625 North Street, Grenwich, Connecticut that he knows Paul Davidoff, Neil M. Gold, Linda Davidoff, Marth B. Gold, Dorothy M. Finlay to be the individuals described in and who executed the foregoing instrument; that he, said suscribing witness, was present and saw them execute the same, and that he, said witness, at the same time suscribed his name as witness thereto.

NONPROFIT CERTIFICATE OF AMENDMENT OF CERTIFICATE OF INCORPORATION

The undersigned, the President and the Assistant Secretary of Garden Cities Development Corporation, duly incorporated under the laws of the State of New Jersey, hereby certify, that a regular meeting of the said Association held at its Club House at 715 Park Avenue, in the City of East Orange, on 7 May 1973, at 10:00 a.m. o'clock, and said Association by a majority of the votes cast by the members of said Association present at said meeting resolved to change the purposes of said Association as hereinafter specified, and to that end we do certify and set forth:

1. That the name of said Corporation in use immediately preceding the passage of the resolution as aforesaid, and at the making, recording and filing of this certificate is Garden Cities Development Corporation.

2. The location of the principal office of this corporation is at No. 715 Park Avenue, in the City of East Orange, County of Essex and the name of the resident agent therein and in charge thereof, upon whom process against the corporation may be served is Neil N. Gold.

3. The purposes of the corporation are:

(a) To create an entity for the sponsorship of, and to develop housing and related commercial and other facilities for all income groups, but with particular attention to making decent, safe and sanitary housing available to families

and individuals of low and moderate income and non-white and minority group families in these localities from which it has been excluded, in whole or in part, heretofore

(b) To engage in research activities pertaining to the development of housing and related facilities, on its own behalf, and on behalf of all other organizations involved in the production of housing and new communities.

In Witness Whereof, we have hereunto set our hands and the seal of the said Garden Cities Development Corporation, as aforesaid at East Orange, New Jersey on this 7th day of May 1973.

NEIL N. GOLD,
President.

Attest:

J. JACKSON WALTER,
Assistant Secretary.

STATE OF NEW YORK
County of Westchester: ss

Be it remembered that on this 7th day of May A.D. one thousand nine hundred and seventy three, before me, the subscriber, a Notary Public in and for the County of Westchester and State of New York, personally appeared J. Jackson Walter who, being by me duly sworn, does depose and say that he is the Assistant Secretary of the Garden Cities Development Corporation as aforesaid, and well knows the corporate seal of said Association so as aforesaid in the foregoing certificate named; that the same was so affixed thereto and the said certificate was signed by Neil N. Gold, who was at the date and execution thereof the President of the said Association, in the presence of said deponent, as the voluntary act and deed of the said Association in pursuance of a resolution so as aforesaid passed and that the said deponent at the same time signed the same as subscribing witness.

Sworn and subscribed before me at Tarrytown, New York the day and year aforesaid.

A. SEVENEVXO.

STATE OF NEW JERSEY,
DEPARTMENT OF INSTITUTIONS AND AGENCIES,
DIVISION OF PUBLIC WELFARE,
Trenton, N.J., May 8, 1973.

Re Garden Cities Development Corporation (Amendment).

Mr. NEIL W. GOLD,
East Orange, N.J.

DEAR MR. GOLD: This is to advise that we have reviewed the Amended Certificate of Incorporation pertaining to the above mentioned corporation.

In our opinion, this is not the type of corporation that is contemplated by R.S. 15:1–15 as requiring the affirmative approval of the Commissioner of Institutions and Agencies. Athough described and structured as a non-profit corporation, it does not appear to be essentially charitable or eleemosynary within the purpose and means of the cited statute.

This determination means that the approval of the Commissioner of Institutions and Agencies is found not to be a necessary prerequisite to acceptance of your amended certificate. You may not, however, infer that all aspects of the Amended Certificate of Incorporation are correct and approved. The office of the Secretary of State will advise you as to other statutory requirements.

We are retaining a copy of the Amended Certificate for our files and are returning the original herewith, which you may proceed to transmit to the Secretary of State who has been informed of our finding as stated herein.

Sincerely yours,

OGDEN GLENN,
Public Welfare Consultant.

P.S.—We also reviewed a copy of the original Certificate of Incorporation noting that the Secretary of State had filed your incorporation papers on September 7, 1971. We are retaining a copy of these papers for our files.

STATE OF NEW YORK,
DEPARTMENT OF STATE,
CORPORATIONS BUREAU,
Albany, N.Y., September 28, 1973.

Garden Cities Development Corporation, a New Jersey corporation, received authority to do business in this state 8/4/72 Westchester County.

We do not furnish extensive abstracts from certificates on file. An uncertified copy of the certificate of authority may be obtained upon statutory fee of $3.50.

JOHN P. LOMENZO,
Secretary of State.

C

[From the Yorktowner, Apr. 11, 1973]

CATCHBASINS FOR A DISINTEGRATING NEW YORK

THE DEVELOPERS CALL IT "SOCIAL CONSCIOUSNESS," BUT AUTHOR SIRKIN SEES DECEPTION AND TROUBLE FOR WESTCHESTER

(By Natalie Sirkin)

The "friends" of the American city can think of nothing better to do for it than to pull it apart and litter the countryside with it. Though the activities of New York State's Urban Development Corporation to force nine Westchester towns to accept apartments have slowed since President Nixon said the Federal Government will not pay for them, the issue is far from dead. In fact, now that the Regional Plan Association has launched its formidable indoctrination campaign with the same objectives as UDC's, it is more pertinent than ever to ask what UDC's purpose is. What motivates UDC to attach local zoning ordinances, in an attempt to force the construction of apartments, in rural Westchester towns, most of which do not allow apartments?

Their motive cannot be to fill a housing "need" in those nine towns. The UDC has not even attempted to show that the housing in those towns is "substandard" or "unsanitary," to a degree justifying its overriding the local zoning. As for Westchester County as a whole, UDC has been arguing that construction of housing cannot keep up with demand, under present regulations: and up until late January, 1973, they have been using a figure of 92,000 additional housing units required in the County by 1980. But half of that estimated 92,000 is based on expected immigration into Westchester, and only half is based on the increase of the natural population. In effect, they have been arguing that the construction problem arises from heavy immigration. On the contrary. The rate of immigration depends closely upon construction: for, to a great extent, the immigration is a response to the ready availability of housing.

Their reasoning has thus been hopelessly circular. They claim that a demand for housing exists, and that they are meeting that demand. They are not. They are creating a demand, by putting up additional housing. Their method of estimating "need" would mean that Westchester County could never supply enough housing to catch up with demand.

The more housing that is built, the greater the immigration in response to that new housing, and the more the housing which will (as a result) be needed to supply that expected greater immigration, etc., etc., etc.

On January 28, the UDC, without explanation, stated its estimate of additional housing needed by 1980 as 46,000 instead of 92,000, apparently eliminating the immigration component in response to criticisms of its estimating methods. But, though this correction removed the UDC's grounds for intervening in Westchester's home rule, no change in UDC's policy followed.

The UDC's motive cannot be to benefit the urban poor by relocating them in the rural areas. The inadequate employment opportunities, the high cost of transportation, the absence of mass transportation, the meager entertainments of country life compared to city life—all these are disadvantages for people of limited means, many of whom moved to the cities to escape them. It is significant that the Regional Plan Association, which found great number of people to complain on TV about the quality of their housing, could not find a single person who wanted to move out of the city and into the country.

Their motive cannot be to help the cities. They do not intend to redevelop city blocks which have been cleared for redevelopment, or to demolish apartments which they have emptied. Those apartments will be allowed to fill up again with still poorer people, attracted into the city by the vacancies. Neither UDC nor the Regional Plan Association has a plan to plug up the hole in the bottom of the boat.

So if they are not helping the people whom they intend to relocate, or the places they intend to move them from, or the places they intend to move them into, who is to gain?

Possibly the gainers include some who derive enjoyment from despoiling a pleasant area. There are unquestionably those who enjoy pulling others down, not to raise anyone, but leveling for its own sake. Let us hope that these vindictive egalitarians are no more than an aberrant fringe of our society.

But the main force behind the UDC, we believe, lies elsewhere. We can get a clue from looking at the occupations of the Directors of the UDC—building contractors, real estate middlemen, bank directors—all the people who will profit by breaking down zoning in suburban and rural areas. We can get another organization dedicated to breaking down zoning in suburban and rural areas, also, ostensibly, in the public interest—the Suburban Action Institute.

The Suburban Action Institute, of 180 East Post Road, White Plains, is a trust organized on June 16, 1969. According to their application to the Internal Revenue Service to be classed as an educational foundation, they received more than ten per cent of their income "for services rendered." What services? Rendered to whom? Their answer to another and perhaps-not-unrelated question on their application form is that they "will seek contract work with government agencies in the areas of research and development." What Government agencies? UDC?

Suburban Action Institute was granted foundation status. It can receive tax-free money not only from foundations but from any taxpayer. Its application states that it has been receiving money from the Stern Family Fund and the Taconic Foundation. The Taconic Foundation is also helping to finance the Regional Plan Association's present attack upon zoning; and the wife of one of Suburban Action Institute's founders, Linda Davidoff, is also associated with the Regional Plan Association.

Suburban Action Institute has been active in forcing apartments into municipalities which are zoned for single-family houses, in New York, New Jersey, and Connecticut. But foundations like Suburban Action Institute, organized under Section 501(c)(3) of the Internal Revenue Code, are distinctly barred from "carrying on of propaganda or otherwise advocating or approving pending or proposed legislation." There are some who suppose that local zoning ordinances in New York, New Jersey and Connecticut are "legislation" within the meaning of this provision. They may well wonder why the Internal Revenue Service has never withdrawn Suburban Action Institute's foundation status.

Suburban Action Institute has been active in forcing apartments into single-family zones apparently for altruistic reasons. But information has recently come to light that Suburban Action Institute has a business affiliate, Garden Cities Development Corporation, whose function is large-scale housing and commercial development in areas where zoning can be destroyed. Surprise, surprise! The same men who are the Directors of the Suburban Action Institute are also the Directors of the developer-affiliate.

Suburban Action Institute announced on November 15 that its developer-affiliate is planning a 4,600-apartment PUD ("planned unit development") with large-scale commercial facilities and other mass facilities in Lewisboro. Lewisboro is one of the "softer" of the nine Westchester towns where UDC is leading the developers' assault on local zoning.

This pattern—developers with gigantic projects preparing to follow UDC through the small and innocent-looking breach which UDC threatens to make in the local zoning ordinances—is already appearing elsewhere in Westchester.

In Somers, another of the nine towns, Henry Paparazzo, whose Heritage Village changed the rural character of Southbury, Connecticut, applied for a variance to put up a similar Heritage of 3,000 apartments.

Perhaps 3,000 did not seem horrendous compared with the 10,000 which the Town officials were told UDC intended to build originally. But whatever the reason, Paparazzo appears to have had no difficulty. He reported the councilmen "trying to be cooperative," and, at a Zoning Board of Appeals hearing, which seems to have attracted an unexpectedly large crowd, "something in the air in

Somers caused 'flu' to strike down two members" requiring cancellation of the meeting (Yorktowner, June 28 and October 21). In due course, Developer Paparazzo was granted his variance.

In Greenburgh, another of the nine towns, Robert Weinberg, founder of Robert Martin Associates, Westchester County's largest developer, has sold UDC seven-and-a-half acres of his tract of 177 acres. Now that UDC has pried open Greenburgh's zoning door, Developer Weinberg has appeared before the Planning Board with a proposal to wipe out the one-acre, single-family zoning and deposit a vast PUD of 1760 apartments, office buildings, and a shopping center on a narrow, serpentine country road. Developer Weinberg did not sell his seven-and-a-half acres to UDC because he thought that UDC's low-income garden apartments would enhance the value of his remaining 170 acres. On the contrary, he threatened a League of Women Voters' meeting, a year ago last spring, that unless he was allowed to build as he pleased, he would sell land to UDC. A few months later, Weinberg told the New York Times, "Within a half hour of here, I've got 500 to 600 acres I can't do anything with because of zoning. It's all zoned for one house an acre . . . We just can't run with local hometown rule. Every idiot can come down to the town hall and have his say and the guys up front tremble because they're afraid they won't be reelected (August 15, 1971)."

Developer Weinberg can, of course, make a reasonable profit by building single-family houses, as builders always have. But he prefers making a windfall profit, with the help of New York State's UDC, which intends to override local zoning wherever it chooses; and with the help of the Regional Plan Association, which intends to take the power to zone out of the hands of the municipalities entirely, and give it to the counties, who shall take into consideration the housing "needs" of New York City and Newark, and the rest of what it calls the New York Metropolitan Region, which extends from New Haven to Trenton, from Montauk to Pougkeepsie. The Regional Plan Association wants wall-to-wall peopling.

Can there be any doubt but that UDC's and the Regional Plan Association's socialwelfare arguments, thin and implausible as they are, are merely a new camouflage for the familiar old developers' battering ram?

As speaker at a zoning hereing recently observed, "It is a sad commentary when the owners of a piece of land are continually forced to defend their position against the encroachment of developers who disguise their aims under the heading of 'social consciousness.'"

D

[From the Sherman, (Conn.) Sentinel, Aug. 1, 1973]

VIEWS AND OPINIONS

Editor:

Since it is of public interest, I enclose a copy of a letter I mailed July 27 to the director of the National Endowment for the Arts.

MALCOLM COWLEY.

DEAR SIR: As the former recipient of a grant from the National Endowment for the Arts, I was horrified to learn that a later and more substantial grant—of $38,000—had gone to Paul Davidoff and Neil Gold of the Suburban Action Institute. I should like to know what connection, if any, exists between this grant and the arts in America.

Messrs. Davidoff, Gold, and their colleagues belong to an organization whose announced purpose is to upset local zoning ordinances by a mixture of law suits, propaganda, argument, and intimidation. Usually the method of Suburban Action Institute is to file requests for urban developments in various suburban or rural towns or townships. In this way the Institute forces many towns to defend their zoning regulations in court actions that—so the Institute threatens—will be carried to the Supreme Court at a legal cost to the towns involved of $200,000 or more for each action. The excuse for this is that the ghetto dwellers of New York, Bridgeport, Hartford, and other cities should have access at a low cost to the joys and advantages of suburban living. But in most of the proposed developments, the plans are so ambitious and the building costs so high that absolutely no one from the inner cities could afford to live in them.

Messrs. Davidoff and Gold profess to be acting for the public good. But one notes in every development with which their Institute has been associated that there is also present a land speculator bent on making the largest possible profit. For example, in the proposed WatersEdge development in the towns of New Fairfield and Sherman, the speculator holds an option to buy 270 acres. He has associated himself with Messrs. Davidoff, Gold, *et al* in their effort to upset the zoning regulations. If the effort succeeds, the speculator will make a profit of more than a million while having risked very little capital.

WatersEdge (our local Watergate) involves still other horrors. The developers are planning to build a community housing at least 8,000 people in a remote area without a safe water supply and without effective means of sewage disposal. The area borders on Candlewood Lake, already overcrowded and near the danger point as regards pollution. There are no highways to accommodate the 4,000 automobiles that the community would require.

There are schools nearby, but they are already overcrowded and could not possibly accommodate 2,500 new pupils.

Local representatives of the Institute talk grandly about building a new school that would accommodate perhaps 1,000 of those pupils. They talk about running hot-water pipes under the access road to keep it open in winter. They talk about sinking a huge pipe under Candlewood Lake that would cross Candlewood Mountain and eventually drain the sewage of the new community into the Housatonic River, after passing through a new sewage plant to be built jointly by New Milford and Brookfield. Neither of those towns, however, has undertaken or has even been requested to accommodate the sewage of 8,000 nonresidents. Moreover, there are other problems created by siting this new community in an area where there is no public transportation, or prospect of such transportation, and where there are no industries to provide new residents with jobs. The residents would have to travel long distances by private automobiles to their places of employment, thus burning up more gasoline and adding to the overcrowding of the highways and the pollution of the countryside.

WatersEdge is our local example of the sort of activity now to be encouraged by a grant of $38,000 from the National Endowment for, my God! *the Arts.*

The problem of housing the 40 million people, more or less, of our Eastern Megalopolis, the vast urban and suburban area extending from Portland, Maine, to Norfolk, Virginia, simply cannot be solved by upsetting the local zoning ordinances of one little town after another. If Messrs. Davidoff and Gold succeed in their undertaking, the effect will be to hasten the process of depopulating the cities and destroying the open countryside. More and more suburban sprawl. Higher and higher taxes for those who now live in the little towns. More and more crowded developments that will turn quickly into new slums.

Of course what our vast conurbation needs is more long-range planning for larger and larger areas. There should be new towns—many of them—but they should not be placed at random wherever Suburban Action Institute finds a greedy landowner and weak-kneed town officials. They should be placed where there is need for new industries or a new labor force. They should be placed near highways and railroads and in districts with a safe water supply. They should be planned so that people of different races and different incomes can live there in comfort and security and find employment in the neighborhood.

Around the new towns—and the old ones too—there should be a greenbelt where building is severely restricted and where every effort is made to preserve farms and open spaces. That brings me back to WatersEdge, the latest Davidoff-Gold monstrosity. In any logical plan for the metropolitan area, Sherman and New Fairfield would not be the site for a new town. They would be part of a greenbelt area preserved for the benefit of everybody—not only for their own residents, but also for city dwellers who would like to find green pastures and fresh air without traveling for hundreds of miles.

That is one of the ideals that Messrs. Davidoff and Gold are trying to destroy. For them to be encouraged by the National Endowment for the Arts seems to me a complete turning away from the purposes for which the Endowment was funded by Congress and which it has served admirably in the past. Oh, yes, the grant to them is "for study," but with their background and announced purposes, everybody knows what the results of the study will be. In this great country eager for the arts, aren't there projects and artists that the Endowment

can sponsor without diverting $38,000 to confrontation politics and an undertaking that is essentially short-sighted and destructive.

Sincerely,

MALCOLM COWLEY.

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HOLMDEL TOWNSHIP,
Holmdel, N.J., July 18, 1973.

MARSHALL MUNCH,
Sherman Civic Association,
Sherman, Conn.

I am enclosing a copy of an article which appeared in a New Jersey newspaper. From the article, it seems that the Town of Sherman is faced with a problem similar to the Township of Holmdel in New Jersey.

We, along with a number of other New Jersey municipalities, are being sued by Suburban Action Institute. In an effort to ascertain the real motives and money behind Suburban Action Institute, we find information like that reported by your organization to be of great interest.

The article stated that a grant had been received from the National Endowment for the Arts. Do you have any information regarding this organization? Specifically, if it is a department of the Federal government, or what branch of the Federal government it is under? Is it inferred in your release that the National Endowment for the Arts is not a Federal organization, but receives some Federal support? If you have any additional information which you think would be of interest to us, we would appreciate it if you could forward it to us.

There is a group in Holmdel incorporated under the name United Citizens for Home Rule, which may have a similar purpose as the Sherman Civic Association. Any information which you pass on to us we would forward to the United Citizens for Home Rule in hopes of disseminating this information as broadly as possible.

Thank you very much for your interest.

JACK COUGHLIN, *Administrator.*

Enclosure.

[From the West Essex Tribune, Livingston, N.Y., July 5, 1973]

SUBURBAN ACTION INSTITUTE GETS $38,000 GRANT FROM FEDERAL AGENCY

A statement released this week by a Connecticut organization indicates that the Suburban Action Institute has received a $38,000 federal grant. The SAI currently has suits against Livingston and several other New Jersey municipalities pending in court, attempting to overturn the present concept of zoning.

The Sherman Civic Association of Sherman, Connecticut, announced this week that SAI had recived a grant from the National Endowment for the Arts in Washington, D.C., to be used for "study."

The report from the Sherman Civic Association continued that Suburban Action Institute operators Paul Davidoff and Neil Newton Gold "are not impartial scholars. Their attacks on zoning show that they have already reached a conclusion on the question they are supposed to be studying. They are known developers, who proposed to build apartment houses and commercial facilities in our town (Sherman, Connecticut) and New Fairfield, and in Ridgefield; in Reading and Mahwah, N.J.; in Lewisboro, N.Y."

Town supervisor George F. Oettinger of New Castle called the attention of his congressmen to the $38,000 grant with the statement: "SAI is so bold as to publicize that the same architect, Peter Kitchell, who designs the commercial and residential developments, will head the research project financed by the grant."

The Sherman Civic Association charged that federal government funds being used in this manner amount to "taxing us for funds being used to attack us." The statement continued that the residents of such towns as Livingston, which are being attacked in the courts on the premise that municipal zoning does not allow the construction of low income housing, "must now dig into our pockets to raise more money to defend ourselves."

The association has called for an investigation of the grant by the U.S. Congress on the ground that it is a misuse of funds.

