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Gift of Appreciated Property. Proposed project. 2 March 1966.

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PAUL, SHWAYDER & WEINSHIENK  
Attorneys at Law

OFFICE MEMORANDUM

Date: March 2, 1966

Subject: Gifts of Appreciated Property  
to the UJA

Rabbi Herbert Friedman,  
To: National Executive Board--UJA,  
Proposed Participants  
From: Paul, Shwayder & Weinshienk  
(H. Michael Miller, Bruce B. Paul)  
cc:

AMERICAN JEWISH  
PROPOSED PROJECT

The following plan is proposed to facilitate charitable gifts to the UJA, which will maximize the tax advantages to the donor with minimal or no dollar costs to him. The purpose is to increase the volume of gifts of appreciated property by making the mechanics easier: use of simplified techniques may increase the amount of giving in many communities. The following figures, of course, are used only for illustration. If the concept works after a trial period, the project may be considerably broadened.

It is proposed that five individual donors will each make a \$10,000 investment in a common pool. The \$50,000 can be financed by means of personal bank loans rather than using the participants' cash. The \$50,000 will then be invested for trading purposes in the stock market. It is suggested that the \$50,000 pool be managed by a professional investment broker skilled in managing such funds. The objective of this fund will be to realize short term appreciation. Assume, for illustrative purposes only, that the \$50,000 pool appreciates to \$75,000, sometime prior to six months from the date of organization. The fund will then be sold to the UJA at cost, or \$50,000. The participants will then have made a charitable gift to the UJA of \$25,000, the difference of the fair market value in excess of the donors' cost. In practice, trading would be done and the donation then made by means of a series of bargain-sales.

The consequences of this plan are:

- (1) The individual donors will receive a charitable deduction for their portion of the gift.
- (2) There will be no tax to the donor on the gain or appreciation of the pool's investment.

(3) The donor will have recouped his initial investment, and therefore the cost of making this gift will be zero (except for possible carrying charges if the initial \$10,000 investment was financed).

(4) The donor will have actually gained tax free dollars. Assuming the donor was in the 50% tax bracket and his share of the charitable gift was \$5,000, he would thereby have gained \$2,500 tax free or "hard" dollars as a result of the charitable deduction, which in reality was made at no cost to the donor.

(5) Losses (this should be contemplated) would be taken by the individuals on their own returns on a short term basis.

(6) Incidental expenses, such as interest, if any, and New York State Stock Transfer tax, are all ordinary expenses.

Query: can we, over time, use this device to crack Wall Street? Can giving be increased by getting the Street to compete for our business and striving to show big trading results?

Why do this? Many people now give appreciated securities--but not enough people nor enough money. We suspect the reason is that the mechanics seem too difficult. Give people an easy way mechanically, and we may be able to augment gifts of appreciated securities; we could then go on to solving the mysteries of other less liquid appreciated property.

(See attached legal authority and supporting documents for the legal and tax intricacies relating to this plan.)

## APPENDIX A

### LEGAL AUTHORITY:

The charitable contribution entitles the donor to a deduction which decreases the net taxable income. I.R.C. Section 170. Charitable contributions to the UJA are fully deductible so long as the contributions are 30% or less of the taxpayer's adjusted gross income for the year. Contributions to the UJA receive the favorable 30% maximum under I.R.C. Section 170(b)(1)(A)(vi) since the UJA "normally receives a substantial part of its support . . . from direct or indirect contributions from the general public."

### DEDUCTIONS FOR CONTRIBUTIONS OF APPRECIATED PROPERTY (STOCK):

A. The tax laws clearly provide that the donor is entitled to a charitable deduction for the full fair market value of the donated appreciated property. Reg. 1.170-1(c). Thus, if one were to make a gift of stock which has a basis of \$10,000 and a fair market value on the effective date of the gift of \$20,000, the donor is entitled to a charitable deduction in the amount of \$20,000. Furthermore, the taxpayer escapes the tax on the gain or appreciation. Rev. Rul. 55-410, 1955-1 C. B. 297. See also Law Opinion 1118, 1923-11-2 C. B. 148; Reg. 1.1001-1(e) Example (3).

