

These striking illustrations of foundation participation in business are not isolated phenomena, peculiar to a limited group of very unusual private foundations. On the contrary, the available information indicates that the involvement of foundations in business activities is frequent. Of approximately 1,300 private foundations recently surveyed by the Treasury Department, about 180 reported ownership of 10 percent or more of at least one class of the outstanding stock of a corporation. One hundred and nine foundations in this group own 20 percent or larger interests;¹² 40 hold 100 percent interests. Forty-three foundations reported that they possess 10 percent or larger interests in two or more corporations. A recent report on foundations states that, of 543 foundations studied, 111 owned 10 percent or more of at least one class of stock of a corporation.¹³ Together these 111 foundations held interests of not less than the described magnitude (most were in fact considerably larger than 10 percent) in 263 separate corporations. In other cases, of course, foundations own and operate businesses directly.¹⁴

(2) *Evaluation*

Examination of any broad sampling of the commercial ventures of foundations reveals that several kinds of undesirable results frequently follow from them. In the first place, taxable businesses are often placed at a serious competitive disadvantage. Congress recognized this problem in 1950, and, by the Revenue Act of that year, aimed at solving it. The statute which resulted subjects the so-called unrelated business income of foundations and certain other exempt organizations to tax at ordinary rates and removes the immunity formerly enjoyed by "feeder" organizations—entities primarily engaged in business, whose sole claim to exemption is the turning over of profits to exempt entities.

Fourteen years of experience under these rules, however, has demonstrated that organizations which pay careful heed to the exceptions prescribed by the 1950 act and retained in the 1954 code can frequently shield their commercial enterprises from tax. Because of the fact that the unrelated business income tax does not, for example, apply to rents derived from property with respect to which the lessor has no outstanding indebtedness, foundations are able to lease business assets owned free of debt to operating subsidiaries, siphon off most or all of the business profits by means of rent which is deductible by the subsidiary but not taxable to the parent foundation, and thereby accumulate large reservoirs of untaxed capital which can be used to support the future operations of the business. Another exception to the unrelated business income tax immunizes rents stemming from a lease whose term is not longer than 5 years even if the lessor has an outstanding indebtedness with respect to the leased assets. The C foundation, referred to in example 3, is typical of the private foundations which have tailored their acquisitions of businesses to make use

¹² Further information about the business ownership of those of these foundations which have assets valued in excess of \$10 million is set forth in Appendix A.

¹³ Patman Report, 1st installment, *supra*, p. 8.

¹⁴ The transfer of businesses to foundations and other exempt organizations has been encouraged by decisions of several courts that, under the arrangements ordinarily employed for these transfers, the transferors are entitled to treat the proceeds which they receive as capital gains. E.g., *Union Bank v. United States*, 285 F. 2d 126 (Ct. Cls.); *Anderson Dairy, Inc. v. Commissioner*, 40 T.C. 172; *Commissioner v. Brown*, 325 F. 2d 313 (C.A. 9th). The Supreme Court now has under consideration the question of whether or not, after such a transaction, the former owners of the business receive capital gains treatment where the exempt organization makes no downpayment other than from the assets of the business itself, has no fixed personal obligation to pay a purchase price, and is required simply to turn over a specified proportion of the future earnings of the business. *Commissioner v. Brown*, *supra*, certiorari granted June 8, 1964. Whatever the outcome of that case, however, it seems clear that substantial inducements for the transfer of businesses to foundations will remain.