F

SHERMAN CIVIC ASSOCIATION,
Sherman, Conn., May 11, 1973.

HON. RICHARD M. NIXON,
President of the United States,
Washington, D.C.

DEAR MR. PRESIDENT: It would be appreciated if you would request the Secretary of the Treasury to request the Internal Revenue Service to rule on the question of whether the Suburban Action Institute should be permitted to retain its tax-exempt foundation status.

The Suburban Action Institute is a non-profit tax-exempt foundation organized under Section 501(c)(3) of the Internal Revenue Code. Although distinctly barred from engaging in "the carrying on of propaganda, or otherwise attempting to influence legislation"—as stated in the application form for tax-exempt status—it has nevertheless commenced law suits to influence legislation in the form of the zoning ordinances of New Canaan and numerous other municipalities in Connecticut, New York, and New Jersey. (See *New York Times* of 3/7/71, p. 56, and its Magazine, 11/7/71, "The Suburbs Have To Open Their Doors," by the directors, Paul Davidoff and Neil Gold.)

Despite their tax-exempt foundation status, the directors, Davidoff and Gold, have formed a "development affiliate, Garden Cities Development Corporation (*NYTimes* 11/15/73)." The foundation has commenced action to break down local zoning ordinances in order to construct residential/commercial projects either by itself, or by its development affiliate, or in cooperation with still another profitmaking partner, in the towns of Readington and Mahwah (New Jersey); Lewisboro (New York); Ridgefield and Sherman/New Fairfield (Connecticut—*NYTimes* 4/2/72, 4/25/72, p. 47; 11/15/72; 4/13/72; (Danbury) *News-Times*, 5/6/73).

The Suburban Action Institute states that it receives financial support from the following foundations: "Rockefeller Brothers Fund; the Irwin, Sweeney, Miller Foundation . . .; the Taconic Fund . . . and the Field Foundation (*New Milford Times* 4/26/73, p. 2). In addition, it names the Stern Family Fund (now the Stern Fund) as another contributor in its application for foundation status filed with the Internal Revenue Service.

Our understanding of the spirit of the Community Development plank in the Republican Party platform of 1972 leads us to believe that the Suburban Action Institute is in alliance with forces working in direct opposition to that plank.

Yours sincerely,

President.

H

[From the Catholic Transcript, Nov. 9, 1973]

FOURTH ANNUAL MEETING AND CONSULTATION

CONSULTATION THEMES: "EXCLUSIONARY ZONING IN SUBURBIA"

OFFICE OF URBAN AFFAIRS OF THE ARCHDIOCESE OF HARTFORD

Albertus Magnus College, New Haven, Saturday, November 17, 1973

9:00 A.M.—Registration and coffee

9:20 A.M.—Opening Prayer—Most Rev. Joseph F. Donnelly, D.D., Auxiliary Bishop of Hartford

9:30 A.M.—Welcoming Remarks—Dr. Francis L. Horn, President, Albertus Magnus College and Rev. James J. Cenetrey, President of the Board of Directors, Office of Urban Affairs to the Archdiocese of Hartford.

9:40 A.M.—Introduction of Keynote Speaker:

"A Call to Action," Hon. Donald M. Fraser, United States Representative from Minnesota and National Chairman, Americans for Democratic Action.

10:30 A.M.—Reactor Panel—

Rev. John P. Cook, J.C.D., St. Martin de Porres Roman Catholic Church, New Haven, Moderator.

Atty. John Rose, Jr., Law Firm of Ribicoff and Kotkin, Hartford and Chairman, Connecticut Advisory Committee, U.S. Commission on Civil Rights.

Rev. Joseph D. Duffy, Professor adjunct of Church and Community, Yale Divinity School, New Haven and Past National Chairman, Americans for Democratic Action.

11:00 A.M.—Audience Participation—

Questions from the audience will be handled to the best of our ability; depending, of course, on the size of the audience.

11:30 A.M.—Break—

Participants are encouraged to visit the displays and exhibits in the outer lobby which represent the grantees from the Archdiocesan Cooperative Parish Sharing and Archdiocesan Campaign for Human Development Programs.

12:00 Noon. Introduction of Afternoon Speaker:

"A Call to Action in Connecticut"—Atty. Paul Davidoff, Co. Director, National Suburban Action Institute. Tarrytown, New York and author of "The Suburbs Must Open Their Gates."

12:40 P.M. Reactor Panel—

Rev. John P. Cook, J.C.D., Moderator.

Mr. William Olds, Executive Director, Connecticut Civil Liberties Union, Hartford.

Atty. Robert G. Oliver, Law Firm of Dagget, Colby and Hooker, New Haven and former member of the Connecticut General Assembly (House of Representatives).

1:00 P.M. Audience Participation—

1:15 P.M. Summary and Class:

"Strategies for Action"—Mr. Frederick B. Routh, Special Consultant to the Staff Director, U.S. Commission on Civil Rights, Washington, D.C. and Past President and Executive Director, National Association of Human Rights Workers (NAHRW).

Notice: At the end of the program there will be an official announcement of the formation of the Connecticut Coalition on Exclusionary Zoning in Suburbia. Please telephone your reservation to the Office of Urban Affairs of the Archdiocese of Hartford: (203) 77-7279 or (203) 777-7270.

This program developed in cooperation with the Archdiocesan Campaign for Human Development.

CLARICE A. OSIECKI,
State Representative, 103th Assembly District, Danbury, Conn.

I

[From the Catholic Transcript, Nov. 23, 1973]

COALITION TO FIGHT ZONING BAR

NEW HAVEN—Nine Civil rights and social action organizations banded together in a coalition here last Saturday to mobilize support for equal access in Connecticut's suburbs to "employment, land, and housing opportunities to which all people have a right."

The new Connecticut Coalition for Open Suburbs, formation of which was announced at the annual meeting of the Archdiocese of Hartford's Office of Urban Affairs, has as its purpose "the achievement of a more socially just and environmentally sound growth policy in suburban Connecticut."

Members of the coalition are the Anti-Defamation League B'nai B'rith, the Connecticut Civil Liberties Union, the Connecticut Council of Churches, the Connecticut League of Women Voters, Education-Instruction, the Ministry of Social Concerns, Diocese of Bridgeport, the National Association for the Advance-

ment of Colored People, the Office of Urban Affairs of the Archdiocese of Hartford and the Suburban Action Institute.

Some 300 persons attended the meeting, which heard speakers and panels discuss exclusionary zoning in suburban Connecticut.

One of the speakers, Congressman Donald M. Fraser of Minnesota, said that despite fair housing laws, "we have not found the answer to opening up the suburbs to minorities, a problem arising partly out of continuing attitudes about race, but more importantly, continuing negative attitudes toward the poor and the near-poor."

Congressman Fraser, who is also national chairman of Americans for Democratic Action, noted that "the suburbs dominate metropolitan area growth."

ROCKEFELLER BROTHERS FUND,
New York, N.Y., July 27, 1973.

Dr. and Mrs. ALFRED VAGTS,
Sherman, Conn.

DEAR DR. AND MRS. VAGTS: Thank you for sending to the Rockefeller Brothers Fund a copy of your letter of July 10, 1973 to Congressman Wright Patman.

I understand that the WATER'S EDGE project to which you refer in your letter is being developed by Garden Cities Development Corporation, a non-profit corporation which is a development affiliate of Suburban Action Institute. As I noted in my reply of June 19, 1973 to Mr. Frederick Benedikt, executive secretary of the Candlewood Lake Defense Associates, the only contribution which the Rockefeller Brothers Fund has made to Suburban Action Institute related to its national technical assistance program, toward which the Fund made a grant of $35,000 last August. This grant has been used in connection with litigation involving migrant worker housing in Delray Beach, Florida, and in several other locations throughout the country. The Fund has made no contribution to Garden Cities Development Corporation, nor has one been requested.

I further noted in my letter to Mr. Benedikt that while the Fund was appreciative of being informed about current developments in connection with the WATER'S EDGE project, we regretfully declined an invitation to visit the New Fairfield Town Hall since the project was not one in which we had any direct or significant involvement.

Yours sincerely,

ROBERT W. SCRIVNER.

L

[From the Sherman Sentinel, Apr. 10, 1974]

ON SECOND THOUGHT

(By Natalie Sirkin)

The SENTINEL editorial of March 27—"Know Your Neighbor: The Garden Cities Development Corp."—seems to me quite correct in condemning Gold and Davidoff for their mismanagement of the four garden apartment developments which they have bought, as reported by the *New York Times* of March 24 (Real Estate Section, p. 1).

What the *New York Times* says is true. Indeed, it understates the facts, and omits to draw any conclusions. Other visitors have found numerous faults in the relatively new Lake Katrine apartments in Ulster, New York, including exceedingly poor drainage, broken ventilator covers, shingles coming apart from the buildings. A second published account of this development, in the *Times Herald RECORD* (Orange County, N.Y.) of March 25, adds many new and extraordinary facts. For instance, the package sewage treatment plan "often erupt[s] through the ground and creates a choking stench," according to one tenant (p. 4).

The conclusion from these exposés should be explicitly stated: There is a great gulf between the preaching and the practice of Gold/Davidoff. They speak, even to the TIMES reporter, of wanting to subsidize their own tenants, but they charge rents which are out of the reach of the poor and high for even moderate-income families—$195, $215, and $225 according to the manager, for one- and two-

bedroom units. (These are steep for deteriorating apartments in an unpleasant neighborhood of mixed industrial and residential buildings, the residences including trailer camps.) Despite their oft-repeated goal, there is no "economic integration" here.

And "racial integration?" No. Observers differ only on whether one or no nonwhites have been seen in Lake Katrine. The *Times* reporter says the same is true of the other developments.

"Know Your Neighbor," you say. What are they then? Failed idealists, or suburbanslumlandlords?

If they were "failed idealists," they would recognize that their idea is utopian, incapable of being put into practice; and they would announce the end of their efforts to build a new town in our town and in four others.

But they have not done this. On the contrary, at Lake Katrine—which seems to be typical of the others—they collect rents of about $25,000 monthly but do not pay utility bills. They owe $26,753 for their tenants' heat and light, which includes $3,500 that they tried to pay off previously with a bum check, according to the *Times Herald Record*. They owe $650,000 on the first mortgage covering three of their four garden-apartment developments, and the *Record* reports that foreclosure proceedings are under way.

It appears that they may be siphoning off rents for other (undisclosed) purposes. Is this the "recycling" referred to in their Water's Edge publicity releases that speak of how they will plow their profits from Water's Edge into their other new towns? Isn't this siphoning-off of rents the characteristic of suburbanslumlandlordism?

And in the midst of this news comes the biggest foundation of them all bearing the biggest gift of them all. The Ford Foundation has just announced a $50,000 grant to Suburban Action Institute. I telephoned the Foundation and asked Robert Chandler, who is in charge of the grant, if he had read the *Times* account. It was the fifth day after it had been published. He had not. He said the Ford Foundation had given the grant to SAI, not to GCDC, and the article was about GCDC. He said further that he had read all that elsewhere. When challenged to cite the sources where he had read it, he of course could not, since the *Times* report is (we believe) the first. (And if it is not the first, and if he had read it elsewhere, the grant is all the more inexcusable.)

The pretense by the Ford Foundation that GCDC and SAI are separate organizations exposes the Foundation's lack of objectivity.

M

[From the Times Herald Record, Orange County, N.Y., Mar. 25, 1974]

APARTMENT TENANTS DIFFER ON PAYING UTILITY BILL

KINGSTON.—Lake Katrine Apartments tenants have split ranks on whether to pool their April rent money and pay their landlord's overdue utility bill or risk having Central Hudson Gas and Electric shut off heat and lights.

Garden Cities Development Corp., owner of the 15 2-unit complex, owes the utility $26,753. On March 18, the utility notified tenants that it was cutting off heat and lights this Wednesday because Garden Cities had not paid the bill.

Neil Gold, president of Garden Cities, could not be reached for comment, so it was not known why the utility's bills have not been paid.

However, Sunday's New York Times reported that Garden Cities is having management problems at several apartment complexes in the state, including Lake Katrine. In the article, Gold was quoted as saying that Garden Cities is a non-profit company in which "nobody has a dime of capital.

"We have no investors. We have no stock. We are all here on rather modest salaries. Therefore, what Garden Cities has to work with is the money it gets in. There are times—sometimes for months—when we are cash poor."

The corporation also is the target of a state Supreme Court mortgage foreclosure action.

Friday, 135 Lake Katrine tenants met to discuss the situation. Mrs. Patricia Welch, a spokesman for tenants who want to pay Central Hudson's bill, said

attorney Sherwood Davis told the group that public service law permits the tenants to pay rent money to Central Hudson. Davis, a Town of Ulster justice of the peace, is serving as the unofficial legal adviser to the group.

Mrs. Welch said she knew the tenants legally are not responsible for the bill. "Those of us who want to pay the utility are going ahead," she said. "The rest are willing to take the risk and wait for the courts to act."

She said she would deliver between $4,000 and $7,000 to Central Hudson's Kingston office this morning. She said that amount would almost cover the bill for the last two-month billing period.

According to Clarence Jansen, a utility customer representative, the overdue amount for electric power and natural gas used to heat the apartments is $7,331 Another $3,300 is for a bad check, he said, and the current bill, which the corportation has 30 days to pay, is $6,700. The remaining $10,000, Jansen said, is an unpaid security deposit.

At her apartment Sunday, Mrs. Welch said, "Many of us feel we can't take any chances with the electric and gas being shut off. We have many families with young children and a number of senior citizens."

Asked if she believed Central Hudson would ignore the tenants' need for heat and light, and carry out the shutoff threat, Mrs. Welch replied, "They were very firm."

The Masten Corp. of New York City, which holds a mortgage on the apartments, has filed a foreclosure suit against the owners in State Supreme Court in Ulster County.

Kingston attorney Francis T. Murray said Sunday he expects to be confirmed as the court-appointed receiver in the case today. He said two other apartment complexes are tied into the foreclosure which stems from nonpayment on two mortgages totaling $650,000.

One mortgage covers the Lake Katrine Apartments and the 111-unit Hilton Heights Apartments near Rochester. The second, Murray said, is on the Lancer Court Apartments in Depew, near Buffalo.

Murray said that as receiver he would collect rent money and be responsible for payment of bills accrued from the date of receivership. He said debts contracted for before that date probably would be subject to separate court actions against the owners.

Murray declined to comment on the utility's threat to turn off tenants' lights and heat.

Mrs. Welch and a neighbor, Mrs. Kathleen M. Heisey, said the apartment complex was "steadily deteriorating under present management."

"We have constant sewer and drainage problems here," Mrs. Welch said, "and maintenance is extremely poor." Mrs. Heisey said the management took five weeks to repair a washing machine. Only after persistent complaining were the hallways in her building cleaned, she said.

According to Mrs. Heisey, many tenants have refused to pay their rent because of the poor service. She said the County Health Dept. has been called frequently to force repair of the sewer systems which often erupt through the ground and creates a choking stench. Rentals run from $185 for a one-bedroom apartment to $300 for three-bedrooms.

N

[From the New York Times, Mar. 24, 1974]

ACTIVISTS IN SUBURBS UNDER FIRE AS LANDLORDS

(By Ernest Dickinson)

TARRYTOWN, N.Y.—Neil Gold hopes to reshape America's traditional housing patterns. His dream is to provide an alternative to all-white suburban enclaves of single-family homes.

On the drawing boards he already has plans for more than 15,000 units of housing in five mixed-income, racially integrated communities in New York State, New Jersey and Connecticut. They would cost an estimated half a billion dollars to build.

The vehicle established to fulfill this vision—Garden Cities Development Corporation—has submitted plans for 3,675 townhouses and apartments at Waccabuc Hills, a project that would triple the population of the town of Lewisboro, N.Y., in 10 years. Also on paper are 6,000 housing units at Ramapo Mountain in Mahwah, N.J.; 2,570 at Candlewood Lake in New Fairfield, Conn.; 2,200 at Readington Village in Hunterdon County, N.J., and 850 in Fairfax County, Va.

These projects have stirred considerable controversy, and some are in litigation. But while the debates swirl over Garden Cities' brochures, presentations and claims for the future, the corporation in the last year has been quietly picking up existing garden-apartment complexes. And as an owner it has drawn considerable fire from local officials.

At the development known as Chateau Le Mans on the outskirts of Indianapolis, Mayor Morris Settles of the town of Lawrence said that he had to threaten to shut off water to all 524 units to collect a long-overdue water bill of almost $10,000.

At Lancer Courts in Depew, near Buffalo, the Erie County Water Authority is petitioning in Federal Court to have portions of the rents assigned to cover a back water bill of about $3,000. At Katrine Apartments, just outside Kingston, N.Y., Central Hudson Gas and Electric Corporation has threatened to shut off utilities to collect a bill of about $20,000. There, also, the Ulster County Health Commissioner, Dr. B. J. Dutton, said that his office had received an inordinate number of tenant complaints since Garden Cities took over.

He has been trying since July, he said, to get the company to put in pumps and remedy other violations in its sewage treatment plant. The company has a poor record of maintenance, he said, with many promises but no major improvement.

In Hilton, N.Y., a residential Lake Ontario community west of Rochester, Robert Elliott, the village administrator, said that he had been getting numerous complaints from tenants since Garden Cities bought the 111-unit Hilton Heights apartments.

"They are leaving the place like flies," he said, Things go wrong. You can't get them fixed. Even simple little things."

Garden Cities' problems in Hilton involve management, street dedication and complaints for nonpayment of bills, Mr. Elliott said. "There hasn't been a water or utility bill paid in almost a year, since they have owned it," he said. He said that a lien would be placed on the property "if things aren't straightened out."

Garden Cities Development Corporation occupies a suite in an office building at 150 White Plains Road here in Tarrytown. That suite is also the headquarters for subsidiaries that Mr. Gold has established—Garden Park Realty Company and Garden Park Management Company. He also foresees setting up an engineering company.

Mr. Gold, a man of medium stature who is in his mid-30's, declined in an initial interview to discuss for the record any of Garden Cities' properties, or even to identify them. Later he relented when it developed that there was criticism of the company's management.

He made two principal points. "Garden Cities is a not-for-profit membership company in which nobody has put a dime of capital," he said. "We have no investors. We have no stock. We are all here on rather modest salaries. Therefore, what Garden Cities has to work with is the money that it gets in.

"There are times—sometimes for months—when we are very cash poor. This is so for normal companies operating for profit, but for us it is particularly so. The results is that in those periods we defer payment of bills. But, all the time, our first concern is to upgrade the properties. That is what we have been doing."

Moreover, Mr. Gold said, "it is not as though we bought projects that were viable and they went to hell. We bought projects that were going to hell and we are making them viable. Garden Cities' theory, he said, is to acquire properties with problems and gradually upgrade them.

A native New Yorker who graduated from Columbia University in 1959 and took a master's degree in history, Mr. Gold was relaxed and articulate as he discussed the social theories that led to his present activities.

Early in his career, he said, he reached the conclusion that racial problems in the United States could not be solved before an attack was mounted on the basic problems—the separation of families residentially by race and income.

In 1966, while he was program director of the National Committee Against Discrimination in Housing, he met Paul Davidoff, a Yale Law School graduate who has taught planning and urban affairs at the University of Pennsylvania and Hunter College. "We realized that we had a lot in common and have been close ever since," he said.

Two years later the two created the Suburban Action Institute as a New York State charitable trust to fight exclusionary land use controls. It received foundation grants and is tax exempt.

Garden Cities was organized in 1971 under New Jersey law as a not-for-profit corporation, and while Mr. Davidoff was its board chairman until last September and Suburban Action's offices are on the same floor of the same building as Garden Cities', the two organizations are now totally separate, according to both Mr. Davidoff and Mr. Gold.

The most critical part of the housing crisis, in Mr. Gold's view, is not its shelter aspect. It is the emplacement of homes—where they are located—that determines one's basic outlook on the world, he said.

It is necessary, he maintained, to provide an alternative environment—one less isolating, less antisocial than the present "monuments to American affluence"—the one-class, single-family suburb.

Hence the large, mixed-income planned communities that Garden Cities proposes. Typically they consist of townhouses and garden apartments, with schools, shopping centers, sewage plants, libraries, recreational facilities and a network of pedestrian walkways.

In order to bring in lower income families, Mr. Gold said, Garden Cities has been devising a system of private subsidies for the poor—subsidies completely independent of Federal and state grants. In effect, the corporation would be setting up its own welfare program.

Discussing the specific complaints raised about the quality of Garden Cities' present management, Mr. Gold and the corporation's special counsel, Allen Zerkin, made several observations.

Lake Katrine and Hilton, Mr. Gold said, were "suffering when we bought them." The former he described as a "first-rate rescue job," adding that it would be "one of the most beautiful garden apartments in the region when we finish improving it."