B. An alternative to the outright gift of the entire appreciated property is a bargain-sale gift. This is a gift whereby the donor sells to the charity the appreciated property for a sale price equivalent to the donor's cost or basis, thereby making a gift of the excess of the fair market value of the property over the donor's cost or basis. The tax laws are likewise clear that the donor escapes the tax on the appreciation and also receives a charitable deduction for the excess of the fair market value over the cost or basis which is equivalent to the sale price. In other words, in the above example, if the donor were to sell the stock (rather than give it outright) to the charity for \$10,000, he would receive a charitable deduction for the \$10,000 appreciation and also escape the tax on this appreciation. These favorable tax consequences were confirmed in an unpublished ruling responding to an inquiry based on the above example; unpublished ruling, November 12, 1954, in a letter bearing symbols T: R: 1 RFW-3, and signed by Lester W. Utter. The same result was reached by the tax court where the question was raised in a different but analogous context. Waller vs. Comm'r, 39 T.C. 665 (1963). This case involved a donor making a bargain-sale gift to a charitable trust created by the donor. The tax court held in that case that the donor was entitled to a deduction for the charitable contribution to the trust in the amount of the excess of the fair market value over the donor's basis.

C. The effective date of the gift can be determined by the donor by means of the method used to effect transfer of the stock. To assure the donor that the value of the gift will be determined by the fair market value on the day on which the transfer is made, the donor's broker should be appointed by the charity as the charity's broker and agent as well. The fair market value will then be computed on the date on which the donor notifies his broker to transfer the stock to the charity's account. See Rev. Rul. 54-554, 1954-2 C. B. 317 and compare with 54-135, 154-1 C. B. 205.

D. The proposed project will not present a problem of establishing a donative intent as required by I.R.C. Section 170. Here there can be no question since the gift consists of highly marketable securities which will be sold to the charity at a price substantially less than the readily determined fair market value.

E. To assure the availability of the charitable deduction, care must be taken to separate the activities of the participants in the common pool and the role of the UJA. The method of giving must be structured in such a fashion to avoid having the UJA characterized for tax purposes as the owner of the pool at its inception and having the participants characterized as merely the agents of the UJA. Such a characterization would, of course, defeat the charitable deduction to the participants, since there would be no gift if the UJA were the initial owner. It appears, however, that the proposed project would not be susceptible to this detrimental characterization. Since it would be the objective and purpose of the participants to make charitable gifts of the appreciated securities only, the UJA could in no way be characterized as the owner of the pool ab initio. In the event the pool should encounter short term losses, the participants' intent and objective is to take the short term loss individually rather than make a gift. Furthermore, it makes no sense to consider the UJA an owner in a stock account which encounters losses. No charitable institution operates for the purpose of accepting a financial loss as a charitable gift. In view of this contingency, that the participants specifically intend to make a gift of the pool's securities only in the event that there is an appreciation, it appears that the two entities are sufficiently separately identified. Thus, the gift would become effective at such time as the pool's securities are transferred to the UJA in the form of a charitable gift. See Reg. 1.170-1(e).

## APPENDIX B

### ILLUSTRATIONS OF THE MECHANICS OF CHARITABLE GIVING AND THE AFTER TAX REWARDS OF SOME GENEROSITY

#### ASSUMPTIONS:

The illustrations below are based on the following assumptions. The hypothetical taxpayer has \$100,000 net taxable income at the end of the taxable year, and therefore he is taxed on any income in excess of \$100,000 at the rate of 62%, assuming he files a joint return. In addition, he has stocks with a cost or basis of \$10,000 and a present fair market value of \$20,000; and these stocks have been held for less than six months, and therefore are short term capital assets.

Illustration No. 1: The taxpayer here sells the stock at \$20,000 and retains the \$10,000 short term gain.

Illustration No. 2: The taxpayer first sells the securities for \$20,000 and then makes a charitable gift of the \$10,000 gain.

Illustration No. 3: The taxpayer here sells the stock to the charity at his cost of \$10,000 and thereby makes a charitable gift of the additional \$10,000 gain.

Illustration No. 4: The taxpayer here makes a gift directly to the charity of the entire \$20,000 in securities.

No. 1	\$100,000 ordinary income excess rate=62%	Tax=	45,180
	Take \$10,000 short term gain	Tax=	6,200
	Total		<u>51,380</u>
No. 2	\$100,000	Tax=	45,180
	Take \$10,000 short term gain		
	Give away \$10,000	Tax still	45,180

No. 3

\$100,000

Don't take \$10,000. Sell stock with \$10,000 gain to UJA at cost--you still get deduction plus get your investment back

Effect:

\$100,000 income

-0- gain

( 10,000) deduction

\$ 90,000 taxable income

Tax= 39,180

Savings= 6,000

No. 4

\$100,000

Gift directly to UJA of entire

\$20,000

Effect:

\$100,000 income

-0- gain

( 20,000) deduction

\$ 80,000 taxable income

Tax= 33,340

Savings= 11,840

CASH POSITION:

After payment of taxes, taxpayer has the following cash or "hard" dollars left.

