Measures to increase financial support for universities and discourage investments which might jeopardize the tax-exempt status that educational institutions now enjoy have been recommended by the Association of American Universities, Dr. Henry M. Wriston, President of Brown University and of the association, announced today.

Discussing the economic problems raised by steadily increasing costs of operation and the decrease in returns on endowments which have caused widespread financial distress in universities, Dr. Wriston cautioned universities in search of acutely needed new sources of revenue to avoid investments which might place them in the position of taking improper advantage of their tax-free status. The amount of such "loophole" investments has been grossly exaggerated, said Dr. Wriston, and the effect on tax revenue has been negligible.

The recommendations are based on the report of a committee of the association, which includes 37 leading American and Canadian educational institutions, which has just completed an intensive study of financial and taxation problems. The members of the committee were President James R. Killian, Jr. of the Massachusetts Institute of Technology, chairman; President Colgate W. Darden, Jr. of the University of Virginia; President Harold W. Dodds of Princeton University; President Theophilus S. Painter of the University of Texas; and President Harold E. Stassen of the University of Pennsylvania.
In presenting the report, Dr. Killian, chairman of the committee, emphasized the committee's disapproval of tax-free ownership of mercantile and manufacturing businesses by educational institutions when such activities are unrelated to the purposes of education.

Emphasizing that the future financial stability of universities is dependent upon exemption from taxation on income or property used for educational purposes, the committee warned that "any impairment of the long-standing principle of tax exemption would be a fatal blow to the educational system."

The critical need, the committee reported, is for positive measures to conserve and increase the income and resources of those institutions if they are to meet the educational needs of the youth of the nation. It stressed the importance of a government tax policy which will not only protect university resources, but stimulate increased support through private philanthropy.

The committee recommended that the Association of American Universities take vigorous measures to defend the fundamental tax exemption principle and to support changes in the revenue laws which would encourage private philanthropy.

The report, Dr. Wriston said, seeks to set up an investment policy which would provide revenue and at the same time avoid investments which might be construed as unfair competition with tax-paying organizations.

In making its recommendations the committee reported its belief, "that in addition to investing its funds, it is proper for an educational institution to carry on a variety of other activities which primarily serve its students and members. Such activities aid the educational objectives of the institution and cannot properly
be distinguished from the over-all operations of the institution. The committee believes that it is impractical, if not impossible, to segregate these activities. If the educational institution is to continue to be exempt from income tax, it must be wholly exempt from such taxes, and any effort to tax one part and not another places in jeopardy the whole principle of tax exemption.

Discussing the problem of ownership and operation of business and commercial enterprises by educational institutions, the committee warned against transactions in which tax exemption might be claimed for an organization which would ordinarily be subject to taxation.

"The committee believes, however, that a different situation arises when a manufacturing or mercantile business is carried on by a separate corporation or trust which would certainly not be entitled to tax exemption if all its property and income were not dedicated to some university and when such manufacturing or commercial business has no significant connection with the educational or scientific work of the university other than the attribute of producing income for the university.

"It is sound policy," the committee believes, "for a university not to seek tax exemption for such a separate entity; and not to enter into a transaction involving such a separate entity if the advantage of the transaction depends upon the separate entity being free of federal income tax."

If those conditions are satisfied, the report continued, "the university should then continue to be free from income tax on the dividends or other distributions of income by such separate entity just as the university is free from income tax on other income.

(more)
"The committee believes that the taxation of such separate entities would cover practically all the business investments which have been subject to criticism. Few boards of trustees of a university would be willing to accept the liability which would be involved if such business enterprises were to be owned directly by the university, rather than by a separate corporation or foundation. If there should be any change in the revenue laws designed to tax such business operations, it should not be aimed at the university which receives income from the separate entity. Any effort to tax the university or some part of it would violate the tax exemption principle."

Although the committee believes that "a university should not be subject to tax on any earnings which it may derive from an operation carried on directly by the university, nevertheless the committee believes it is neither proper nor in the public interest for a university to carry on directly any manufacturing or mercantile business having no significant connection with the educational or scientific work of the university other than the attribute of producing income for it.

"The committee believes that an educational institution should continue to be free from income tax on rents and royalties from its interests in real estate."

There has been criticism of transactions, said the report, in which an educational institution has directly or indirectly bought a business plant and leased it back to the seller. The committee believes that "many such transactions are unobjectionable. It may often be wise for a company to sell its plant to acquire cash and the sale may not be possible unless the seller leases back the (more)"
plant either because the seller needs occupancy for a period or because no buyer would pay the price if the plant had no tenant. There is no more objection to a university than to anyone else becoming the owner of such a plant. The exemption of the university from income tax on the rental received does not differ from its exemption from income tax on dividends or on rentals from other real estate. Any sound basis for criticism must rest on some special aspect of the particular transaction other than the tax-exempt status of the buyer.

"To avoid jeopardizing the larger interests involved, the committee believes that it is wise for a university to refrain from purchasing property directly or indirectly in a transaction in which such property, or the real estate portion thereof, is to be leased back to the seller with an option in the seller to repurchase the property; and that it is also wise to refrain from directly or indirectly making such a purchase and lease-back in a transaction in which the university supplies no substantial part of the purchase price from its funds other than funds received in the transaction or from money borrowed on the specific transaction."

The committee recommended that the association take action to secure a change in the federal income tax law permitting the deductible charitable gifts of an individual in any year to be free of the present 15 per cent limit. The report also urges that universities seek the enactment by various states of amendments to their corporation laws authorizing business corporations to make charitable donations.

"Universities should take such action as they deem appropriate," the committee believes, "to obtain an amendment of the federal income tax law so that charitable corporate gifts within the
present five per cent limit instead of being deductible on the tax return of the donor corporation, should to the extent of 50 per cent of the gift, be a credit against the corporate tax." The deduction at present allowed in effect reduces the tax by 38 per cent of the gift.