It will take time, he said. Contracts have been let but work cannot start until the ground softens.

About the sewer plant violations at Lake Katrine, Mr. Zerkin contended that the problems were the result of sabotage done in a "very sophisticated way," allegedly by a former employe. "But the sewer plant is running fine now," he said. Taking issue with that statement, the health agency reiterated its charge of improper maintenance.

At Hilton Heights, according to Mr. Gold, Garden Cities must have invested "almost $100,000," including $40,000 worth of trees, a $20,000 pool and $10,000 worth of play equipment. Mr. Elliott, the Hilton administrator, conceded that improvements had been made.

A visitor to Hilton Heights last week observed that many new trees had been planted. But he was informed by one tenant, Mrs. Beverly Wing, that "quite a few people are breaking their lease and moving out."

"One of our windows blew out the other day and we couldn't get the kid who's in charge to replace it," she said. "Finally my husband took a window from the model apartment."

Another tenant, Mrs. Pamela de Baker, said: "These places are falling apart. They're not being kept up. We've lived all over the United States and I've never dealt with a place like this. My husband's company pays our rent and they've held back payment for two months until some things get taken care of."

She complained of water in the basement, leaking windows and a large crack in the bathtub.

A third tenant, however, was milder in her comments. "It's a place to live," said Mrs. Louis Scuderi. "I'm not wild about it but I don't have that much against it either."

According to Mr. Gold, Garden Cities bought Hilton Heights at a low price after being informed that all bills had been paid. "Apparently we were informed incorrectly because a few months ago we were told that the water bill was still outstanding," he said.

Agreeing with Mr. Gold, Mr. Zerkin insisted that Garden Cities had not been bad managers. But there have been times when the inability to pay a bill has made it hard to get work done.

"Everything traces back to the financing," he said, "the fact that we have been 'bootstrapping'—building something from nothing, literally nothing."

In the Lake Katrine purchase, for example, Garden Cities bought 152 units plus adjacent property on which permits for additional construction had already been granted. A wealthy, unidentified partner took a 50 per cent interest in this second, or construction, phase of the deal, Mr. Zerkin said. The partner's signature was sufficient to obtain an institutional loan of approximately $200,000 to help finance the purchase. In addition, the seller provided a $65,000 loan, or purchase money mortgage. The loans covered more than 100 per cent of the purchase price, so that Garden Cities did not have to invest any of its own cash.

Mr. Zerkin said that by personally guaranteeing institutional loans and also by supplying some cash, two wealthy individuals had greatly assisted Garden Cities in its purchases.

Garden Cities is moving toward construction both at Lake Katrine and at Hilton, Mr. Zerkin said. There are also plans to build 135 condominium units in the so-called Rose Garden on the south side of the village of Newark, N.Y., 30 miles east of Rochester.

Although Garden Cities put in none of its own cash at first, Mr. Zerkin said, its object is to "turn the property around" fairly rapidly and syndicate it, and then lease it back from the syndicate. So far this has occurred on one investment, he said—a 132-unit project known as Sherwood Manor on Dodge Street in Rochester.

In that instance, Garden Cities came away with a $200,000 profit after a sale to a syndicate, which consists of Garden Cities as general partner and about a dozen limited partners. Limited partners in such a syndicate are normally high-income investors seeking the benefit of tax shelter.

The profit from that sale has been used in part to support the staff of about 15 or 16 persons in Tarrytown. In addition, the unnamed benefactors have on occasion supplied cash.

"But it's been rough," Mr. Zerkin acknowledged, as he said it would be in any such operation with a social purpose. The procedure of upgrading and then syndicating the properties has been even more difficult than had been anticipated, he said.

"We had to go into the hole at various times," he said. "We've fallen behind, and we've been bailed out."

Most if not all of the properties have a smattering of black tenants, though the Garden Cities officials indicated that no affirmative action program had been adopted to change the racial or economic composition of the developments.

Mr. Gold indicated that he was eager to move forward with the construction project. "We have our staff of accountants and controllers that run our projects," he said. "We are geared up. We are ready to move."

If construction has not yet started, it is not because Garden Cities lacks the means to do it but because it has been blocked by municipal zoning and planning bodies, he said.

"We are not litigating for its own sake," he said, "but where we feel the basic reason for denying Garden Cities the right to build is racial or economic, we intend to litigate and are so doing."

The $200-million Ramano Mountain project is in the courts. So, too, is the 2,570-unit WatersEdge project proposed for Candlewood Lake. Waccabuc Hills is before the Lewisboro Planning Board. Mr. Gold anticipates that a suit will be filed soon in the application for Readington Village in Hunterdon County, N.J.

This leaves only one of the five big planned communities with no procedural hurdles to clear—the 850-unit project in Fairfax County, Va. But there a sewer moratorium blocks construction and may do so for as long as a year.

Asked where the money would come from to finance the half-billion dollars worth of new construction, Mr. Gold said: "What money? It doesn't cost any money to do this that won't be provided by mortgage loans. You don't have to have resources to build houses. You have to have access to people who have resources. Good plans, sound economic analysis and good people willing to wait for their fees until development starts."

Q

[From Patent Trader, May 17, 1973]

SUBURBAN ACTION RESEARCH GRANT HIT

To the Editor:

I am thoroughly dismayed by the announcement appearing in your May 10 issue, that Suburban Action Institute has received federal funding to study feasible "New Town" housing effects and needs in Northern Westchester.

I am dismayed, because any researcher or statistican worth his salt knows that statistics can be slanted in any direction, and are only as objective as the researcher handling and interpreting those figures.

Now, Suburban Action Institute may call itself a non-profit organization, but its officers, Neil Gold and Paul Davidoff, are Directors of Garden City Development Corporation, a limited 6 per cent profit construction firm. In my estimation, 6 per cent profit can be a sizable sum in the pocket of a large scale developer.

At the Suburban Action Institute conference held on January 17 of this year, Mr. Gold stated that only 50 per cent of the stock shares are under the control of this corporation. The other 50 per cent are private investors, whose names he did not divulge, and although he hoped that these investors would plow their profits back into the corporation as Garden City planned to do, he hoped they would realize a handsome profit.

At this same conference, which I attended, the majority of the speakers addressed themselves to the primary task of "breaking the zoning in the suburbs".

What kind of objectivity can be expected from the researchers such as Suburban Action Institute?

Federal funds have been cut in areas of the most vital needs. Why is $38,000 made available for such obvious waste?

LEE V. BLUM,
South Salem.

(No specific area was designated for study by Suburban Action Institute. The Garden City organization proposes to build in New Jersey and Connecticut as well as in N.Y. State.—Editor)

R–I

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT,
Hartford, Conn., December 6, 1972.

MRS. GERALD SIRKIN,
Sherman, Conn.

DEAR MRS. SIRKIN: In answer to your letter to Senator Ribicoff dated October 1, 1972, we offer the following development.

The variables involved in the development of single-family and multi-family housing are too numerous to quote a cost that would be of significance in all situations. However, we are offering a comparison between the costs of a single-family house and the costs of a townhouse unit in a two-story apartment, of approximately equal size and in the same general area.

The house consists of 1,154 square feet of living area including a finished bedroom and half bath on the lower level. Basically, the house has four bedrooms, one and one-half baths, with a one-car built-in garage and is heated electrically.

The townhouse unit consists of 1,350 square feet of living area, four bedrooms, one and one-half baths and a full basement. Heat is forced circulating hot water, oil-fired, centrally located.

The total replacement cost is estimated as follows:

	Single family	Multifamily
Replacement cost of improvements	$17,594	$16,600
Market price of equivalent site	5,500	[1] 2,000
Miscellaneous allowable costs	600	1,800
Marketing expense	1,180	600
Total replacement cost	24,874	21,000

[1] No write down.

Sincerely,

LAWRENCE L. THOMPSON,
Area Director.

R-2

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT,
Hartford, Conn., January 2, 1973.

MRS. GERALD SIRKIN,
Sherman, Conn.

DEAR MRS. SIRKIN: In reference to your letter of December 12, 1972, your conclusion that there is only a slight difference between the cost of construction of a single-family house and of a multifamily dwelling unit is correct. Your assumption about the quality being comparable is also correct.

Discussing land costs, we know that land costs have increased in the past and expect them to continue so in the future. Wherever the land has been down zoned to permit multifamily housing, the land cost rise has automatically followed.

Your conclusions are valid for construction cost except for the Stamford-Ridgefield area which rates a locality adjustment of +16%. However, land prices will vary considerably due to location.

We are pleased to be able to furnish you with this information and hope we have been of help to you.

Sincerely,

LAWRENCE L. THOMPSON,
Area Director.

S

[From the Public Interest, No. 32, Summer 1973]

THE COST OF HOUSING

(By B. Bruce-Briggs)

The cost of land is a tiny part of total housing costs. For example, take the breakdown of monthly cost for a then typical $16,000 home (Table 7) published by the (Kaiser) Commission on Urban Housing in 1968. Merely halving the cost of land would reduce the total cost by one per cent, and would achieve some, but not proportionate, savings in land development costs.

TABLE 7. *Monthly Cost Breakdown for a $16,000 Home (1968)*

Land (2 percent)	$4
Development (5 percent)	9
Construction (17 percent)	29
Interest (29 percent)	50
Taxes (26 percent)	45
Utilities (17 percent)	29
Maintenance and repair (5 percent)	8
Total (100 percent)	174

When someone writes, "X per cent of the public cannot afford a house," and cites the cost of new homes to support his position, he is ignoring the fact that most families buy *used* homes. The readily available data for used homes are less complete than for new houses, but they show the same lack of increase in relative cost.

TABLE 8.—EXISTING HOMES SOLD, 1960-1970 [1]

	With FHA mortgages		With VA mortgages	
	Sales price	Ratio to median family income	Sales price	Ratio to median family income
1960	$13,227	2.36 to 1	$12,238	219. to 1.
1965	15,114	2.18 to 1	16,371	2.35 to 1.
1970	17,842	1.81 to 1	19,500	1.98 to 1.

[1] Statistical Abstract.

T

New Community in Westchester Will Be Environmental Landmark

The Suburban Action Institute announced today that its development affiliate, Garden Cities Development Corporation, will build a landmark new community in Lewisboro, New York, housing 13,800 people from all income and racial groups while meeting the highest standards of environmental and ecological soundness. Lewisboro, located in northeastern Westchester County, is 36 miles from Manhattan.

According to Paul Davidoff and Neil N. Gold, Directors of the Institute and Chairman and President of Garden Cities Development Corp., the new community of Waccubuc will be developed on a 600 acre site lying north and east of Lake Waccabuc. It will consist of 4,600 units of housing in buildings ranging from two to three stories in height. Forty percent of the units will be for families with incomes below $10,000, 20 percent for families earning between $10,000 and $12,000, and 40 percent for families with incomes of $12,000 and above.

"GCDC's aim at Waccabuc is to provide housing for low-income, moderate-income, and middle-income families in the New York City and Westchester areas," Davidoff and Gold explained at a press conference today. "GCDC's aim is also to show that such housing can be planned and built in a way that takes full account of our region's ecological balance, and that works sensitively with the site itself. At Waccabuc, it is the land that has dictated the form and disposition of the buildings it will hold."

Housing will cover only 8.8% of the total site. According to plans prepared by the prestigious firm of Callister, Payne, and Bischoff, working with a team of environmental planners and other consultants, buildings have been "shoehorned" into the restricted open spaces of a rocky and hilly site that has long been thought suitable only for luxury housing on 4-acre tracts.

"In addition," Davidoff and Gold pointed out, "Waccabuc will be not only environmentally sound but a pleasing and rewarding environment to live in. Housing will be clustered into 'neighborhoods' that will each have a unique and individual identity. Some of these neighborhoods will nestle in the hollows on the site, some will be on knolls and hillsides, some have been arranged along streams or around ponds. Each neighborhood is organized around a neighborhood center that will contain basic shopping, day-care, and other facilities. In turn, the neighborhoods will form three 'villages,' each with its own village center. The entire site will be connected by a system of pedestrian walking streets, trails, and service roads. Special attention has been given to the pedestrian network in the belief that most modern suburban development focuses too exclusively on the automobile. At Waccabuc the roads and parking areas will be kept at the periphery of the neighborhood areas. Circulation within the neighborhoods will be pedestrian."

According to Davidoff and Gold, "this site will give each of our small housing clusters real privacy and individuality. For the families who will live here, Waccabuc will be a tremendous step upward in housing standards and quality of life. At the same time, Waccabuc will give them access to the expanding job markets in Westchester County and in Connecticut's Fairfield County."

Davidoff and Gold emphasized that Waccabuc will have little visual or transportation impact on the surrounding community. Housing tucked in hollows and under trees will be invisible from roads. Two hundred seventy acres have been set aside for open space and conservation purposes. The Community's internal parking and street system will be more than adequate for its needs. Waccabuc will have its own commercial areas, parks and playgrounds, schools and daycare centers, library, fire house, and ambulance service.

At the same time, the site was carefully chosen in terms of its ecological and environmental significance. "What is important about sites like this one," Davidoff and Gold explained, "is that it is not unique enough in its natural attributes or composition to be declared inviolable parkland. But it is attractive land that can absorb careful development while removing development pressure from other lands that are more valuable to society for agriculture, forestry, and wildlife production."

Davidoff and Gold stressed the landmark aspects of Waccabuc as a development that will preserve environmental standards while meeting an increasingly severe shortage of housing for those in our society who happen not to be rich.

"According to the Westchester County Planning Commission, the County needs more than 100,000 new housing units by 1980. Four thousand units were started in 1971. In the first eight months of 1972, housing starts dropped even further, to a total of 2,000 units. The County's housing production is way down from the 6,000 units per year that were started in the 1960's. And that takes account of Westchester only, not of the conditions that apply in New York City. This is a housing emergency of the first magnitude. Projects like Waccabuc will at least go a short distance toward meeting Westchester's estimate of its own needs."

Gold and Davidoff explained that the basis of planning for Waccabuc was a Preliminary Natural Resources Survey that was completed in October 1972. It includes careful studies of the site's regional context, vegetation, geology, soils, slopes, wildlife, habitat, water drainage, climatic conditions, and visual qualities. On the basis of the Natural Resources Survey, the planners have determined to preserve the agricultural open land on and around the site. Gold and Davidoff pointed out that conventional development practices favor the placing of houses on flat agricultural land because this cuts the builder's costs. "What we have tried to achieve is a community that will keep housing prices down while not allowing cost to dominate our attitude toward the landscape. Flat, open areas at Waccabuc are going to be carefully preserved and in some cases, where they are poorly drained, are going to be improved. Our purpose in doing this is both to give Waccabuc's residents a sense of spaciousness, and to create visual 'buffer zones' that will minimize the impact of the new community on the surrounding area."

Davidoff and Gold emphasized that Waccabuc will be removed from the main population centers in this part of Westchester County, and that the community will have no dramatic effect on the existing towns of the area. "What it is going to do is to make it possible for families that are not rich to live in a developing area that can offer them both the housing and the employment they desperately need. In 1969, the median income in Lewisboro was $16,400, higher than the median income for all of Westchester County. According to the U.S. Census for 1970, about 1.4% of Lewisboro residents are non-white. In the same year, 88.5% of Lewisboro's housing units consisted of one-family homes selling for an average of $50,000. This represents a very lopsided income and racial structure that Waccabuc will go some distance toward balancing."

Waccabuc represents the third major development that the Suburban Action Institute and Garden Cities Development Corporation have undertaken in the New York-New Jersey area. In August 1971, SAI announced plans to build a 2,000 unit planned community in Readington, New Jersey. In April 1972, GCDC unveiled plans for a 6,000 unit planned community in Mahwah, New Jersey. Like Waccabuc, these developments are designed to serve all income and racial groups.

The Suburban Action Institute is a nonprofit organization for research and action in the suburbs. It was established to focus public attention on the role of the suburbs in solving metropolitan problems of race and poverty. Garden Cities Development Corp., the Institute's nonprofit development affiliate, is undertaking the actual building of new communities in suburban areas that offer expanding job and income opportunities to the families now trapped in America's declining center cities. It is a basic conviction of SAI and of its affiliates GCDC that the cities will be able to bring their own rehabilitation only when they have been relieved of the pressure of chronic unemployment and underemployment.

PROJECT STATISTICS

Total acreage: 660.25.
Total units 4,600=±7 units per acre.
Total population: 13,800 @ 8 per D/U.
Ground coverage (percent):

Housing (2,520,000 sq. ft.)	8.8
Parking and streets (2,710,000 sq. ft.)	10.6
Walks and recreation (650,000 sq. ft.)	2.1
Total coverage	21.5

Ground use (percent):	
Residential, parking and immediate grounds (290 acres)	43.6
Parks and playgrounds (60 acres)	9.3
Open space and conservation (270 acres)	41.0
Commercial (15 acres)	2.3
Educational (15 acres)	2.3
Community facilities (10 acres)	1.5
Total (660 acres)	100.0
Housing by type (D/U):	
Single level units in 3-story buildings	1,200
Single level units in 2-story buildings	1,500
Multiple level units in 3-story buildings	400
Multiple level units in 2-story buildings	1,400
Elevator buildings	100
Total	4,600
Housing by size:	
1 bedroom	1,400
2 bedrooms	1,600
3 bedrooms	1,200
4 bedrooms	400
Total	4,600
Commercial space (square feet)	250,000
Community space (square feet):	
Recreation and miscellaneous community	70,000
Library (2)	5,000
Firehouse (4 trucks)	3,000
Ambulance service (2 vehicles)	1,000
Boathouse	2,000
Pools—Dressing, etc	3,000
Total	84,000
Schools (square feet):	
Daycare 500 children: 10 centers, each 1,600 square feet	16,000
Elementary schools, 1,440 children:	
2 schools, each 360 children, 20,000 square feet each	40,000
1 school, each 720 children	40,000
Total	96,000

U

[From the Yorktowner, Aug. 8, 1973]

AN EGG FACIAL FOR THE GOVERNOR

The problem was that though it was an environmental plan, it didn't seem to be doing anything for the environment

(By Natalie Sirkin)

The problem was that though it was an environmental plan, it didn't seem to be doing anything for the environment.

Such was the position of most of the speakers at the hearing, on July 12 in New York City, on the "Preliminary Edition" of the Environmental Plan for New York State. Two gentlemen representing New York State's Department of Environmental Conservation listened politely.

To the speakers it seemed that the Plan consisted entirely of pious vaporizing about environmental ailments and the need to do something about them, but that the concrete proposals for policy were omitted. The point which the speakers missed was that they were dealing, not with foggy planning, but with planned fog. The policies which the Department of Environmental Conservation had in mind are only lightly glossed over because to make them more explicit would produce an explosion of opposition.

At the center of the Plan, garnished with pretty statements about preserving environmental quality, is an objective which conflicts with those pretty statements. The chapter is blandly entitled "Land." It is yet another attack on local control of zoning, yet another attempt to cram cluster developments, planned unit developments, and new towns down the throats of the suburban and rural areas.

It must be obvious to the planners that cluster development and PUD's are devices for accelerating the disintegration of New York City and speeding the scattering of the population. It must be obvious to the planners that, far from preserving open space, these devices will only accelerate the rate at which developers will devour open space. It must be obvious to the planners that, though they deplore the "extremes of concentration and scatteration," by reducing the concentration of population in New York City and removing it into their new towns, their plans for lowering New York City's concentration will create more of all the environmental destruction which their Plan is supposed to be combatting—more commuting, more consumption of gas, more production of fumes, more damage to water resources, more highways, more sewers. Indeed, here and there they explicitly favor more highways and more sewers in partly-developed areas. Their reason is that putting in the highways and sewers first will lower the costs of putting them in later. In fact, it will increase costs, by encouraging high-density development which otherwise might not occur in those areas.

Several speakers pointed out these consequences, while expressing their bewilderment at finding them in a plan for environmental—"conservation." One speaker pointed out that "new towns" rapidly become "spread cities," that the filling in of the green space between those new cities cannot be prevented, and that the new cities are, therefore, just one more booster for space consumption. Mr. Robert Rickles, newly resigned chief of New York City's environment department, assailed the plan for its failure to propose specific policies to hold the existing cities together, to improve the environment of the cities, and thus to help preserve the environment of the countryside.

What these far-sighted commentators failed to grasp is that the failings of the Plan represent, not the weakness of the planners, but the strength of the Politican—Developer Complex. The Complex is at its old game of attacking home rule—but with more subtlety than other states have shown, or than has been shown in the past in New York State.

Compare the smoothness of New York with the crudeness of Connecticut. In Connecticut, the developing governor gave the task of overriding local zoning to a "Governor's Task Force on Housing" composed by his order only of persons "with a proven record and interest" in housing—and that is what he got—developers, realtors, bankers, and other associates of the construction industry and friendly civil rights activities.