No. 1	(\$100,000 + 10,000) - 51,380	=	58,620
No. 2	(\$100,000 + 10,000) - 45,180	=	64,820
No. 3	(\$100,000 + 10,000) - 39,180	=	70,820
No. 4	(\$100,000) - 33,340	=	66,600

The additional gift of \$10,000 of this donor was made at a actual additional cost of only \$4,220 as opposed to the smaller gift made by donor No. 3.

**SPECIFIC ILLUSTRATION OF TAX CONSEQUENCES OF THE PROPOSED PROJECT:**

Assumptions: Again we assume the taxpayer has \$100,000 ordinary income and therefore is taxed at the excess rate of 62%. It is further assumed for purposes of the illustration below that the taxpayer has a stock with a cost of \$5,000 and a fair market value of \$8,000. It is also assumed that the stock has been held for a period less than six months and therefore is short term. The illustration below graphically demonstrates that the taxpayer who sold the stock to the UJA at his cost and made a charitable gift of the additional \$3,000 is actually \$720 ahead of the other taxpayer who did not make a gift but rather sold the stock at the fair market value and retained the short term profit.

I. Sale at fair market value	\$8,000
Tax on short term gain	1,860 (62% of \$3,000 short term gain)
	<u>\$6,140</u> net tax-free dollars
II. Bargain-sale	
Sale to UJA at cost	\$5,000
Deduction for charitable gift of \$3,000 (tax dollars saved)	1,860
	<u>\$6,860</u> net tax-free dollars



## APPENDIX C

### PARTNERSHIP AGREEMENT (Outline)

#### 1. Name and Business:

The parties will form a partnership for the purpose of investment in marketable stocks and securities on a short term basis with the further objective of making charitable contributions of appreciated property, if any, of the partnership.

#### 2. Term:

The partnership shall continue for a period of six months.

#### 3. Capital:

The five individual partners shall each contribute \$10,000.

#### 4. Management:

The partnership will appoint a managing partner. His duties will consist of:

- (a) Opening a bank account in the name of the partnership.
- (b) Opening brokerage accounts in the name of the partnership with authority to accept, deliver and execute the necessary instruments which the brokerage firms may require in connection with the business affairs of the partnership.
- (c) Conducting the general and daily management of the partnership, including consultation with and control of the brokerage firms in regard to the purchase and sale of the partnership security investments.
- (d) Retaining physical possession of the books and records of the partnership, performing the necessary ministerial functions, and giving to the partners any necessary notices and information. (As a matter of practice, the brokers, as an inducement to get the business, will provide the bookkeeping together with the UJA offices.)

#### 5. Liability and Removal of the Manager:

The manager will be liable only for gross negligence and willful default, but may be removed and replaced if the partnership so decides.

6. Meetings:

The managing partner will inform the other partners of the periodic and current progress and position of the partnership, and the partnership itself will meet from time to time as determined by the partnership.

7. Capital Accounts:

An individual capital account will be maintained for each partner, consisting of his original capital contribution: (a) increased by his additional contributions to capital, if any, and by his share of partnership profits transferred to capital; (b) decreased by his share of partnership losses and by distributions to him and reduction of his capital; and (c) increased or decreased (as the case may be) on any valuation date for any increase or decrease in the net value of the partnership assets. The individual capital accounts will further reflect the partner's pro rata share of any charitable contributions made by the partnership.

8. Profit and Loss:

The net profits or net losses will be allocated equally to the individual partners.

9. Books and Records:

The accounting records of the partnership business shall be kept by the manager, or his delegate. The partnership shall report for income tax purposes on the cash basis of accounting. At the termination of the partnership or at the end of each calendar year, whichever is sooner, a complete accounting of the affairs of the partnership shall be furnished to each partner, and a certified public accountant selected by the partners shall be retained for the purpose of preparing this partnership report.

10. Custody of Securities:

Securities will be held in the custody of either the appropriate brokerage firm or the managing partner on behalf of the partnership, or in a custodian account by our bank.

