

62 TREASURY DEPARTMENT REPORT ON PRIVATE FOUNDATIONS

The Treasury Department is of the opinion that the recommendation of the Ways and Means Committee Advisory Group is a sound one. Restriction of the charitable deduction which a donor receives on the contribution of section 306 stock to a private foundation⁵ is consonant with the particular concern which Congress has, by the adoption of section 306, manifested for the earnings bailout problem. Measuring the reduction in the allowable charitable deduction by the amount of the ordinary income upon which the donor would have been taxed if he had sold the contributed stock makes the approach consistent with the provisions of section 306 itself. Furthermore, this approach is precisely that which Congress recently twice applied to analogous problems. In its 1962 enactment of section 1245 of the Internal Revenue Code, providing rules to insure ordinary income treatment of gain attributable to post-1962 depreciation of tangible personal and certain other property, and in its 1964 enactment of section 1250, prescribing rules of broadly the same direction for depreciable real property, Congress took care to specify that deductions for charitable contributions of such property should be diminished by the amounts which the new sections would characterize as ordinary income if the property were sold at fair market value.⁶

For these reasons, the Treasury Department recommends application of the Advisory Group proposal to contributions of section 306 stock to private foundations.

(2) *Other ordinary income assets*

When donors secure deductions for contributing to private foundations other classes of property which would have produced ordinary income upon sale, problems fundamentally analogous to those present in the section 306 stock context arise. Items includible in the donor's inventory and stock in collapsible corporations afford examples. In all of these cases the full amount of value which the donor would normally have had to include in his ordinary income is permitted both to escape taxation itself and to reduce the amount of his other taxable income. In many of these situations there exists the same anomaly pointed out above in connection with section 306 stock: the donor can make more profit by giving the asset to a foundation than he would have been able to retain if he had sold it.

Because of the basic similarity of the present problems to those generated by section 306 stock and because of the direct relevance here of the recent congressional action on the closely related ordinary

⁵ The Advisory Group proposal is not limited to situations in which the recipient charitable organization is a private foundation: the group's recommendation would apply wherever a donation of sec. 306 stock gives rise to a charitable deduction. The American Law Institute Tax Project working view and Professor Bittker's discussion, similarly, treat the problem as one whose nature does not depend upon the character of the charitable organization involved. By its observation that the problem exists within the area to which the present report applies, the Treasury Department intends no implication that these views are in error.

⁶ The American Bar Association in 1959 offered two objections to the Advisory Group proposal. Hearings on Advisory Group recommendations on Subchapters C, F, and K of the Internal Revenue Code, House Ways and Means Committee, 86th Cong., 1st sess., pp. 923, 931-933 (1959). One, advanced by some members of the Committee on Corporate Shareholder Relationships, was that the contribution of sec. 306 stock to charity represents only one facet of the broad problem presented by donations of appreciated property. The members who entertained this view were of the opinion that all aspects of the general question should be examined before action is taken upon any particular portion of it. This objection has, in a large measure, been undercut by the congressional decisions with respect to secs. 1245 and 1250. In both instances, Congress recognized that specific restriction of the charitable deduction affords an appropriate method of dealing with the problems posed by particular classes of assets. A second objection, made by other members of the Bar Association committee, was that the proper method of curbing abuses in this area is to grant a full charitable deduction for the donation of sec. 306 stock, but to tax the donor as though he had realized the entire fair market value of the stock at that time. Such a rule would be more stringent than that recommended by the advisory group: it would, like the Advisory Group proposal, cancel that portion of the donor's charitable deduction attributable to corporate earnings at the time of the distribution of the stock; but, in addition, it might occasion a capital gains tax where the stock has appreciated in value after its distribution to the donor. Without passing on the merits of this proposal, the Treasury Department is of the view that the less rigorous approach of the Advisory Group is sufficient to foreclose the sec. 306 stock abuse in the private foundation area.