"There has already been too much discussion," the Governor told them on September 7, 1971. "The issue . . . is not how great the need is, but what are we willing and able to do about it. In short, what is our commitment to housing?"

It was like asking drug addicts to commit themselves to drugs. Obligingly, the Task Force—or the "Trash Force," as some of its critics call it—wrote a still semi-secret "Interim Report" calling for state-overriding of local zoning regulations to allow cluster developments and PUD's in every municipality, with a host of subsidies for themselves and the other "sponsors" who would be profiting from this arrangement.

Their efforts have been slowed by an outcry of the enraged citizenry and candidates for political office in the last election. Their final "Report" calls for the clusters and PUD's to be "voluntarily" accepted into the local zoning regulations, except that if the planning and zoning commissioners do not "volunteer," then it must be recognized that the only way to meet housing needs is through "firmer measures." Meanwhile, as in Westchester County, the so-called "housing needs" are well below the national average, amounting to only 3.9 percent of all year-round housing (being substandard or overcrowded). (In Westchester, the figure is about 3.1 percent.) There is no justification for the planned massive statewide down-zoning.

Compare the smoothness of New York's elegant Department of Environmental Conservation with the crudeness of New York's arrogant Urban Development Corporation. The UDC claimed a compelling need for 92,000 new housing units in Westchester County by 1980. The figure was overstated by precisely fifty percent. Half of it was for immigrants expected to move into Westchester who would not come at all if all that new housing were not built. In fact, though required by law to make a "finding" of chronic unemployment and substandard housing in a community before overriding the local zoning of that community to build apartments there, the UDC apparently made no such findings but selected nine Westchester towns as its target-subjects, all of them—as it would seem—poor cases for putting apartments in non-urban acreas where the housing need and the employment opportunities were the smallest.

Now, in this latest attack, the Politican-Developer Complex is trying to slip past the defenders of home-rule disguised as that beloved figure, the good environmentalist.

We can safely predict.

No matter how fuzzy and subtle the initial pronouncements the effect of the Plan must eventually become known. The suburban and rural public will rise up in opposition. The experiences of the popular protest culminating in the defeat of the Urban Development Corporation, of the Rye-Oyster Bay Bridge, of the Hudson River highway, will be repealed. The Governor will be forced to retreat, with egg on his face.

Couldn't we save all that time, trouble, and eggs for the Governor's face, by advising Albany now that we have already caught on and the game is up?

V

[From the Yorktowner, Jan. 16, 1974]

LETTERS TO THE EDITORS

OPEN LETTER TO COMMISSION ON CRITICAL CHOICES FOR AMERICA

This letter has been sent to all members of Governor's Commission on Critical Choices for America

We take the liberty of addressing you in the belief that the issue of home rule is certain to be raised in your Commission. On this issue, we believe that your Commission is a "stacked deck." It were better that you were not associated with it at all. As you are, we respectfully request that you do your best to see that the cards be dealt out as honestly as you can effectuate it.

Recent efforts make us fear that one purpose of your Commission is to propagandize on the so-called "problem of land-use." The objective of this propaganda has been to take the authority to zone out of the control of the municipalities, where by law and custom in most states it resides, and to assist developers to force the municipalities to down-zone in order to allow the construction of huge new developments, particularly in the suburbs and rural areas.

It is axiomatic that government governs best which is the most responsive to the needs of the people. It is local government which is best in a position to appreciate those needs, and therefore local government which is best in a position to respond to them the most adequately. Therefore, good government requires that all those functions which can reasonably be reserved to local government, should be. Such functions include zoning and planning.

Local government's power to zone and plan is now under assault by the enemies of home rule. The assault is not a response to failure of local governments to protect their environment. (This fact may be inferred from the evidence that these attacks are designed to lower local standards, not to raise them.) Rather, the attacks are a response to a powerful stimulus—the strong, sweet smell of easy money. Developers can make immense profits by successfully forcing down-zoning. In this fertile field there has grown up an alliance of developers and politicians and financial institutions who can do much for each other.

We see your Commission as but the most recent and prestigious of a series, which began slowly.

(a) In 1969, two guys and a mimeograph machine organized their Suburban Action Institute. Its attack upon zoning now threatens zoning in the entire State of New Jersey and is making progress in Connecticut. They have recently gone

into the development business and their wholly owned development affiliate, Garden Cities Development Corporation, proposes to put new cities in the midst of old towns in Connecticut, New Jersey, and New York.

(b) New York State, at the Governor's request, set up the Urban Development Corporation, which propounded a plan to override local zoning in Westchester County (The Yorktowner, April 11, 1973, pages 16–17). UDC's power to override has since been curtailed by the State legislature. It seems to us significant that the first speaker at your first meeting was Edward J. Logue, head of UDC.

(c) Regional Plan Association put on a TV series called "Choices for '76," which aims to replace local with tri-state regional zoning. (Letters to editor, New York Times, May 22, June 27, 1973.) There is information that this series will be repeated.

(d) New York State's Department of Environmental Conservation produced a preliminary edition of a Statewide Environmental Plan which, in a chapter benignly entitled "Land," calls for removal of zoning from municipalities in order to permit construction of Puds (planned unit developments), new towns, and cluster developments, and urges as facts matters which are in dispute, including the "economy" from building highways and sewers in anticipation of development, and the economic and environmental "superiority" of cluster developments over single-family houses. (The Yorktowner, August 8, 1973). Your own Executive Director headed up the Statewide Environmental Plan and the Department.

(e) At the federal level, the Citizen's Advisory Committee on Environmental Quality, under Laurence S. Rockefeller, has issued a report asking for "state zoning with federal support" (New York Times, editorial, June 3, 1973, Section E, page 16). It is believed that this report proposes taking land by eminent domain upon the death of the land-owner where it is in the State's interest.

(f) Governor Rockefeller's "Temporary State Commission on the Powers of Local Government" has issued its report, "Strengthening Local Government in New York", which proposes weakening local government in so fas as zoning and planning are concerned. (New York Times, "State Study Urges Curb on Zoning," June 15, 1973, page 39.)

The Rockefeller brothers have given much money and time to these efforts. The Rockefeller Brothers Fund financed "e" above. It contributed $50,000 to "Choice for '76" (c) and $35,000 to Suburban Action Institute (a) in 1973 alone. The Department of Housing and Urban Development of the U.S. Government gave $800,000 to "Choices for '76" and has given many hundreds of thousands to similar "social engineering" projects, including, perhaps, your own Commission. Another U.S. Government agency, the National Endowment for the Arts, chaired by another of your members, Nancy Hanks, announced a $38,000 grant for Suburban Action Institute to study "the effect of breaking zoning in the suburbs," the practice of which that organization (a) is continuously and successfully pursuing (Patent Trader, May 17, 1973). SAI's income in 1972 was $350,000, according to Dun & Bradstreet, most of which probably was from grants from tax-exempt 501(c)(3) foundations.

Three members of SAI attended a conference of parties interested in destroying local zoning, along with representatives of the National Association of Home Builders, the Rockefeller Brothers Fund (Portia A. Smith), and some other anti-home-rule authorities. (See Potomac Institute, 1501 Eighteenth Street, N.W. Washington, D.C. 20036, "Controlling Urban Growth—But for Whom?", 1973, especially pages 1, 2, 33) No doubt there are similar activities and grants which can easily be identified by anyone with the time to track them down.

We ask that you acquaint yourselves with all the arguments, on this and other controversial questions which will come before you, and that you make an effort to see that the views of the critics of some of your members be heard. In proportion as your mission on "land" is successful, the lives of all Americans are likely to be altered, but not for the better.

If you give them a chance, the critics can point out that (a) the destruction of local zoning will not produce low-cost housing, and (b) therefore will not help the underhoused poor, but (c) will contribute to the disintegration of the cities, and (d) the destruction of the countryside, with (e) the proliferation of highways and additional automobile traffic. (f) However much these efforts will assist the special interest group of the developers, they are unlikely to assist the general welfare.

Mrs. Gerald Sirkin,
Citizens United for Home Rule.

W

APRIL 22, 1974.

Re Panel 6—Quality of Life of Individuals and Communities.

Mr. HENRY L. DIAMOND,
Executive director,
Commission on Critical Choices for Americans,
New York, N.Y.

DEAR MR. DIAMOND: Thank you for your letter of the 8th, giving me the information which I had requested, to wit, the names of the members of this Panel, and the news that this panel will be considering the question of zoning and other forms of "land-use."

It is apparently your approach to submit "critical questions" to your panels. Kindly send me the list of "critical questions" which have been or will be put to this Panel.

It is well-known that you, and three or more of the members of this Panel, take a strong view of the utility of *overriding* local control of zoning, while none of the members of this Panel (or of your Commission) is known to be equally committed to the opposite view, the view of the people, the view that that government is best which recognizes the need for preserving home-rule in zoning and other forms of "land-use planning." However, you are organized under the section of the Internal Revenue Code which requires that you present *all views*, of all the subjects which you choose to survey. Kindly advise, therefore, what plans or steps, precisely, you have made or taken, to present all views to this panel on home-rule in zoning, including the view that down-zoning does not lower the cost of housing and may raise it.

Yours sincerely,

Mrs. G. SIRKIN.

P.S.—The news release which you enclosed at my request states that a list of the members of your entire Commission is "attached." That list was not attached to my copy. Inasmuch as there have been changes since the list first announced, kindly send me an up-to-date list. May I again thank you for your expressed willingness to put my name on your mailing list. I hope that in the future I will get your news releases automatically. The last one I received was that of March 18, enclosed in your last letter.

X-1—TACONIC FOUNDATION, INC., 1971

[Itemized statement of corporate stocks held at close of taxable year]

Issue	Number of shares	Cost
American Telephone & Telegraph Co	4,000	$198,174
Crown Zellerbach Corp	3,000	112,392
Delta Airlines	2,000	99,855
Ethyl Corp	6,000	162,395
Goodyear Tire & Rubber Co	4,500	155,191
Guardian Mortgage Investors	3,000	129,175
International Business Machines	500	147,181
International Telephone & Telegraph	3,000	193,894
Lomas & Nettleton Financial	6,000	115,500
Masco Corp	4,000	101,936
Russell Stover Candies	4,500	154,625
Sony Corp	6,250	149,771
Southern Co	8,000	204,622
Standard Oil of New Jersey	2,200	137,296
Trane & Co	2,500	164,266
Tropicanna Products	2,600	106,791
Zale Corp	4,000	162,072
Fairfield Communities Land Co	26,515	37,500
Inforex	2,000	25,000
Land Resources Corp	6,591	23,071
Leisure Group, Inc	3,500	94,180
Module Communities	1,000	50,151
National Student Marketing	4,000	56,660
Open Road International	3,000	24,000
U.E.C.	[1] 4,137,500	75,041
Total		2,880,739
Less: Reserve for unrealized losses		398,897
Total		2,481,842

[1] Preferred.

X-2—TACONIC FOUNDATION, INC., 1971

[Itemized statements of other investments

Program related investments:	
Cooperative Assistance Fund	$159,000
Baltimore Community Investment Co	5,000
Union Settlement Federal Credit Union	2,500
Total	157,500
Investment in Canterbury Institutional Associates, an investment limited partnership, at book value before unrealized gains	2,798,853
Total	2,955,458

SECURITIES HELD BY CANTERBURY INSTITUTIONAL ASSOCIATES

	Number of shares	Cost	Market value ' at Dec. 31, 1971	
Amerada Hess Corp	2,300	95,000	96,025	
Braniff Airways	20,600	239,818	327,025	
Braniff Airways special cv. class "A"	20,600	247,131	321,875	
Champion Homebuilders Co	17,000	540,456	726,750	
Community Psychiatric Centers	10,000	215,000	187,500	
Crum & Forster	18,000	337,500	567,000	
Eastern Airlines	20,000	378,188	452,500	
Felsway Corp	10,000	247,314	238,750	
Gordon Jewelry Corp. Class "A"	10,000	199,805	276,250	
Guerdon Industries, Inc	20,000	570,471	582,500	
Imperial Oil, Ltd	25,000	736,415	718,250	
I.N.A. Corp	10,000	479,029	490,000	
N.N. Corp	15,000	648,750	618,750	
Petrolane Inc	12,000	571,704	678,000	
Ralston Purina Co	12,500	439,135	442,188	
Trans World Airlines	20,000	650,492	820,000	
Zale Corp	10,700	422,249	446,725	
Hallcraft Homes, Inc. CV s/d 5.75 percent	200,000	223,319	150,000	
National General Corp. 4 percent Cv s/d	700,000	419,369	423,500	
Subtotal		7,661,145	8,626,588	
Taconic Foundation's share of Canterbury Institutional Associates' net worth of $11,622,250, at market value at Dec. 31, 1971				2,999,850

Appendix B

Supplemental information supplied by various witnesses

THE MYRON STRATTON HOME,
Colorado Springs, Colo., June 14, 1974.

Hon. VANCE HARTKE,
U.S. Senate, Senate Office Building,
Washington, D.C.

MY DEAR SENATOR HARTKE: This will acknowledge receipt of your letter of May 28, 1974.

The Myron Stratton Home is operated solely on the income generated by its endowment. Mr. Stratton directed in his Will that no charges were ever to be made for the care of the residents taken into the Home. We do not receive any other income from other sources, nor do we receive any assistance from the Federal, State or local governments.

Since the Home was founded in 1909, we have received a few small bequests, the majority of them being in the nature of a few hundred dollars each left to us by deceased residents, although no resident is required to leave his property to the Home upon death. In this 65 year period, the total amount received has been in the neighborhood of $45,000.00.

You will remember that during my testimony before your sub-committee, we engaged in a discussion concerning the possible subsidization of homes such as The Myron Stratton Home by the taxpayers of this country. You will recall that I suggested to you that The Myron Stratton Home, if it were to be considered a profit corporation and permitted to deduct expenses incurred in the care of its residents, would rarely pay any corporate income tax. You advised me at that time that you would like to see further information concerning this statement. As a result, I enclose herewith a schedule using the homes that were listed on the summary attached to my statement to the Subcommittee on Foundations and showing the Federal corporate income tax that would be payable by them if they were not exempt organizations.

The figures shown on this schedule are the same as those shown on the summary except for the investment income of the Moor Children's Home in El Paso, Texas. I have rechecked the figures shown on the orginal summary with this home and found that the figures shown on the summary constitute gross investment income, and because of ownership of real estate, the difference between the net income and the gross income was substantial. I have, therefore, used in the enclosed computation the actual net investment income of this home for the year involved.

I should also point out to you that the figures shown on the summary attached to my statement to the Sub-committee on Foundations and also on the enclosed schedule do not necessarily reflect the same year for the operations of each of these homes, as the information concerning these homes was accumulated through the efforts of Senator Allott and American Association of Homes for the Aging during the period 1971, 1972 and 1973. Nevertheless, I feel that the figures shown on the schedule give a fair test of the subsidy question.

From an examination of the enclosed schedule, it becomes quite apparent that not only is the American taxpayer not subsidizing these homes, but that the reverse is true. You will note that if these homes had been subject to Federal corporate income tax, they would have paid a total sum of $51,042.00, but by reason of being exempt from Federal income taxes but subject to the excise tax on private foundations, these homes instead paid $198,684.00 in excise taxes. In addition, all but eight of the homes were founded prior to 1913, so that their founders received no Federal income, estate or gift tax benefits as a result of their initial endowment. I also feel that we should remember Senator Dominick's observation that if these homes were not in existence, the American taxpayer would have the burden of the care of their residents.

I appreciated being afforded the opportunity to testify before the Sub-committee on Foundations, and I hope the enclosed schedule will be of some use to you in your investigation of the problems of foundations.

Very truly yours,—

KARL R. ROSS.

Enclosure.

35-686—74——25

Name and address of organization	Date founded	Investment income	Revenue from residents	Operating expenses	Excess of income over operating expenses	Federal corporation income tax	4 percent excise tax
1. Hendrick Home for Children, Abilene, Tex	1939	$416,177		$385,797	$30,380	$6,900	$16,647
2. Home for Homeless Women, Wilkes-Barre, Pa	1893	96,800	$6,006	102,500	(5,100)		3,872
3. Judson Palmer Home, Findlay, Ohio	1950	150,000		135,000	15,000	3,300	6,000
4. Myron Stratton Home, Colorado Springs, Colo	1909	438,628		475,232	(36,604)		17,345
5. Aged Woman's Home of Georgetown, Washington, D.C	1868	14,000		18,000	(4,000)		560
6. Heritage, San Francisco, Calif	1850	296,025	350,000	670,000	(23,975)		11,841
7. Warner Home, Jamestown, N.Y	1911	36,063	27,444	69,000	(5,493)		1,442
8. Elizabeth Shoemaker Home, Washington, D.C	1952	66,757	25,271	97,810	(5,782)		2,670
9. Smith Memorial Home, New London, Conn	1881	61,987	16,033	116,202	(38,182)		2,480
10. Guyer Memorial Home, Peoria, Ill	1889	32,054	15,132	87,665	(40,479)		1,282
11. Sand Springs Home, Oklahoma City, Okla	1908	541,753		597,000	(55,247)		21,670
12. Miriam Osborn Home, Rye, N.Y	1908						
13. James Sutton Home, Wilkes-Barre, Pa	1920	32,000	20,000	52,000			1,280
14. Widows and Old Men's Home, Cincinnati, Ohio	1848	700,000	100,000	850,000	(50,000)		28,000
15. Amaza Stone House, Cleveland, Ohio	1877						
16. Lisner Home, Washington, D.C	1941						
17. Society for the Relief of Destitute Orphan Boys, New Orleans, La	1820	134,385	3,431	110,546	27,270	6,090	5,375
18. State Street Children's Home, New Orleans, La	1866	39,500	2,322	55,650	(14,828)		1,580
19. Moor Children's Home, El Paso, Tex	1959	539,850	11,000	460,428	90,422	22,509	21,594
20. Andrew Freedman Home, Bronx, N.Y	1924	293,000	203,000	697,000	(201,000)		11,720
21. Rogerson House, Boston, Mass	1860	236,884	80,122	316,826	180	40	9,475
22. Marcus L. Ward Home, Maplewood, N.J	1921	413,377	204,613	741,962	(123,792)		16,535
23. Cartwell Home, Palestine, Tex	1953	164,232	90,397	213,880	40,749	9,595	6,569
24. Wales Home, Brockton, Mass	1893	55,722	20,565	84,789	8,502	1,870	2,229
25. St. Lukes Episcopal Church Home, Highland Park, Mich	1861	207,956	196,886	401,474	3,348	737	8,318
Total						51,042	198,684

AMERICAN ASSOCIATION OF MUSEUMS,
Washington, D.C., May 29, 1974.

Hon. VANCE HARTKE,
Chairman, Subcommittee on Foundations, U.S. Senate, Committee on Commerce, Washington, D.C.

DEAR SENATOR HARTKE: I had wanted to respond earlier with this interim report on the additional information you requested during my testimony before your Subcommittee on Foundations, May 13, 1974. Specifically, I am enclosing a list of museums classified as private foundations (private operating foundations for purposes of this testimony). Along with the amounts of the 4% excise tax they paid in 1972, this information was obtained from the public records available at the Internal Revenue Service and to the best of my knowledge is inclusive.

I have written each of these institutions asking them to provide specific information about the amounts of grant support they receive in the year prior to the Tax Reform Act of 1969 and the most recent year (FY 1973). This was done in order that a comparison might be made to determine the extent of impact on foundation grants from the increased filing requirements applied to private operating foundation museums set forth in the Tax Reform Act of 1969. This additional information I will send to you by June 17, 1974, in accordance with your letter of May 28, 1974.

Again, my deep appreciation for the opportunity to appear before your committee and bring to your attention the burden on museums classified as private foundations.

Sincerely.

KYRAN M. MCGRATH,
Director.

Enclosures.