11. Restriction and Liability of Partners:

Each partner's liability shall be limited in the same proportion and ratio as his capital account is to the total partnership assets. Furthermore, the individual partners will be prohibited from selling, assigning, mortgaging or pledging his interest in the partnership.

12. Withdrawal:

A partner shall withdraw only upon termination of the partnership.

13. Death:

In the event of death, the partnership shall not terminate. In such event, the partner's estate shall be deemed to be substituted for such partner and shall be deemed a limited partner for all purposes of this agreement. Said limited partner shall not be liable for partnership debts or losses in excess of the interest of the deceased in the partnership as of the date of death.

14. Liquidation:

The partnership may be dissolved and terminated upon agreement of a majority of the partners. Upon any such dissolution and termination, the partners shall promptly liquidate the affairs of the partnership by discharging all debts and liabilities of the partnership and distributing all remaining assets, in cash or in kind, or partly in cash and partly in kind, to the partners or their representatives in the ratios of their respective capital accounts on the date of dissolution and termination.

15. Benefit:

This agreement shall be binding upon the parties hereto, their heirs, successors, personal representatives, and assigns.

AMERICAN JEWISH



APPENDIX D

\_\_\_\_\_, 1966

United Jewish Appeal

Gentlemen:

We presently own \_\_\_\_\_ (No. of shares) shares of \_\_\_\_\_  
(Class of Stock) of \_\_\_\_\_ (Name of Corporation).  
We hereby offer to sell our entire right, title and interest in and to said shares to  
you for \$ \_\_\_\_\_ per share or a total selling price of \$ \_\_\_\_\_. It is our  
intention that the difference between the present fair market value of the aforesaid  
shares of stock and the selling price be and be considered to be a gift to the United  
Jewish Appeal for its general uses and purposes.

If the terms and conditions of this sale and gift are acceptable to you, please  
indicate your acceptance below and issue your check to our order in the amount  
of \$ \_\_\_\_\_. Delivery of the aforesaid shares to your account at

\_\_\_\_\_ will be made immediately upon  
your acceptance of this offer.

Very truly yours,

\_\_\_\_\_  
(Name of donor)

ACCEPTED: United Jewish Appeal

By \_\_\_\_\_ (Title)

\_\_\_\_\_, 1966

\_\_\_\_\_, 1966

(Name and Address  
of Broker)

Gentlemen:

Pursuant to a resolution adopted by our Board of Trustees on \_\_\_\_\_,  
1966, you have been and are hereby appointed the duly authorized agent of the United  
Jewish Appeal to accept, receive and hold on its behalf any and all securities which  
may be delivered to you for its account.

Until you receive notice from the United Jewish Appeal to the contrary, you  
are authorized promptly after receipt of any such securities, to sell the same at market,  
to charge the account of the United Jewish Appeal with any and all expenses and federal  
and state transfer taxes incurred in effecting such sale, and to remit the net proceeds  
of such sale to the United Jewish Appeal when available.

Please indicate your acceptance of this appointment and authorization by endorsing  
and returning the enclosed copy of this letter.

Very truly yours,

UNITED JEWISH APPEAL

By \_\_\_\_\_ (Title)

\_\_\_\_\_, 1966

(Name and Address  
of Broker)

Gentlemen:

We presently own and you hold for our account in street form \_\_\_\_\_ (No.  
of shares) of \_\_\_\_\_ (Class of stock) stock of \_\_\_\_\_  
\_\_\_\_\_ (Name of Corporation).

We have this day given, granted, sold, assigned and transferred to the United  
Jewish Appeal all of our right, title and interest in the aforesaid shares of stock.

We are advised by the United Jewish Appeal that it has designated your firm  
as its agent to accept delivery of securities given, granted, sold, assigned or transferred  
to it. We and the United Jewish Appeal hereby request that immediately upon the receipt  
of this letter you designate on your records that the aforesaid shares of stock are now  
held by you as agent for and for the account of the United Jewish Appeal. You are  
authorized to charge our account with the cost of any federal or state transfer taxes  
which may be due on account of this transfer.

Very truly yours,

\_\_\_\_\_  
(Name of donor)

This is to confirm the above instructions on our behalf. Please indicate below  
your receipt and acceptance of these instructions.

United Jewish Appeal

By \_\_\_\_\_ (Title)

\_\_\_\_\_, 1966

Receipt and acceptance of the foregoing is hereby acknowledged.

\_\_\_\_\_  
(Name of Broker)

By \_\_\_\_\_ (Title)

\_\_\_\_\_, 1966