Museums classified by IRS as private foundations

Name of museum	*4-percent excise tax paid for 1973*
San Francisco Aquarium Society, Inc., Golden Gate Park, San Francisco, CA 94118	$149.00
Pajaro Valley Historical Association, P.O. Box 960, Watsonville, CA 95076	30.00
Butte County Pioneer Memorial, % Irene Parker, P.O. Box 309, Oroville, CA 95965	80.00
Briggs-Cunningham Automotive Museum, 747 E. Green Street, Pasadena, CA 91101	19.00
American Air Museum Society, 616 Canal Street, San Rafael, CA 94901	(2)
The J. Paul Getty Museum, 17985 Pacific Coast Highway, Malibu, CA 90265	97,279.00
Norton Simon Inc. Museum of Art, 3440 Wilshire Boulevard, Suite 1216, Los Angeles, CA 90010	10,164.00
Western Museum of Mining and Industry, P.O. Box 387, Colorado Springs, CO 80901	14.95
Automotive Museum, Inc., % W. S. Brown Agent, P.O. Box 18, Berlin, CT 06037	(2)
The Litchfield Nature Center and Museum, Inc., Litchfield, CT 06759	(2)
Torrington Historical Society, % Colonial Bank and Trust Co., P.O. Box 148, Torrington, CT 06790	96.00
Hagley Museum, Eleutherian Mills-Hagley Foundation, Wilmington, DE 19735	$126,411.00
Delaware Museum of Natural History, P.O. Box 3937, Greenville, De 19807	1,496.00
The Henry Francis DuPont Winterthur Museum, Inc., Winterthur, DE 19735	[1] 113,174.00
The Phillips Collection, 1600 21st Street, NW., Washington, D.C. 20007	18,000.42
The De Ette Holden Cummer Museum Foundation, 829 Riverside Drive, Jacksonville, FL 32204	6,752.18
Marie-Selby Botanical Gardens, c/o Palmer First National Bank & Trust Co., P.O. Box 2018, Sarasota, FL 33578	4,159.00
Ships of the Sea, Inc., 501 East River Street, Savannah, GA 31401	3,475.00

See footnotes at end of table, p. 383.

Kauai Library and Museum Association LTD, Lihue Kauai, HI 96766	22.00
Morton Arboretum, 110 North Wacker Drive, Chicago, IL 60606	51,402.00
Harry & Della Burpee Art Gallery, 737 N. Main Street, Rockford, IL 61103	37.00
Prime Mover Control Museum Association, P.O. Box 2131, 4989 N. 2nd Street, Loves Park, IL 61111	0
George F. Harding Museum, 86 E. Randolph Street, Chicago, IL 60601	(2)
Treaty-Line Museum, Inc., Rural Route 4, Liberty, IN 47353	260.32
Rush County Historical Society, c/o Priscilla Winkler, RR No. 5, Rushville, IN 46173	1,528.00
Historic New Orleans Collection, 533 Royal Street, New Orleans, LA 70130	17,170.00
The Zigler Museum Foundation, P.O. Box 986, Jennings, LA 70546	789.54
Old Gaol Museum, c/o York Historical Society, York, ME 03909	946.13
Fruitlands Museums Inc., Prospect Hill, Boston, MA 01451	167.00
Isabella Stewart Gardner Museum in the Fenway Inc., 225 Franklin Street, Suite 800, Boston, MA 02180	27,653.00
The Kendall Whaling Museum Trust, c/o Hale & Dorr, 28 State Street, Boston, MA 02110	2,749.00
Merrimack Valley Textile Museum, Inc., Massachusetts Avenue, North Andover, MA 01845	3,978.00
Thayer Museum Inc., 314 Main Street, Lancaster, MA 01623	10.59
Manchester Historical Society, 14 Union Street, Manchester, MA 01944	605.42
Cape Cod Museum of History and Art, South Main Street, Centerville, MA 02632	99.75
Western Hampden Historical Society, Westfield, MA 01085	38.31
Haverhill Historical Society, 240 Water Street, Haverhill, MA 01830	302.83
Cambridge Historical Society, 159 Brattle Street, Cambridge, MA 07138	315.76
Sterling & Francine Clark Art Institute, Williamstown, MA 01267	58,832.44
Somerville Historical Society, Westward Boulevard and Central Street, Somerville, MA 02143	38,91
Blandford Historical Society, Main Street, Blandford, MA 01008	46.77
Heritage Plantation of Sandwich, Grove Street, Sandwich, MA 02563	251.00
N. Andover Historical Society, 153 Academy Road, N. Andover, MA 01845	325.43
Lynn Historical Society, 125 Green Street, Lynn, MA 01902	1,033.00
Fall River Historical Society, 451 Rock Street, Fall River, MA 02720	900.00
Leonard Boyd Chapman Wildbird Sanctuary, Suite 4500 Prudential, Boston, MA 02199	363.00
Stockman Historical Society, % Clark A. Richardson, 3 Barrett Avenue, Stoneham, MA 02180	35.64
Historical Society of Old Yarmouth, Yarmouthport, MA 02675	119.95
Historical Building, 19 Grove Street, Petersborough, NH 03458	176.34
Manchester Historic Association, 129 Amherst Street, Manchester, NH 03104	579.00
Alpena Museum Association, % Jessee Besser Museum, 491 Johnston Street, Alpena, MI 49707	4,992.94
Woodstock Museum, 747 Chillicothe Road, Amora, OH 44202	133.00
Dawes Arboretum, RR No. 5, Newark, OH 43055	14,242.00
Sauder Museum, Inc., % Mrs. Erie J. Sauder, 502 Middle Street, Archbold, OH 43502	3.00
Campbell Museum, Campbell Place, Camden, NJ 08101	(2)
Henry L. Ferguson Museum, Fishers Island, NY 14453	86.00
Hill-Stead Museum, % Manufacturers Hanover Trust Co., 650 Park Avenue, New York, NY 10022	172.00
Millicent A. Rogers Memorial, Museum, Inc., % Jerome W. Sinsheimer, 660 Madison Avenue, New York, NY 10021	16.80
Trotting Horse Museum, Inc., 240 Main Street, Goshen, NY 10924	40.23
Corning Museum of Glass, % Corning Glass Works, Corning, NY 14830	(2)

See footnotes at end of table, p. 383.

Sleepy Hollow Restoration, P.O. Box 245, Tarrytown, NY 10591	$38, 330. 00
Long Island Historical Society, 128 Pierrepont Street, Brooklyn, NY 11101	1, 033. 00
American Museum of Immigration, Liberty Island, New York NY 10004	221. 00
Genesee Country Museum, 445 St. Paul Street, Rochester, NY 14605	138. 00
Rochester Historical Society, % Security Trust Co., 1 East Avenue, Rochester, NY 14638	534. 00
Dutchess County Historical Society, P.O. Box 88, Poughkeepsie, NY 12601	364. 00
Johnstown Historical Society, 17 N. William Street, Johnston, NY 12095	54. 00
Alice T. Miner Colonial Collection, Chazy, NY 12921	810
Storm King Art Center, Mountainville, NY 10953	2. 634. 00
Adirondack Museum, Blue Mountain Lake, NY 12812	--
Bucks County Historical Society, Pine & Ashlands Streets, Doylestown, PA 18901	2, 400. 00
John J. Tyler Arboretum, % Providence National Bank, 1632 Chestnut Street, Philadelphia, PA 19103	157. 00
Taylor Memorial Arboretum, Girard Trust Bank, Philadelphia, PA 19101	306. 00
Barnes Foundation, Merion, PA 19066	[2]
Colonial Flying Corps Museum, Inc., 1200 Packard Building, Philadelphia, PA 19102	3. 00
Merrick Free Art Gallery and Museum and Library E.D. Merrick, % Union National Bank, New Brighton, PA 15066	673. 00
Heard Natural Science Museum and Wildlife Sanctuary, Route 2, McKinney, TX 75069	1, 828. 00
Widner Memorial Museum, 1518 Republic Bank Building, Dallas, TX 75201	[2]
Kimbell Art Museum, Fort Worth, TX 76107	12, 859. 00
Lynchburg Museum, c/o Fidelity National Bank, P.O. Box 700, Lynchburg, VA 24505	200. 27
Sheldon Art Museum Archaeological and Historical Society, % R. C. Kingsley, E. Biddlebury, VT 05740	239. 00
Mr. David Collins, Frick Collection, 1 East 70th Street, New York, NY 10021	--

[2] Information not available.
[4] $68,000 in 1973.
[6] $121,318 in 1973.

AMERICAN ASSOCIATION OF MUSEUMS,
Washington, D.C., June 17, 1974.

Hon. VANCE HARTKE,
Chairman, Subcommittee on Foundations, U.S. Senate, Committee on Commerce, Washington, D.C.

Dear SENATOR HARTKE: In accordance with Kyran McGrath's letter of May 29, 1974, which stated that we would send you more information about the museums which are classified as private foundations, enclosed please find statistics on the amount of tax these museums paid in 1971, 1972, and 1973 and statistics on the amount of grant support the museums received in 1968 and 1973. In addition to the figures, we have attached some comments taken from letters to the AAM as a result of our survey; the comments reaffirm the burden placed on museums classified as private foundations. We will be glad to provide any other information you may need. Thank you.

Sincerely yours,

MARILYN HICKS FITZGERALD,
Executive Assistant to the Director.

Enclosures.

MUSEUMS CLASSIFIED BY IRS AS PRIVATE FOUNDATIONS

Name of museum	4 percent excise tax paid			Income from private fundings	
	1971	1972	1973	1968	1973
Pajaro Valley Historical Association, P.O. Box 960, Watsonville, Calif. 95076	(1)	$30	(1)	(1)	(1)
San Francisco Aquarium Society, Golden Gate Park, San Francisco, Calif. 94118	(1)	149	(1)	(1)	(1)
Butte County Pioneer Memorial, c/o Irene Parker, P.O. Box 309, Oroville, Calif. 95965	(1)	80	(1)	(1)	(1)
Briggs-Cunningham Automotive Museum, 747 E. Green Street, Pasadena, Calif. 91101	0	19	$82	0	0
American Air Museum Society, 616 Canal Street, San Rafael, Calif. 94901	(1)	(1)	(1)	(1)	(1)
The J. Paul Getty Museum, 17985 Pacific Coast Highway, Malibu, Calif. 90265	$669,025	97,279	54,273	0	0
Norton Simon Inc., Museum of Art, 3440 Wilshire Boulevard, Suite 1216, Los Angeles, Calif. 90010	12,251	10,164	52,494	0	0
Western Museum of Mining and Industry, P.O. Box 387, Colorado Springs, Colo. 80901	Not open	15	$1,534	Not open	$20,000
Automotive Museum, P.O. Box 13, Berlin, Conn. 06037	(1)	(1)	(1)	(1)	(1)
Litchfield Nature Center and Museum, Litchfield, Conn. 06759	(1)	(1)	(1)	(1)	(1)
Torrington Historical Society, c/o Colonial Bank & Trust Co., P.O. Box 148, Torrington, Conn. 06790	(1)	96	81	(1)	(1)
Hagley Museum, Eleutherian Mills-Hagley Foundation, Wilmington, Del. 19735	43,419	126,411	68,697	0	0
Delaware Museum of Natural History, P.O. Box 3937, Greenville, Del. 19807	(1)	1,496	(1)	(1)	(1)
The Henry Francis DuPont Winterthur,[2] Museum, Inc., Winterthur, Del. 19735	(1)	113,174	121,318	(1)	(1)
The Phillips Collection, 1600 21st Street, N.W., Washington, D.C. 20007	4,411	18,690	6,400	0	0
The De Ette Holden Cummer Museum Foundation, 829 Riverside Drive, Jacksonville, Fla. 32204	(1)	6,752	(1)	(1)	(1)
Marie-Selby Botanical Gardens, c/o Palmer First National Bank & Trust, P.O. Box 2018, Sarasota, Fla. 33578	(1)	4,159	(1)	(1)	(1)
Ships of the Sea, Inc., 501 East River Street, Savannah, Ga. 31401	(1)	3,475	(1)	(1)	(1)
Kauai Library and Museum Association, Lihue, Kauai, Hawaii. 96766	(1)	22	(1)	(1)	(1)
Morton Arboretum, 110 North Wacker Drive, Chicago, Ill. 60606	41,166	51,402	51,799	0	0
Harry and Della Burpee Art Gallery, 737 N. Main Street, Rockford, Ill.	(1)	37	(1)	(1)	(1)
Historical Building, 19 Grove Street, Petersborough, N.H. 03458	(1)	176	(1)	(1)	(1)
George F. Harding Museum, 86 E. Randolph Street, Chicago, Ill. 60601	(1)	(1)	(1)	(1)	(1)
Treaty-Line Museum, Inc., Rural Route 4, Liberty, Ind. 47353	(1)	260	(1)	(1)	(1)
Rush County Historical Society, c/o Priscilla Winkler, Rural Route 5, Rushville, Ind. 46173	(1)	1,528	(1)	(1)	(1)
Historic New Orleans Collection, 533 Royal Street, New Orleans, La. 70130	(1)	17,170	(1)	(1)	(1)
Zigler Museum Foundation, P.O. Box 986, Jennings, La. 70546	(1)	789	(1)	(1)	(1)
Old Gaol Museum, c/o York County Historical Society, York, Maine 03909	826	779	946	(1)	(1)
Blandford Historical Society, Main Street, Blandford, Maine 01008	49	47	54	0	0
Fruitlands Museums Inc., Prospect Hill, Boston, Mass. 01451	(1)	167	(1)	(1)	(1)
Isabella Stewart Gardner Museum, 225 Franklin Street, Suite 800, Boston, Mass. 02180	(1)	27,653	(1)	(1)	(1)
Kendall Whaling Museum Trust, c/o Hale & Dorr, 28 State Street, Boston, Mass. 02110	57	80	96	(1)	(1)
Leonard Boyd Chapman Wildbird Sanctuary, Suite 4500 Prudential, Boston, Mass. 02199	147	363	246	0	0
Cambridge Historical Society, 159 Brattle Street, Cambridge, Mass. 07138	374	316	286	0	0

See footnotes at end of table, p. 386.

MUSEUMS CLASSIFIED BY IRS AS PRIVATE FOUNDATIONS—Continued

Name of museum	4 percent excise tax paid			Income from private fundings	
	1971	1972	1973	1968	1973
Cape Cod Museum of History and Art, South Main Street, Centerville, Mass. 02632	(1)	99	(1)	(1)	(1)
Fall River Historical Society, 451 Rock Street, Fall River, Mass. 02720	(1)	627	1,843	0	0
Haverhill Historical Society, 240 Water Street, Haverhill, Mass. 01830	(1)	303	(1)	(1)	(1)
Thayer Museum Inc., 314 Main Street, Lancaster, Mass. 01623	(1)	11	(1)	(1)	(1)
Lynn Historical Society, 125 Green Street, Lynn, Mass. 01902	919	1,033	1,224	0	0
Manchester Historical Society, 41 Union Street, Manchester, Mass. 01944	173	177	605	0	0
Merrimack Valley Textile Museum, Massachusetts Avenue, North Andover, Mass. 01845	2,842	2,979	5,994	167,000	83,757
North Andover Historical Society, 153 Academy Road, North Andover, Mass. 01845	(1)	325	(1)	(1)	(1)
Heritage Plantation of Sandwich, Grove Street, Sandwich, Mass. 02053	261	251	37	0	0
Somerville Historical Society, Westward Boulevard and Central Street, Somerville, Mass. 02143	(1)	39	(1)	(1)	(1)
Stockman Historical Society, c/o Clark A. Richardson, 3 Barrett Avenue, Stoneham, Mass. 02180	(1)	36	(1)	(1)	(1)
Western Hampden Historical Society, Westfield, Mass. 01085	(1)	38	(1)	(1)	(1)
Sterling and Francine Clark Art Institute, Williamstown, Mass. 01267	(1)	58,832	(1)	(1)	(1)
Manchester Historic Association, 12 Amherst Street, Manchester, N.H. 03104	467	140	907	(1)	(1)
Alpena Museum Association, c/o Jesse Besser Museum, 491 Johnston Street, Alpena, Mich. 49707	(1)	4,993	(1)	(1)	(1)
Campbell Museum, Campbell Place, Camden, N.J. 08101	(1)	(1)	(1)	(1)	(1)
Adirondack Museum, Blue Mountain Lake, N.Y.	0	0	0	10,000	0
Long Island Historical Society, 128 Pierrepont Street, Brooklyn, N.Y. 11101	796	1,033	(1)	0	0
Alice T. Miner Colonial Collection, Chazy, N.Y. 12921	853	811	822	0	0
Corning Museum of Glass, Corning, N.Y. 14830	0	1,011	(1)	(1)	(1)
Trotting Horse Museum, 240 Main Street, Goshen, N.Y. 10924	(1)	40	(1)	(1)	(1)
Henry L. Ferguson Museum, Fishers Island, N.Y. 14453	14	86	71	0	0
Johnstown Historical Society, 17 N. William Street, Johnston, N.Y. 12095	29	54	59	0	0
Storm King Art Center, Mountainville, N.Y. 10953	(1)	2,634	(1)	(1)	(1)
Frick Collection, 1 East 70th Street, New York, N.Y. 10021	52,935	77,513	70,000	0	4,050
American Museum of Immigration, Liberty Island, New York, N.Y. 10004	(1)	221	(1)	(1)	(1)
Millicent A. Rogers Memorial Museum, c/o Jerome W. Sinsheimer, 660 Madison Avenue, New York, N.Y. 10021	(1)	17	(1)	(1)	(1)
Hill-Stead Museum, c/o Manufacturers Hanover Trust Company, 350 Park Avenue, New York, N.Y. 10022	(1)	172	(1)	(1)	(1)
Dutchess County Historical Society, P.O. Box 88, Poughkeepsie, N.Y. 12601	377	381	(1)	0	0
Genesee County Museum, 445 St. Paul Street, Rochester, N.Y. 14605	(1)	138	(1)	(1)	(1)
Rochester Historical Society, c/o Security Trust Co., 1 East Avenue, Rochester, N.Y. 14638	(1)	534	(1)	(1)	(1)
Sleepy Hollow Restoration, P.O. Box 245, Tarrytown, N.Y. 10591	38,448	43,519	48,115	0	0
Woodstock Museum, 747 Chillicothe Road, Amora, Ohio 44202	(1)	133	(1)	(1)	(1)
Dawes Arboretum, Rural Route 5, Newark, Ohio 43055	10,726	14,242	14,094	0	0
Barnes Foundation, Merion, Pa. 19066	(1)	(1)	(1)	(1)	(1)

See footnotes at end of table, p. 386.

MUSEUMS CLASSIFIED BY IRS AS PRIVATE FOUNDATIONS—Continued

Name of museum	4 percent excise tax paid			Income from private fundings	
	1971	1972	1973	1968	1973
Merrick Free Art Gallery and Museum, c/o Union National Bank, New Brighton, Pa. 15066	(1)	673	(1)	(1)	(1)
Colonial Flying Corps Museum, 1200 Packard Building, Philadelphia, Pa. 19102	(1)	3	(1)	(1)	(1)
John J. Tyler Arboretum, c/o Providence National Bank, 1632 Chestnut Street, Philadelphia, Pa. 19103	(1)	157	(1)	(1)	(1)
Taylor Memorial Arboretum, Girard Trust Bank, Philadelphia, Pa. 19101	(1)	306	(1)	(1)	(1)
Widner Memorial Museum, 1518 Republic Bank Building, Dallas, Tex. 75201	(1)	(1)	(1)	(1)	(1)
Kimbell Art Museum, Fort Worth, Tex. 76107	(1)	12,859	(1)	(1)	(1)
Heard Natural Science Museum and Wildlife Sanctuary, Route 2 McKinney, Tex. 75069	0	0	1,828	0	1,000
Lynchburg Museum, c/o Fidelity National Bank, P.O. Box 700, Lynchburg, Va. 24505	200	747	(1)	(1)	(1)
Sheldon Art Museum, Archaeological and Historical Society, East Middlebury, Vt. 05740	(1)	239	(1)	(1)	(1)

[1] Information not available or not yet computed.
[2] Advance ruling for public charity status under regulation section 1.507-2(e) "60-month procedure."

EXCERPTS FROM LETTERS TO AMERICAN ASSOCIATION OF MUSEUMS IN RESPONSE TO AAM SURVEY TO MUSEUMS CLASSIFIED BY IRS AS PRIVATE FOUNDATIONS

"The excise tax on our P.O.F. status constitutes approximately ten percent (10%) of our annual operating deficit." James P. Hurley, Executive Director, Long Island Historical Society, Brooklyn, New York

"Additional burden is (the) necessary expense of (a) professional accountant preparing (the) tax forms." Peter Van Kleeck, Treasurer, Dutchess County Historical Society, Poughkeepsie, New York

"Along with the tax and restriction on contributions, the costs of detailed accounting to the IRS should be also considered." "The public test should be whether the general public uses the foundation's operating assets." Edward J. Durkin, The Dawes Arboretum, Newark, Ohio

"Our educational offerings to students and adults are reduced by the amount paid as excise tax." John W. Harbour, Jr., Sleepy Hollow Restorations, Inc., Tarrytown, N.Y.

"Maintenance, security, utilities, and related expenditures are rather well fixed. One cannot reduce them without closing down parts of the Museum. Excise taxes are, therefore, not paid by reducing basic operating expenses, but rather are taken from funds that normally would be available for educational programs." Charles van Ravenswaay, Director, Winterthur Museum, Winterthur, Delaware

"Our work with school groups has been curtailed . . . it has meant dropping many programs." Mrs. Mary B. Gifford, Curator, Fall River Historical Society, Fall River, Massachusetts

"We are a new museum not yet open to the public. This tax is already a burden on our limited resources and we expect this burden to increase substantially in years to come. Edward A. Pacey, Treasurer, Western Museum of Mining & Industry, Colorado Springs, Colo.

PHOENIX, ARIZ., *June 2, 1974*

Senator VANCE HARTKE,
Chairman, Subcommittee on Foundations,
Committee on Finance,
U.S. Senate,
Washington, D.C.

DEAR SENATOR HARTKE: I will do my best to answer the questions contained in your letter to me of May 28, in seriatim:

(1) Since it takes the Internal Revenue Service nearly three years to compile and publish its compilations known as *Statistics of Income*, we do not yet

have a complete report for 1972. For example, that for 1969 did not appear until late in 1971. I have, therefore, not yet seen the report for 1972.

You ask how many individuals avoided paying ANY Federal income taxes as a direct result of charitable contributions; this again is impossible to answer, for deductions permissible for this purpose constitute only one category of allowances, of which there are many.

You ask also whether this type of tax-avoidance can take place under the 1969 amendments to the Internal Revenue Code. The answer is that these revisions made possible far greater tax-avoidance through gifts to so-called charity than before. The maximum deduction against adjusted gross income was increased from 30 to 50%; but, more significantly, "operating" foundations were given status in this regard with churches, educational institutions, hospitals, governmental units, etc., under section 501(c)(3). In other words, a man can now establish his own foundation and if it engages in some kind of research, the man who established and controls it can deduct 50% of his own agi from this as gifts to his own foundation.

Of course, there are many other ways in which wealthy persons can reduce their tax-liabilities—through the payment of interest, fast real-estate writeoffs, depletion allowances, etc., etc.

(2) (a) When a gift is made as a charitable contribution, full allowance is made for its present market value and there is no tax on the capital gain. For example, if a man has stock that cost $10,000 but is now worth $100,000, full credit is given for the larger amount, with no tax due on the $90,000 of gain.

(b) In the case of a personally controlled foundation, the assets of which consist, for example, of stock in a corporation owned by the same individual, the foundation is expected to exchange such assets for others within five years so that they will be reduced to 20% of the total. However, the same person or persons can continue to control both the corporation and the foundation.

(3) I have been unable to find any official information concerning current foundation assets in addition to that given on page 4 of my prepared statement. It takes several years before such data becomes available to the public.

(4) The facts about the Disney Will and Foundation are contained in a book written by John D. Cunnion, in which he describes 62 intricate wills.

The income from the Disney Worlds is not unrelated business income under the definition of the Internal Revenue Code, because this income is the very thing for which the foundation was created. Income is unrelated only if it is different from that for which the "charity" was created. For example, if a hospital were to establish a plant to manufacture refrigerators or automobiles, the revenue from such an enterprise would be unrelated and therefore taxable income.

Under the title of charity, Disney World in California is also exempt from real estate taxation, as is the Ontario Speedway, owned by another "charitable" foundation.

(5) Johnnie Walters stated to the editors of the *National Enquirer* in an article published on the front page of an issue of this publication during 1973 (I do not have the paper before me at the moment) that the IRS knew of at least 1.4 million individuals who owed Federal income taxes but had not paid anything. You can easily verify this.

But this is only the tip of the iceberg reflecting the extent of the current tax-rebellion. In its issue of September 17, 1973, USN&WR published a feature article containing the following statements: (1) the present tax-dodging spree or Hidden Taxpayers' Strike, is spreading rapidly, is costing the government in Washington at least 6 billion dollars a year and threatening to get completely out of hand." And (2) further: "Tax experts outside the IRS say the agency is understating the problem in an effort to soften resentment among honest taxpayers. Some put the real losses . . . at around 20 billions a year . . ." which would be about one-third of the total now collected from personal incomes at all levels and would probably involve not less than 5 or 6 billion middle- or above-average-income taxpayers.

According to another article in the same publication of April 24, 1972, John B. Connally declared that 97% of all returns prepared in Southeastern States "were fraudulent." According to an article published in the Los Angeles *Times*, April 13, 1973, Johnnie Walters stated that noncompliance in other parts of the country was worse than in the Southeast.

According to a poll taken by Lou Harris in 1972, 74% of all American taxpayers are so angry that they would be in complete sympathy with a national strike against the federal income tax system and its administration.

I thank you for the opportunity of offering this clarification of my statements during the recent hearing in Washington. And I would be pleased to have this letter included in the public hearing record.

Most sincerely yours,

MARTIN A. LARSON,
Tax Consultant of Liberty Lobby.

TAX ADMINISTRATION: TREASURY WOULD SUPPORT CUTTING TAX ON PRIVATE FOUNDATIONS TO 2 PERCENT

Internal Revenue Commissioner Donald C. Alexander told the Senate Finance Subcommittee on Foundations today that the Treasury would support cutting to 2 percent the 4 percent excise on private foundations.

Under the 1969 Tax Reform Act, the tax is levied on the net annual investment income of foundations. Income subject to tax is income from interest, dividends, rents and royalties minus the expense incurred in earning the income.

Earlier witnesses before the Foundations Subcommittee have called for a reduction in the excise on the ground that it not only raised enough money to finance IRS policing of foundations but for all other exempt organizations as well. The objective of the foundation excise was to cover IRS expenses in connection with foundations, although the revenues go into the general fund of the Treasury.

Alexander was questioned by Subcommittee Chairman Vance Hartke (D-Ind) as to why it took so long for IRS to issue regulations under the foundation provisions of the TRA. Alexander, commenting that he just signed one new regulation last Saturday, said the provisions are about the most complex in the Inter Revenue Code.

There is frequently the problem "of meshing our duties on one hand with equity on the other," Alexander said. He added that because some foundation provisions of the TRA were not scheduled to be effective for several years after enactment of the TRA, IRS gave them "low priority."

Chairman Hartke, summing up earlier hearings, said: "We had witnesses who described the many accomplishments which were made possible by foundation money. We had witnesses who recognized the positive contributions of foundations, but who encouraged foundations to do much more, and we had witnesses who concluded that foundations were little more than a tax dodge for the wealthy. I suspect that there is more than a little truth in each of these viewpoints. What is most disturbing to me, however, is the lack of hard facts."

TAX LEGISLATION: FINANCE COMMITTEE SETS HEARING ON PROPOSED TAX INCREASES

The Senate Finance Committee announced today that hearings will begin June 5 on pending tax increase proposals.

The hearings will cover those proposals which various senators have announced will offer as riders to a minor House tariff bill or to the debt limit bill.

The committee announcement follows:

FINANCE COMMITTEE SCHEDULES HEARINGS ON TAX INCREASE PROPOSALS

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee would begin hearings on various pending tax increase proposals beginning Wednesday, June 5, at 10:00 A.M. in Room 2221 of the Dirksen Senate Office Building.

THE WAIN FOUNDATION,
Los Angeles, Calif., June 11, 1974.

VANCE HARTKE,
Chairman, Subcommittee on Foundations of Senate Finance Committee, U.S. Senate, Dirksen Senate Office Building, Washington, D.C.

DEAR SENATOR HARTKE: Thank you for your letter of May 28. It confirms the faith I so strongly expressed at my appearance May 14 before your committee—our democracy works! I take pleasure in answering each of your questions in the order listed in your letter, and I shal lbe happy to have my answers included in the public hearing record.

1. RE 20% VS 50% LIMITATIONS REFERRED TO IN MY MAY 14 STATEMENT, PAGE 3

I did not intend to suggest that you relax these limitations. I do recommend that you eliminate the discrimination against private foundations. This can be accomplished by providing that contributions to private foundations be subject to the same 50% limitations as to public foundations.

This would give no cause for tax abuse concern because the 1969 Tax Reform Act restrictions have removed uncertainties and loopholes in the prohibited transactions and accumulation of income provisions of the 1950 act. Furthermore the penalties on foundations, foundations managers, and substantial contributors and ultimate imposition of confiscatory tax on foundations are powerful deterrents to tax abuse.

A most important deterrent to tax abuse is the apparent adoption by the Internal Revenue Service of a policy of audits on the same basis and frequency as taxable entities to assure compliance with the provisions of the 1969 Tax Reform Act. The excise tax provisions of the 1969 Act will provide the finances for the necessary cost of assuring compliance at less than a quarter of the 4% excise tax rate.

All the above are your assurance against tax abuse. The 20% vs 50% discrimination against private foundations has no relationship to tax abuse. It "throws out the baby with the dirty bathwater".

2. THE WAIN FOUNDATION HISTORY AND THE INVOLVEMENT OF MY FAMILY

I established the foundation December 13, 1963 with a contribution of $11,000. I estimate that my annual contributions thereafter averaged approximately $10,000. There was and is no relation between any business activity of mine and the creation of the foundation.

To what extent do I and members of my family remain involved with my foundation? I and my wife, son and daughter are officers and members of Board of Directors with no compensation for our services to or on behalf of the foundation. I and my wife are involved almost every day. My son is involved to the extent that attention to his wife, two children and a growing business career permit. My daughter is also involved to the extent that attention to her husband and two children permit. My wife and I have nurtured the involvement of our son and daughter. An illustration comes readily to hand.

On a recent visit from my daughter she brought with her the enclosed copy of a May 29 letter to Robert Hutchins which she received from me bearing my handwritten message to her. The fact that a most important 16th birthday in a girl's life is associated with a charitable fund raising affairs and that almost 15 years later she saw fit to bring this letter to me and express her gratitude for the reminder is counted among my blessings. If you wish you may make a copy of this letter for public hearing record but please return the enclosure to me.

3. RE: CLARIFICATION OF MY REASONING FOR MY STATEMENT PAGE 5 OF MY TESTIMONY ON MAY 14 THAT "MY PROGRAMS MIGHT BE LESS INNOVATIVE NOW THAN IN THE PAST YEARS"

In reviewing the 1973 list of The Wain Foundation grants I was struck by the fact that many grantees have been on the list almost every year. I began to wonder whether I was doing this out of habit. Are each of these grantees continuing to do year after year a creative task in the causes which raise the quality of life with the same degree of "leverage" that attracted the first grant from my foundation? Am I succumbing to the "status quo syndrome"?

Yes, I am succumbing to the "status quo syndrome". Why? Because 1969 Tax Reform Act and legislation under consideration thereafter suggests that what is really desired is the demise of Private Foundations. If this be so (and I pray I am mistaken) America would lose a most powerful potential for the solution of problems that have been with us in varied forms since man was "created".

Private Foundations have the human and material resources to address themselves to the root of these problems instead of merely reacting to the symptoms. Remove inhibitions to their freedom to tackle injustice which has been one of the greatest obstacles to achievement of the full potential of our society. There are many ideas and actions that need "a borning" and many ideas and actions

that need "a dieing". But they will not be born unless we help usher them in; and they will not die unless we help usher them out.

Sincerely,

PHILIP WAIN,
President.

PHILIP WAIN & CO.,
May 29, 1974.

MR. ROBERT M. HUTCHINS,
Chairman, The Center for the Study of Democratic Institutions,
Santa Barbara, Calif.

DEAR ROBERT: Emma and I have always admired your independence of thought and your ability to express your ideas succinctly and with a high degree of style, so in replying to your letter of May 28, we frankly borrowed from it because we can't match it.

On the 25th of August we shall complete 15 years of support for the Center as Founders. Our daughter Margo has Romanoff's menu of August 25, 1958, date of Center's fund raising "kickoff" dinner meeting and date of her sixteenth birthday. The menu is signed by you, Justice Douglas, Govenror Brown et al.

The establishment of the Center has been a marvelous experience for us. The Board of Directors has been stalwart, farsighted and generous. The Fellows and the staff have been dedicated and, in the academic jargon, "productive".

To have had the chance to associate with and learn from all these people has been a piece of good fortune we did not deserve. We are deeply grateful to you.

As Life Founders we hope to continue our association with the Center—and with you.

Sincerely,

PHILIP WAIN.

TAX REFORM RESEARCH GROUP,
Washington, D.C., June 17, 1974.

Senator VANCE HARTKE,
Chairman, Subcommittee on Foundations, Committee on Finance, U.S. Senate,
Washington, D.C.

DEAR SENATOR HARTKE: In response to your letter of May 29, 1974, I will be glad to elaborate on any of the information which you requested.

Your first request was for documentation of the payout rate of the Lilly Endowment which was given in my statement as 1.1% for 1972. Those asset and payout figures, and the statistics for all of the foundations listed, were obtained from the files of the Foundation Center, 1001 Connecticut Avenue N.W., Washington, D.C., which is a library and information center for philanthropic foundations. The Foundation Center is supported by foundations and publishes the Foundation Directory. A percentage was computed by our office from those statistics.

You inquired what specific information I could supply on the effect that the minimum payout rate has had on the amount of money going to charitable purposes. Unfortunately, I have no knowledge of any comprehensive statistics which give the payout rates and totals for all foundations. The staff of the House Banking and Currency Committee which has worked on this question estimated that in 1968 the total payout was $1,636 million and that an additional $664.-661,000 would have been paid out under the new 6% requirement. Since those are only estimates and are based on figures that are six years old, they obviously can only serve to describe the scope of the issue and not the fact. The staff personnel did not know of any actual statistics of the sort that you have requested.

I think that the lack of comprehensive and reliable statistics only emphasizes the need, discussed at the hearings, for an annual reporting system. Even if such statistics do exist, they are certainly not publicly or widely known which makes it impossible for those who make policy or those who administer it to gauge the efficacy of their efforts.

As for the uses of the 4% tax, it seems there are many possibilities to be considered. Spokesmen for foundations favor lowering the tax rate because, in 1972, $56 million was collected but only $12.9 million was spent in auditing foundations.

The proposals for sharing these revenues with the states have been considered at length by the House Banking and Currency Committee Subcommittee on Do-

mestic Finance in its hearings of April 5 and 6, 1973. Representative Wright Patman's bill was under consideration and several State Attorneys General appeared at those hearings to testify in support of revenue sharing. Their testimony emphasized several very important points about the enforcement of the 1969 Tax Reform Act provisions and the increased burdens which it placed on the States' Attorneys General. It was pointed out, in fact, that the Ways and Means Committee anticipated and wanted to encourage the strong participation and enforcement efforts by state officials. Committee Report No. 91-413 (1969) states:

"It is expected that effective assurances are most apt to be available in those States where there is vigorous enforcement of strong State laws by the State attorney general or other appropriate official. In order to encourage and facilitate effective State involvement, the bill provides as an additional condition of exemption for private foundations the requirement that the governing instrument require current distributions of income (Section 4942) and prohibit self-dealing (Section 4941), retention of excess business holdings (Section 4943), speculative investments (Section 4944), and taxable expenditures (Section 4945). Existing private foundations are given time to modify their governing instruments. Your committee intends and expects that this requirement will add to the enforcement tools available to State officials charged with supervision of charitable organizations."

Julius Greenfield, Assistant Attorney General for the State of New York, further stated in those hearings:

"The federal approach, the imposition of sanctions, certainly has a deterrent effect upon improper foundations administration. But it only goes part of the way. It does not provide, and there is some doubt that it can, for the various kinds of court and administrative actions that are available to the state attorney general. These would include imposition of personal responsibility on foundation managers for improper administration, removal of officers and directors and appointment or election of new officers and directors, dissolution of foundations and distribution of their assets to public charities and requiring a full judicial accounting of the activities of foundation administrators."

The statemnts of the other Attorneys General appearing at that hearing in support of revenue sharing for foundation auditing spoke in support of Greenfield's analysis. They detailed the size of the staffs, the lack of money and the huge administrative task of overseeing the functions of the foundations in their states. Contrasted to these difficulties is their unique ability to enforce many of the requirements of the 1969 reform act with maximum efficiency.

The benefits of sharing revenues with the states to provide for better enforcement would not be completely eliminated by earmarking the funds collected for special use by the federal government. I think that we have seen ample evidence of the need for better auditing and reporting, and the federal government is certainly in the best position to do much of the comprehensive reporting that needs to be done. It alone can collect and compile all of the figures needed. But it cannot duplicate the continuing casework and legal responsibilities that the state officials have, even aside from their responsibilities under the 1969 Tax Reform Act. The legal concept of cy pres, for example, dates back to the common law where it was recognized that a public representative was needed to safeguard the rights of the public to charitable funds. As beneficiaries of charitable trusts, the public is a class too diffuse and indefinite to protect its own rights otherwise. Present day States Attorneys General have many other responsibilities in addition to those handed down by the common law. State statutes, as well as the Internal Revenue Code itself, impose a wide range of audit and enforcement responsibilities. The earmarking of federal funds for increased federal auditing, while a welcome measure, should not be considered to the exclusion of funding state enforcement activities.

Sincerely,

PATRICIA S. SENGER.

RESPONSE TO SENATOR HARTKE'S QUESTIONS BY JOE G. DEMPSEY, EXECUTIVE DIRECTOR, LOS ANGELES INTER-FOUNDATION CENTER

Question 1. You refer to a study of the impact of the payout requirement on page 2 of your prepared statement. Which study do you have in mind?

The Los Angeles Inter-Foundation Center is attempting to organize a Southern California study of the 6% payout provision using the report by Norman True

as a model. This report, which is the study I referred to on page 2 of my prepared statement, was presented as testimony during your October 1973 hearings. The purpose of our study will be to test the hypothesis of the True report on a wider range of foundations in Southern California, especially small and medium size foundations.

Question 2. Would you expound on your statements about program restrictions and expenditure responsibility to indicate some of the specifics which have led to your conclusions?

In meetings and personal interviews with Trustees and Managers, a common concern has been voiced: it is not possible to develop the procedures that are necessary to satisfy the law while maintaining the ability to respond quickly to hardship scholarship grants. Therefore, adjustments are being made to replace scholarship aid with general scholarship grants to educational institutions. Obviously, this diminishes administrative energies by routing the grants through college committees, which fact, although financially insignificant, should be noted. My personal concern is that this further isolates foundation officials from the community of need and decreases aid to hardship students.

If foundations are to have a distinctive role in society, surely one of their unique abilities is to personally engage community need in ways that established institutional rules and practices do not permit. One of the flaws in TRA'69 is that it effectively disables that quality of quick responsiveness that makes this mode of philanthropy unique and valuable.

Question 3. Would not the proposal contained in the pension bill result in improved knowledge of foundation problems and activities, thus enabling Congress to legislate in a more enlightened manner?

I have seen or heard nothing which indicates the reorganization of IRS under the pension bill (H.R. 2 and H.R. 4200) would improve knowledge of foundation problems.

On page 7 of the IRS report to you, "Background Information in Reply to Senator Hartke's Questions of March 22, 1974", the Commissioner spells out what he expects the proposed legislation to do. It will:

"*elevate responsibility* for the activities within the service"

"*Increase coordination* between headquarters and the field."

"permit *more unified policy guidance* and *more uniform treatment* of cases involving the status of taxexempt organizations."

The Commissioner nowhere states that there has actually been a lack of coordination or uniform treatment, nor am I aware of complaints by foundations to that effect.

But more importantly, the Commissioner makes a statement in paragraph 1 of page 7, which I believe points up the lack of value to the philanthropic community, to charitable institutions, and to lawmaking-bodies-in-search-of-enlightenment, of the proposed reorganization.

"We do not expect major changes in our activities of enforcing the exempt organization provisions of the Internal Revenue Code which do not relate to pension matters."

"We also do not anticipate any major changes in our recruiting and training of exempt organization personnel."

It seems to me that he is saying that there will be a change in form, not in function. There is nothing that we can discover within the present arrangement that would prevent the "improving of knowledge of foundation problems" if they felt it was desirable.

It is reported that it now costs approximately $13 million to audit private foundations, approximately $19 million to audit all exempt organizations. If Commissioner Alexander's recommendation that 70% of private foundations be audited less frequently were implemented, the cost would be substantially less. But if the formula proposed in H.R. 4200 for funding this new office were applied to Excise Tax collections for 1973 (one half of $76 million) foundations would be contributing $38 million to the support of this new office.

It is difficult for us to imagine how these additional funds would be used. On the basis of information released by the IRS and other Washington agencies, we can only speculate that monitoring and auditing activities on 80% of the foundations would be increased dramatically. One alternative seems possible: that, although the revenues for this new office would be equally shared, the expenditures would not. Which is to say, that revenue from the 4% Excise Tax on foundations would subsidize the administration of the Employee Pension Plan section. Before H.R. 2 or H.R. 4200 is voted, there should be detailed clairification on this issue.

APPENDIX C

Statement of Hon. Vance Hartke Together With Questions Submitted by Senator Hartke to the Internal Revenue Service

Statement of Hon. Vance Hartke

During the June 3, 1974, hearings of the Subcommittee on Foundations, I asked I.R.S. Commissioner Donald C. Alexander several questions about the so-called Special Activities Staff within the I.R.S. My interest in this group arose from newspaper reports and testimony during the hearings of the Senate Select Committee on Presidential Campaign Activities which contained allegations that this group was used for the partisan political purposes of the Administration. It had also been alleged that this group had directed its attention to certain private foundations and to other exempt organizations whose activities were, in one way or another antagonistic to the Administration.

The dialogue which I had with Commissioner Alexander will be found in the transcript of the Committee hearings printed in this volume. In addition, I submitted several questions in writing after the hearing to give Commissioner Alexander an opportunity to expound on some of the points raised during his oral testimony. His responses are also printed in this volume.[1]

It is not within the purview of this Subcommittee to embark upon a detailed investigation of the Special Service Staff. The Joint Committee on Internal Revenue Taxation has issued one report on this subject,[1] and other Congressional Committees have held hearings on the politicization of the Internal Revenue Service.

On the basis of the June 3 hearing and the Commissioner's subsequent responses to my written questions, I do have some observations which I am compelled to make.

The Internal Revenue Service is one of the most important of all Federal agencies, not only because it is responsible for collecting Federal revenues and enforcing Federal revenue laws, but because it collects so much detailed information about the private lives of our citizens. It is imperative that the I.R.S. conduct its activities with a full sense of its responsibilities. If it allows its awesome power and information to be used by anyone for selfish political purposes, it fails in performing its tasks and ceases to deserve public trust.

The record shows that, beginning in 1969, an effort was made to direct the attention of I.R.S. to certain "activist organizations," which Commissioner Alexander defines as "extremists on the right or on the left." The Internal Revenue Code is designed to apply to all Americans, without regard to their political beliefs or activities. So should the enforcement of that Code be equally blind to political beliefs and activities.

No matter what the intention of those who established the Activists Organizations Committee (whose name was changed to the Special Service Group and later to the Special Service Staff), the clear message was there: "We want the I.R.S. to direct its attention to certain

[1] See p. 397.

35-686—74——26

individuals or groups in our society who are political activists." That is the message which was sent to the I.R.S., and that—I believe—is the message which the I.R.S. received.

The record of our hearings does not show just which groups received increased attention at the hands of the Special Service Staff, nor does it show that any such group suffered adversely from such increased attention. But those details are unimportant. What is important is that the creation of the Activists Organizations Committee in 1969, was the beginning of the politicization of the Internal Revenue Service.

If the Service can be encouraged to embark upon selective enforcement (and, despite Commission Alexander's denial, the very existence of the Special Service Staff represented selective enforcement), then the next step was to get the I.R.S. to cooperate with efforts directed either in support of Administration "friends" or in opposition to Administration "enemies."

I make no judgment as to whether the Internal Revenue Service ever participated in or cooperated with any policy of harrasment of Administration "enemies." The Select Committee on Presidential Campaign Activities received testimony that a White House memorandum from Tom Charles Huston to H.R. Haldeman contained the following statement regarding the use of the Internal Revenue Service to monitor the activities of "ideological organizations:"

"Nearly 18 months ago, the President indicated a desire to move against leftist organizations taking advantage of tax shelters . . . What we cannot do in a courtroom via criminal prosecutions to curtail the activities of some of these groups, IRS could do by administrative action. Moreover, valuable intelligence-type information could be turned up by IRS as a result of their field audits." The hearing record of the Subcommittee on Foundations shows that the Assistant Attorney General, Internal Security Division, Department of Justice, made 99 requests for the calendar years 1960 through 1973 for information collected by the Special Service Staff. What was done with that information is not known. But I do not conclude that the Internal Revenue Service allowed its name to be tarnished by selecting certain taxpayers for special treatment solely on the basis of their political leanings.

The Commissioner has stated that "there were no established criteria or memoranda used by the Special Service Staff for the selection of organizations about which it gathered information." He goes on to state that "usual standards for referring items from the field were employed." This, however, flies in the face of his own statements and other material in the hearing record that the very existence of this staff was to direct I.R.S. attention to "extremist" groups—a highly subjective term—and that it was the Special Service Staff which collected information and then referred that information to field offices.

Private foundations are particularly susceptible to this type of selective activity on the part of I.R.S. Much was made of certain foundation grants during the Congressional debate leading to the Tax Reform Act of 1969, and there are several provisions in that Act which actually discourage foundations from engaging in innovative activities. I do not disagree with the need for effective controls over

foundation activities. They receive a subsidy in the form of a tax exemption. In effect, the public is allowing foundations to use monies which—to a substantial extent—would go to the Federal Treasury. They have a right to expect that money not to be misused. However, neither laws—or the enforcement of those laws—should discourage foundations from seeking new horizons. That is what concerns me about the establishment and activities of the Special Service Staff.

DEPARTMENT OF THE TREASURY,
INTERNAL REVENUE SERVICE,
Washington, D.C., July 24, 1974.

COMMISSIONER

Hon. VANCE HARTKE,
Chairman, Subcommittee on Foundations, U.S. Senate,
Washington, D.C.

DEAR SENATOR HARTKE: With reference to your letter of July 1, I am forwarding the enclosed material.

As you are probably aware, the Subcommittee on Constitutional Rights of the Senate Judiciary Committee has been looking into certain matters concerning the Special Service Staff. Some of the information contained in this response duplicates that which we made available to the Subcommittee, and, we expect, will be discussed in a report presently being prepared by Senator Ervin's Subcommittee. Under the circumstances, we have advised Senator Ervin of our assistance in the instant matter.

I thank you for the opportunity to provide this information. With kind regards,

Sincerely,

DONALD C. ALEXANDER.

Enclosure.

1. How much of the increase which you have requested for the budget of the Service for Fiscal Year 1975 will go to activities directly related to your responsibility to administer exempt organizations?

Although the FY 1975 IRS Congressional Budget request includes a 64 man-year increase earmarked for activities related to administering exempt organizations, we anticipate significant changes in our programs in this area. As you are aware, pending legislation involving exempt organizations is nearing completion. This proposed legislation will require us to make a complete review of our responsibilities in this area, and a complete reevaluation of our resources.

2. Can you cite the number of instances in which your staff has determined that a private foundation has changed its status to a public charity since 1969?

As explained previously, we don't have a system to collect this information regularly. In an effort to provide you and your subcommittee with some information on the subject, we asked our field offices for their recollections. On that basis, we have found that most organizations whose status was changed from private foundation to public charity since 1969 were erroneously classified initially. These number approximately 1600, and they were, to a large degree, not properly classified in the first instance because of inadequate information being furnished. Also, a few dozen have terminated their private foundation status under the provisions of Code section 507(b)(1)(B) and have become public charities.

3. Without referring to the parties by name, can you cite any instances in which your auditors have determined that section 509(a)(3) organizations are not living up to their statutory restrictions and responsibilities?

Again, on the basis of our field offices' recollection, there are at least fifteen to twenty cases of adverse actions reclassifying section 509(a)(3) organizations to a private foundation status.

4. In your testimony on section 170(b)(1)(A)(vi) organizations, you characterized the support requirement as "substantial." Would you elaborate on the reasons for your characterization?

Regulations under section 170(b)(1)(A)(vi) require an organization to obtain at least ten percent of its support from the public if it is to qualify as a public

charity. Beyond this, an organization that obtains less than 33 percent of its support from the public must also show that it has a "public" board of directors, "public" facilities, or other evidence that it is responsive to the public. The ten percent minimum public support requirement was introduced in an amendment to the section 170 regulations subsequent to the Tax Reform Act of 1969. Since qualification as a section 170(b)(1)(A)(vi) organization is a critical question under the Tax Reform Act provisions, it was necessary to define "substantial public support" with greater specificity. The legislative history indicates that section 170(b)(1)(A)(vi) was intended to except from private foundation status organizations such as museums, libraries, and community centers as well as community chest and other fund-raising organizations. For organizations such as museums and libraries, which are usually endowed, the ten percent requirement is a measure of "substantial" public support. The presence of the other facts and circumstances mentioned above is additional insurance that the organization is responsive to the public.

5. What plans does the Service have to provide a means to determine the fair market value of foundation assets?

The book value and fair market value of foundation assets held at the close of the taxable year are required to be provided on Form 990-AR (Annual Report of Private Foundation). In addition, the fair market value of foundation assets held at the close of the taxable year is required to be entered in the appropriate block on page 1 of Form 990-PF (Return of Private Foundation Exempt from Income Tax). The amounts shown on the Form 990-PF and 990-AR filed by private foundations are available for public inspection.

The Service is presently transcribing private foundation fair market value of assets as entered on the Form 990-PF to our Exempt Organization Master File (EOMF). The data is being transcribed starting with calendar year 1973 and fiscal year 1974 returns filed.

Statistics on the fair market value of assets for calendar year filers will be available by December 31, 1974. Fiscal year statistical data will be available depending upon the accounting period of the private foundation.

These amounts as reported on the returns are subject to verification upon audit. Examiners consider all the relevant facts and circumstances in determining the validity of the fair market value figures reported.

6. What was the relationship between the Activists Organization Group and the Senate Permanent Subcommittee on Investigation?

The Activists Organization Group was established because the Permanent Subcommittee on Investigation of the Senate Government Operations Committee, among others, had expressed serious concern about possible violations of the tax laws. Attached is a copy of a memorandum describing one of the organizational meetings of the Group. This memorandum indicates the relationship involved. Basically, the interest of the Subcommittee was to provide IRS with information developed by the Subcommittee that could be helpful in identifying potential violations.

JULY 29, 1969.

Memorandum for file.

Subject: Activist Organization Committee.

This Committee met in Room 3049 at 9:30 A.M. this morning under the chairmanship of Mr. Paul H. Wright. In addition to the permanent Committee, other persons identified below were present. The principal purpose of the meeting was to discuss what we are doing with representatives of the Senate Committee on Government Operations and to request their assistance and cooperation in this project. The following persons attended: Mr. Paul H. Wright CP:C, Mr. Donald F. Cowles CP, Mr. William F. Gibney CP:I:O, Mr. Gilbert F. Haley CP:I:O, Mr. James J. McGarty CP:A, Mr. Donald O. Virdin CP:C:D, Mr. Thomas F. Casey CP:AT, Mr. Roy T. Orr, Internal Revenue Agent, Atlanta District, Mr. Edward D. Hughes, AT&F Investigator, Southeast Region, Mr. Philip R. Manuel, Senate Committee on Government Operations, Mr. John E. Drass, Senate Committee on Government Operations, Mr. Fred R. Miller, Senate Committee on Government Operations.

Mr. Wright outlined the basic functions, plans, and composition of the Committee and what it hoped to accomplish. He pointed out that although the permanent Committee was composed of individuals from only four Compliance activities, it would be necessary to obtain help from all parts of the Service, in-

cluding the Chief Counsel, Technical, Data Processing, Office of International Operations, and Appellate. Mr. Wright also outlined the following guidelines:

1. Because disclosure of official information will be involved, no changes in this regard will be made. If the Senate Committee on Government Operations or any other outside organization wants information concerning any taxpayer in which the Activist Organizations Committee is interested, requests for disclosure of information must be made through regular channels and the Disclosure and Liaison Branch.

2. From now on, any informal arrangements for the exchange of data or any questions concerning the activities of the Committee which are desired by the Senate Committee on Government Operations will be made directly to Mr. Wright unless he directs otherwise. This is necessary so that close control can be maintained over the work going on.

3. As soon as permanent quarters and telephones have been established, this information will be furnished to Mr. Manuel.

4. The Internal Revenue Service's principal interest in this matter is to insure that all IRS laws have been complied with, that all income tax returns and payroll tax returns have been filed, that required information returns have been filed, that any income is reported properly. In addition, we will make an in-depth study of the sources of funds to support the activist organizations. As part of this, we will want to determine whether individuals contributing money have deducted contributions legally.

5. The permanent members of the Committee will be: Chairman—Mr. Paul H. Wright, Collection Division; Mr. Edward D. Hughes, Alcohol, Tobacco and Firearms Division; Mr. William F. Gibney, Intelligence Division; Mr. James J. McGarty, Audit Division.

6. Although the Committee has been created with an indefinite life, it is expected that the permanent members detailed from outside Washington will be working on a full-time basis at least until the end of November 1969. However, it is quite likely that this assignment will continue for a long period of time.

7. As information is assembled by the Committee on any specific organization, the principal investigating agent in the field will be called to Washington to review the data assembled, and it is expected that considerable travel may be done as part of the Committee's operations.

8. It was again emphasized that the Committee is not taking any function from any Compliance division or from any other part of the Service. What we are doing is trying to assemble all information available from within the Service, from the FBI, from the Department of Defense, from any other Federal agency having information, and from any Congressional committee having information. This data will be collated, analyzed, and given to the proper functional unit for attention.

Mr. Manuel, on behalf of the Senate Committee on Government Operations, offered the cooperation of the Committee and access to the Committee files. However, he plans to discuss this with Senator McClellan to obtain final clearance before giving IRS the green light; but he anticipates no difficulty. He described the method of filing used by the Committee, and it is planned that IRS representatives will inspect those files as soon as possible.

Mr. Manual furnished several charts concerning the Black Panthers, the Students for a Democratic Society, and others, and offered to furnish additional material which we may request. He said the Committee has already published many volumes of hearings and we may obtain copies of these. The hearings which have just been concluded have not been printed, nor has the report been written, and it will probably be two or three months before they are finally issued.

In summary, it can be said that the Committee has been created and will begin full-scale operation as soon as the space has been made available. Also, from today on, any contact with other agencies having to do with the organizations in which this Committee is interested should be cleared with the Chairman, or made as directed by him. We do not want to have this rather sensitive matter handled loosely. Any questions may, for the time being, be directed to Mr. Wright in Room 5242, Extension 3897.

A copy of this memorandum has been delivered to each person attending the meeting, to each Compliance Division Director, and to each person not otherwise receiving a copy who attended the organizational meeting of July 24, 1969. However, copies will not be furnished to representatives of the Senate Committee on Government Operations.

D. O. VIRDIN.

7. Would you supply the Subcommittee with any directives or memoranda which established the group and any directives or memoranda which abolished it?

See, (1) Memorandum establishing the Activists Organizations Committee (AOC), dated July 29, 1969 attached to the response to question 6; (2) IR-1323, August 9, 1973, press release announcing disbandment of the Special Services Staff; and (3) Manual Supplement 11G-75 abolishing the Special Service Staff dated August 13, 1973. The name of the AOC was later changed to the Special Service Group and then to the Special Service Staff.

NEWS RELEASE

DEPARTMENT OF THE TREASURY,
INTERNAL REVENUE SERVICE,
Washington, D.C., August 9, 1973.

IR-1323

Washington, D.C.—The Special Services Staff within the Internal Revenue Service will be disbanded, Commissioner of Internal Revenue Donald C. Alexander announced today.

"The tasks now being performed by the Staff," Mr. Alexander said, "can be handled efficiently by other components of the Service as a part of their regular enforcement activities."

The decision was reached after a two-month study ordered by Mr. Alexander immediately after he entered office. The study showed that the function performed by the Staff could be carried out by other units of the IRS having responsibilities for enforcement and administration of the tax laws.

The Staff was originally formed in 1969 as a result of inquiries made of IRS by the Permanent Subcommittee on Investigations of the Senate Committee on Government Operations. At that time, in the wake of civil disruptions and demonstrations by "extremist" organizations, the Subcommittee raised questions concerning the financial resources available to these organizations. There was evidence that some of the organizations which enjoyed tax exempt status were not complying with the tax laws. The assignment of the Staff was to gather information on the sources of funding of these organizations and to check the income tax status of the organizations and their principals.

The data-gathering work of the group is presently confined to tax resistance organizations and those individuals who publicly advocate noncompliance with the tax laws. "The IRS will continue to pay close attention to tax rebels," Mr. Alexander said, "but political or social views, 'extremist' or otherwise, are irrelevant to taxation; the work of the Staff as a separate unit will be phased out."

August 13, 1973.

MANUAL SUPPLEMENT

(Special Service Staff Activities)

Section 1. Purpose

The purpose of this Manual Supplement is to abolish the Special Service Staff, Collection Division, National Office.

Section 2. Background

The Special Service Staff was established in July 1969 to serve as a central point for coordinating information relating to organizations or related individuals involved in tax strike, tax resister, and tax protester activities, and distributing it to appropriate district offices. A determination has been made that it is no longer necessary to continue this activity.

Section 3. Abolishment of Special Service Staff

The Special Service Staff, Collection Division, Office of Assistant Commissioner (ACTS), is hereby abolished.

Section 4. Effect on Other Documents

IRM 1113. 654 is revoked and Exhibit 1113-5 is amended. This "effect" should be noted in pen and ink on the text and Exhibit with a deference to this Supplement.

The following Manual Supplements dated April 12, 1973, are revoked: 51G-93, CR 1(16)G-18, CR 42G-300, CR 5(17)G-85, CR 93G-133, CR (10)4G-3, and CR (11)6G-70.[1]

DONALD C. ALEXANDER,
Commissioner.

8. What types of "activist" organizations were within the purview of this group? How was "activist" defined? Were any exempt organizations the subject of the information-gathering activities of this group?

In general, the types of "activist" organizations that were within the purview of Special Service Staff were those categorized as extremists on the right or on the left.

Although no formal definition of the term "activist" was ever adopted, the organizations included those which could be classified (1) violent groups advocating revolution against the Government of the United States; (2) nonviolent groups, and (3) stated tax resisters.

Exempt organizations were the subject of the information-gathering activities of the Special Service Staff, particularly where the Staff had information that the organization may not have been complying with the conditions of its exemption.

9. Would you clarify your statements during the Subcommittee's June 3 *hearing* that:

(*a*) ". . . the Internal Revenue Service . . . has not been in the business of selective enforcement."

(*b*) ". . . I do not think the processes of the Internal Revenue Service were being abused by its engagement in selective enforcement."

These statements both mean the same thing, namely, that the Internal Revenue Service has not been engaged in selective enforcement. In other words, the Service followed regular procedures in determining what audits were necessary from a tax administration viewpoint.

10. What criteria were used by the Special Service Staff in selecting the organizations from which it gathered information? Would you supply the Subcommittee with any memoranda which defined these criteria?

There were no established criteria or memoranda used by the Special Service Staff for the selection of organizations about which it gathered information. Usual standards for referring items from the field were employed. Such matters as the following were considered: failure to file required returns, failure to report all items of income, claiming of erroneous deductions or exemptions, or engagement by an organization in nonexempt activity. In other words, as pointed out in the July 29, 1969, memorandum attached to our reply to question (6) above, the Special Service Staff's purpose in collecting information was to check on compliance with the tax laws.

11. Was the information collected by the Special Service Staff turned over to any other person, agency, office or other source than your field audit personnel, or did any other person, agency, office or other source, other than personnel of the Internal Revenue Service have access to this information? If so, who did receive or have access to this information?

The information collected by the Staff was not, as such, distributed to any person, agency, office or source other than to IRS personnel having official responsibility for using such information. However, as with any IRS records, the Justice Department and other agencies had access to this information. In particular, our records show that the Assistant Attorney General, Internal Security Division, Department of Justice, specifically requested access to the information collected by the Special Service Staff. His authority for such access is contained in 26 CFR 301.6103(a)-1 (g) and (h), Treasury Department Regulations. In all, that office made 99 requests for the calendar years 1969 through 1973.

12. During your June 3 testimony, you stated that the Special Service Staff received information from the "Senate of the United States." Would you amplify this statement?

The Staff of the Senate Permanent Subcommittee on Investigation of the Committee on Government Operations initially contacted the Internal Revenue

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[1] Related annotations should be removed, with a reference to this Supplement, from IRM 1(16)41, Physical and Document Security Handbook; IRM 4260; IRM 5100; 100 of IRM 5(17)00, IDRS Handbook; IRM 9370; IRM (10)400; and IRM (11)671, Exempt Organizations Handbook. (At IRM 9370, remove reference to CR 93G-134, shown in error instead of CR 93G-133.)

Service in 1968 and inquired as to what action the Service was taking in regard to certain organizations. From these contacts, meetings were held, the outcome of which was the formation of the Activist Organization Committee. The Subcommittee Staff offered any help that they could give to the Service, such as information in their files and published hearings as mentioned above.

13. By what means did the Special Service Staff get information?

The Special Service Staff obtained information from:

1. Excerpts from public hearings held by the Senate Permanent Sub-Commitee on Investigations of the Committee on Government Operations, Senate Subcommittee to Investigate the Administration of the Internal Security Act and other Internal Security Laws of the Committee on the Judiciary, and the House Committee on Internal Security.
2. Newspaper and magazine clippings
3. Reports from the Federal Bureau of Investigation
4. Department of Justice
   (a) Inter-Departmental Information Unit
   (b) Internal Security Division
5. Social Security Administration—Wage and Earnings Division
6. Internal Revenue Service reports showing tax return filing and payment history.
7. Files of various other functions within the Internal Revenue Service.

The information was secured by making requests through established channels. Also, some unsolicited information was made available to the Special Service Staff.

14. Since 1969, has the White House requested the tax returns of any private foundation or other exempt organization?

Returns of exempt organizations are generally available for public inspection under section 6104(b) of the Code and the applicable regulations. The affiliation of the requester is not pertinent to being able to inspect these types of public returns. It is asked for informational purposes, but it is not insisted upon. We have no centralized, nation-wide record of requests for public inspection. However, from a check of our available record of requests made in the National Office Public Affairs Division, which is the National Office contact point prescribed in the regulations for making such requests, we have not found any requesters identifying themselves as being from the White House.

15. Was there any effort within the Internal Revenue Service to rank foundations on the basis of their "political leanings"? Did any personnel within the Service provide assistance to any other government official or employee which would have enabled such a ranking to be prepared?

No individual or group that we know of in Internal Revenue has ranked a foundation, exempt organization, or other taxpayer on the basis of political leanings. In considering the qualification under section 501(c)(3) for exemption from Federal income tax of a religious, educational, scientific, literary, or other charitable organization, the Service may find it relevant to inquire whether or not the organization engages in political or legislative activity. This inquiry is pertinent because the governing statues and regulations limit the extent to which a qualified charitable organization may engage in political or legislative activities. However, any such inquiry concerns itself only with the questions of whether, and to what extent, the activity is carried on. The kind of political or legislative views espoused is immaterial, and we have no interest in such information.

As mentioned in question (8), the Special Service Staff did collect information about certain types of organizations including some foundations. At all times, the Special Service Staff's interest in any organization about which it collected information was with possible violation of the tax laws. Also, as noted in our transmittal memorandum, this matter is one which will be reviewed in a report to be issued by the Senate Judiciary Committee's Subcommittee on Constitutional Rights.

THE DEPARTMENT OF THE TREASURY,
Washington, D.C., July 16, 1974.

Hon. VANCE HARTKE,
U.S. Senate,
Washington, D.C.

DEAR SENATOR HARTKE: Attached in question and answer format is the list of questions you sent me on July 1, 1974, together with the corresponding answers.

These answers are submitted for inclusion in the record of the June 8 hearings of the Subcommittee on Foundations.

Sincerely yours,

FREDERIC W. HICKMAN.

Attachments.

PRIVATE FOUNDATION HEARINGS

1. The letter attached * from Secretary Simon reiterates the position of the Treasury Department that the 4 percent excise tax on private foundations be reduced to 2 percent.

a. Does Treasury support any specific legislative proposals to accomplish this purpose?

b. What is the position of the Treasury Department on the earmarking of the excise tax revenues for purposes of auditing exempt organizations by the Internal Revenue Service?

c. What is the Treasury Department's revenue projection for the 4 percent excise tax in fiscal year 1974?

Answer. The Treasury Department has not presented any specific legislative proposal for changing the 4 percent excise tax on private foundations. As indicated in Secretary Simon's June 3 letter, we do support the reduction of the 4 percent tax to 2 percent, and we would be glad to work with the Ways and Means Committee and the Finance Committee to develop specific statutory language for effecting that result.

In determining the appropriate level of the excise tax as an audit tax, it is obviously relevant and necessary to look to actual levels of expenditure and revenue collection. We are opposed, however, to earmarking the excise tax revenues for exempt organization audit purposes. The level of expenditures for the audit of exempt organizations should be a function of overall audit priorities and available manpower and resources for all audit activity, and the extent to which exempt organizations are audited should not be artificially limited or expanded solely because of fluctuations in excise tax revenue collections.

In the budget for fiscal year 1975, we projected that private foundation taxes would bring in $80 million in both fiscal 1974 and fiscal 1975. Substantially all of this would come from the 4 percent excise tax. Because of the short experience we have had with the tax and because the revenues raised by it may be greatly affected by the amount of capital gains realized by private foundations, the actual revenues collected may vary significantly from the amount projected.

2. During hearings held by the Subcommittee on Foundations last October, witnesses suggested a modification in the minimum payout requirements of the Internal Revenue Code, as they apply to private foundations.

a. Does the Treasury Department believe it to be appropriate to modify this requirement?

b. If so, what suggestions does the Treasury Department have for modifying this requirement?

Answer. Section 4942 of the Internal Revenue Code imposes an excise tax on the failure by a private foundation to make required distributions for charitable purposes. The required distribution is the greater of the foundation's actual adjusted net income or a constructive income equivalent (minimum investment return), reduced by the income taxes and the 4 percent excise tax paid by the foundation. For the 1970 taxable year, the minimum investment return, which establishes the minimum distribution requirement, was set at 6 percent by the Tax Reform Act of 1969; and the Secretary of the Treasury was authorized to alter that rate for subsequent years in light of changing money rates and investment yields.

The 6 percent standard set by the 1969 Act was the result of a Senate floor amendment, the House bill having adopted the Administration's recommendation that the minimum distribution requirement be set at 5 percent. During the last Congress, the Ways and Means Committee reported H.R. 11197, which would have reduced the minimum distribution requirement to 5 percent. The Treasury Department supported enactment of that bill.

We are continuing to study the impact of the 1969 Act minimum distribution requirement but have no further suggestions to make at this time.

3. The Subcommittee on Foundations has received numerous communications from small organizations which have been classified as private foundations. The

*See p. 404.

thrust of these communications is that various provisions of the Internal Revenue Code, as they apply to private foundations, place onerous burdens on small foundations.

a. Does the Treasury Department have any recommendations for modifications in the law which would relieve small foundations from these burdens?

Answer. The Treasury Department has also received a number of communications respecting the impact of the private foundation provisions on small foundations. In large part, these communications complain about the effect of the 4 percent excise tax and the minimum distribution requirement in forcing depletion of a foundation's corpus. Our comments on the first two questions would be equally applicable here. The small foundations have also voiced complaints respecting the detailed reports and records required by the 1969 Act. We are mindful of these complaints and are attempting to keep these requirements as simple as possible. It should be noted, however, that most private foundations are small. In its 1974 annual report, Giving USA, the American Association of Fund-Raising Counsel estimates that only about one-fifth of all foundations have assets of at least $500,000 or make annual grants of $25,000 or more. Application of the self-dealing, tax expenditure, and excess business holdings provisions to the 80 percent of foundations that are small foundations is essential if the purposes of the 1969 legislation are to be achieved.

4. The June 4 hearings of the Subcommittee on Foundations demonstrated that the Internal Revenue Service does not analyze information which would give the Congress and members of the public an opportunity to assess the impact of the Tax Reform Act of 1969 on private foundations. For instance, there is no information on the impact of the minimum distribution requirement on the amount of private foundation funds going to charitable purposes. (For other examples, see the written response of Commissioner Alexander to questions propounded by Senator Hartke.)

a. What suggestions does the Treasury Department have for improving the data collection process within the Internal Revenue Service so that Congress can make an informed judgment on the benefit which the public receives in return for the tax exempt status accorded foundations?

Answer. The Internal Revenue Service's long-range program of special statistical studies is designed to provide the maximum amount of useful information for purposes of tax policy formulation, given budgetary limitation on manpower and resources. A special study scheduled for the 1974 statistics of income will analyze the private foundation returns (Form 990-PF), including the schedule on minimum distributions. Of course, this study will not be available for some time, as 1974 returns will not be filed until 1975. In any event, such analyses do not always permit us to answer all of the relevant questions that policymakers might pose. For example, it would be very difficult to appraise the impact of the minimum distribution requirement on the amount of private foundation funds going to charitable expenditures, since it will be impossible to know what charitable expenditures would have been absent enactment of the minimum distribution provisions. Judging from the number and intensity of comments respecting the minimum distribution requirement, we may, however, be assured that the impact has been very considerable. Finally, we would note that we are not limited in our sources of information to the statistical activities of the Federal Government, and we are hopeful that much needed information on charitable activities will result from the work of the Commission on Private Philanthropy and Public Policy, which was formed last fall with the encouragement and cooperation of the Treasury Department.

THE SECRETARY OF THE TREASURY,
Washington, D.C., June 3, 1974.

Hon. VANCE HARTKE,
U.S. Senate,
Washington, D.C.

DEAR SENATOR HARTKE: For the record of the hearing on private foundation matters, we submit the following statement of the position of the Treasury Department regarding the 4 percent tax on private foundation investment income.

The tax on private foundation investment income was enacted as part of the private foundation provisions of the Tax Reform Act of 1969. The House bill

provided for a 7½ percent tax. The 7½ percent figure was justified by some as equal in amount (though unrelated in logic) to the net tax on intercorporate dividends. The legislative history indicates that the supporters of the 7½ percent tax looked upon it not as an audit fee but rather as a species of minimum tax. It was intended by them to generate tax revenue from private foundations.

The Treasury Department recommended to the Senate Finance Committee that in lieu of such a revenue-raising levy, a supervision tax be imposed to offset the cost of administering the audit program for foundations. We estimated that 2 percent of net investment income would be sufficient for that purpose. The Senate bill contained a tax based on the value of foundation assets (as distinguished from income) calculated to raise approximately half as much revenue as the House bill's 7½ percent tax. The Conference Committee compromised the divergent House and Senate positions by adopting the present 4 percent tax on income, which was expected to raise revenue roughly equivalent to the Senate bill.

While we have collection data for only a limited period, the available data indicate that the revenues raised by the 4 percent tax greatly exceed the cost of auditing private foundations. The cost of administering the tax provisions relating to all exempt organizations is about $21 million with the larger part allocable to the program for private foundations. Collections from the 4 percent tax on private foundation investment income totaled about $24.6 million in fiscal year 1971, $56 million in fiscal year 1972, and $76.6 million in fiscal year 1973. There is reason to believe that the $76.6 million is abnormally high, including a large amount of non-recurring capital gain. Further, there is some reason to expect that private foundations will contract in the aggregate with a resulting tendency for total revenues to diminish. These data suggest that a 2 percent tax might be an appropriate amount to defray the cost of the private foundation audit program, and we would support a measure to reduce the tax from 4 percent to 2 percent.

Sincerely yours,

William E. Simon
(Signed) WILLIAM E. SIMON,
Secretary.

OCTOBER 9, 1973.

Hon. DONALD ALEXANDER,
Commissioner, Internal Revenue Service,
Washington, D.C.

DEAR COMMISSIONER ALEXANDER: In the course of recent hearings of the Subcommittee on Foundations, two areas were discussed where we found information to be lacking.

The first is the amount of tax revenues which have been lost because of the tax-exempt status of foundations. The second relates to the geographical breakdown of foundation grants.

Any assistance which you can provide the Subcommittee in finding this information would be most appreciated.

With best wishes, I am

Sincerely,

VANCE HARTKE,
Chairman, Subcommittee on Foundations.

DEPARTMENT OF THE TREASURY,
INTERNAL REVENUE SERVICE,
Washington, D.C., October 25, 1973.

Hon. VANCE HARTKE,
Chairman, Subcommittee on Foundations, Committee on Finance, U.S. Senate,
Washington, D.C.

DEAR MR. CHAIRMAN: This is in further response to your letter of October 9, 1973, requesting information as to the amount of tax revenues lost because of the tax exempt status of foundations and also the geographical breakdown of foundation grants.

A geographical breakdown of data on foundation grants is not available from Internal Revenue Service records. Although the names and addresses of recipients of foundation grants are reported on Form 990-AR, Annual Report of

Private Foundations (or optional equivalent form), this information is not input into our computer system because of the costs involved. The information is available on the return for use in case of audit, but we have not felt that compilation of such statistics would be sufficiently useful for our purposes to warrant the additional costs involved.

Some information on foundation grants, however, is published by The Foundation Center. The enclosed table, abstracted from the Foundation Directory, Edition 4, 1971, provides a breakdown of foundation grants classified by the State in which the foundation is located. We are not aware of any statistical compilation of grants classified according to the geographic location of the recipient.

Two limitations on the data in this table should be noted. First, the table does not include data for small foundations, since the Directory (Edition 4) is limited to foundations which made grants of $25,000 or more, or possessed assets of $500,000 or more. Second, the data relate primarily to 1968 and 1969 and therefore do not reflect any impact of the Tax Reform Act of 1969.

Since the Office of Tax Analysis has sole responsibility in the Treasury Department for preparation of revenue estimates, I am sending a copy of your letter to Assistant Secretary Hickman so that his office can provide you with an estimate of the tax revenue lost because of the tax exempt status of foundations.

With kind regards,

Sincerely,

DONALD C. ALEXANDER.

Enclosure.

GRANTS OF 5,454 FOUNDATIONS, BY REGIONS AND STATES

Place	Number of foundations	Grants (thousands)
New England	436	$63,588
Maine	15	961
New Hampshire	16	2,278
Vermont	4	103
Massachusetts	244	28,881
Rhode Island	33	3,858
Connecticut	124	27,508
Middle Atlantic	1,875	838,572
New York	1,409	729,175
New Jersey	139	22,232
Pennsylvania	327	87,164
East north-central	1,177	276,627
Ohio	364	74,781
Indiana	78	20,963
Illinois	389	78,112
Michigan	206	86,382
Wisconsin	140	16,388
West north-central	363	69,735
Minnesota	142	31,829
Iowa	40	3,815
Missouri	128	28,288
North Dakota	1	29
South Dakota	2	44
Nebraska	22	3,738
Kansas	28	1,992
South Atlantic	558	99,275
Delaware	56	17,776
Maryland	75	7,254
District of Columbia	51	8,866
Virginia	53	4,861
West Virginia	8	175
North Carolina	100	22,343
South Carolina	32	8,269
Georgia	107	22,869
Florida	76	6,862
East south-central	107	12,029
Kentucky	26	2,541
Tennessee	55	6,450
Alabama	20	2,215
Mississippi	6	824
West south-central	362	67,631
Arkansas	20	1,103
Louisiana	37	3,225
Oklahoma	57	7,614
Texas	248	55,689
Mountain	99	16,755
Montana	5	237
Idaho	8	616
Wyoming	3	410
Colorado	43	9,468
New Mexico	5	133
Arizona	14	574
Utah	16	1,028
Nevada	5	4,289
Pacific	475	69,152
Washington	43	5,823
Oregon	39	4,117
California	380	56,600
Hawaii	13	2,612
Outlying areas	2	79
Puerto Rico	1	40
Virgin Islands	1	39
Total	5,454	1,513,442

Note: Detail may not add to totals because of rounding.

Source: The Foundation Directory, ed. 4, 1971, pp. x-xi.

OCTOBER 30, 1973.

HON. DONALD ALEXANDER,
Commissioner, Internal Revenue Service,
Washington, D.C.

DEAR COMMISSIONER ALEXANDER: Thank you for your letter of October 25. I am dismayed that the Internal Revenue Service is unable to provide a geographical breakdown of foundation grants. This is important information which would be most helpful to my Subcommittee on Foundations.

After reading your letter, certain questions come to mind.

First, what information on foundations is input into your computer system?

Second, what would be the estimated cost of adding foundation grant recipients and their addresses to your computer input?

Third, since it has been reported that the tax collector from foundations is $56 million and the costs of auditing private foundations were less than $13 million, could not some of the surplus be used to pay the cost of adding the recipient information to your computer input?

I appreciate your taking the time to answer thses questions. With best wishes, I am

Sincerely,

VANCE HARTKE,
Chairman, Subcommittee on Foundations.

DEPARTMENT OF THE TREASURY,
INTERNAL REVENUE SERVICE,
Washington, D.C., December 6, 1973.

COMMISSIONER

HON. VANCE HARTKE,
Chairman, Subcommittee on Foundations, Committee on Finance, U.S. Senate,
Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your letter of October 30, 1973, requesting information regarding input of certain foundation data to our computer system.

The Service has established an ADP Exempt Organization Master File (EOMF) System to assist in carrying out its responsibilities for administering the exempt organization provisions of law and monitoring compliance with these provisions. Under this system there is a magnetic tape record for each organization reflecting basic entity data (see enclosed Form 3936, Exempt Organization Master File Addition Voucher, for input data elements) and a separate magnetic tape record for certain tax return data. The tax return data presently input to the EOMF are as follows:

Gross Dues and Assessments.
Gross Contributions, Gifts and Grants.
Gross Receipts from Other Sources.
Expenses Attributable to Gross Income.
Disbursements for Other Purposes.
Total Assets.
Total Liabilities.
Return Activity Codes.
Net Investment Income.
Tax on Net Investment Income.

In addition, the following tax return data elements will be input to our EOMF for processing year 1974:

Fair Market Value of Assets.
Qualifying Distributions.
Undistributed Income.

It is estimated that the cost of adding foundation grant recipients and their addresses to our master file system would be $100,000 start up costs for system design and programming, and $200,000 annual operational cost for editing, key punching, additional run time of expanded master file, etc. Therefore, the first year costs would be $300,000 with annual recurring costs of $200,000.

With regard to your question about surplus funds, none of the revenue from the four percent tax is directly applied to funding the Internal Revenue Service.

That revenue goes to Treasury as part of the general fund. IRS expenses related to private foundations are covered within the Service's annual budget appropriated by Congress.

With kind regard,

Sincerely,

DONALD C. ALEXANDER.

Enclosure.

ADDITIONAL LINE ITEMS, 1973, FORM 990-PF

Description	Reference	Comment
(1) Adjusted net income: Before deductions	Pt. I: Line 13(C)	Gives a better picture of current yield on foundation investments.
After deductions	Line 25(C)	Provides comparison with minimum investment return.
(2) Net capital gain	Pt. I, line 8(B)	Would provide some measure of how much capital gains are responsible for 4 percent tax yield, and some measure of 4,942 and 4,943 effects.
(3) Contributions, etc. paid	Pt. I, line 23(D) or line 23(A).	Excludes administrative expenses attributable to exempt purposes. Actually measures amounts paid to recipient organizations. The difference between this item and line 24(D) is the only way to obtain a figure for administrative expenses allocable to program.
(4) Minimum investment return	Pt. IX, line 6 or line 7	Valuable comparison with adjusted net income. Will it possible to break out operating foundations? If so, this would give us a numerical count of new and old foundations.
(5) Distributable amount	Pt. VIII, line 7	Valuable comparisons with qualifying distributions, adjusted net income, net investment income and undistributed income.
(6) Total receipts as per books	Pt. I, line 13(A)	Gives overall picture of foundation receipts.
(7) Foundations making grants to individuals or expenditure responsibility grants.	Pt. V, N(1)(c) and (d)	Total number of yes answers to each of these questions would give some measure of the effect of TRA program restrictions.
(8) Organizations filing form 4720 with form 990-PF.	Form 4720 actually filed	Identification of these organizations in data bank will provide a means for compiling information about penalty taxes, problems caused by TRA previsions and so forth, as needed from time to time.

FEBRUARY 12, 1974.

Hon. DONALD C. ALEXANDER,
Commissioner, Internal Revenue Service,
Washington, D.C.

DEAR COMMISSIONER ALEXANDER: Thank you for your letter of December 6.

I asked my staff to analyze the information contained in your letter and to make recommendations of other information which the IRS might place into the ADP Exempt Organization Master File (EOMF).

The staff recommendations together with the reasons for such are enclosed. I would appreciate your comments.

With my best wishes, I am

Sincerely,

VANCE HARTKE,
Chairman, Subcommittee on Foundations.

Enclosure.

DEPARTMENT OF THE TREASURY,
INTERNAL REVENUE SERVICE,
Washington, D.C., April 12, 1974.

Hon. VANCE HARTKE,
Chairman, Subcommittee on Foundations, Committee on Finance, U.S. Senate,
Washington, D.C.

DEAR MR. CHAIRMAN: We have carefully reviewed your staff's recommendations for additional input into the EOMF.

On establishing the EOMF, we considered all line items from the return, including those your staff recommended. We gave primary consideration to those items which would directly assist us in carrying out our responsibilities for administering the exempt organization provisions of the law and for monitoring compliance with those provisions. Since the system is designed to provide data on a continuing basis, we did not want to compile information which would not serve a direct use in the administration of the statutes.

We estimate that under current conditions the cost of adding your staff's recommendations to our master file system would be at least $50,000 start up costs for system design and programming, and at least $10,000 annual operational cost for editing, key punching, additional run time of an expanded master file, etc. Therefore, the first year costs would be at least $60,000. Because of this cost factor and the lack of direct use of such information on a regular basis to the Service, we do not believe it practical to add the recommended items to our EOMF at this time.

Periodically, we review the EOMF system and reconsider our program needs. In addition, the Service has undertaken several statistical studies to provide other data, on a one-time basis, about the operations of exempt organizations.

These studies, which are in various planning stages, are intended to provide information about the characteristics of exempt organizations and the effectiveness of the governing statutes. In connection with our EOMF and these studies, we assure you that we will give full consideration to your staff's recommendations.

With kind regards,

Sincerely,

DONALD C. ALEXANDER.

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