



Howard Hughes . . . as described by pilots on Houston flight

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How it pays to be a billionaire

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In life, Howard Hughes was the beneficiary of special arrangements and favored treatment bestowed by a variety of U.S. government agencies — from the Defense Department to the Internal Revenue Service.

In death, he will be accorded the same favored treatment.

The IRS quietly implemented

in February a series of tax regulations that are expected to save his business organization millions of dollars.

The regulations govern the conduct of medical research organizations. When asked to discuss their effect on the Howard Hughes Medical Institute, which owns Hughes Aircraft Co., two IRS officials said the agency could not discuss individual taxpayers.

Richard Ruge, a member of the

Washington, D.C., law firm of Hogan and Harston, which had lobbied strenuously on Hughes' behalf, was equally silent.

But a top Treasury Department official and several Washington tax law authorities agreed the new regulations contain a special provision favorable to the Hughes business organization.

Here is what happened:

It was disclosed in December

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that the IRS had failed to apply a 1969 tax reform act to Hughes and his Miami-based medical institute, even though the sweeping changes had long since been applied to virtually every other taxpayer in the country.

The 1969 tax reform act provided for two classes of foundations: Private ones, such as the Ford and Rockefeller foundations, and non-private or public charities, such as the United Fund or Community Chest, which receive most of their financial support from the public.

To this day, the IRS has failed to label the Hughes Institute either a private foundation or a public charity. The institute has been operating as a public charity.

The most stringent requirements were imposed on the private foundations.

For example, private foundations are not permitted to own more than 35 percent of the stock of any one company. In the case of the Howard Hughes Medical Institute, the institute owns 100 percent of the stock of Hughes Aircraft Co. That stock is the institute's only holding.

In addition, private foundations must pay a minimum tax on income from their investments.

For a medical research institute to be a public charity — and thus escape the more rigid rules — it had to spend a specific percentage of its assets on medical research.

In proposed regulations to implement the 1969 tax act — regulations vigorously opposed by Hughes attorneys — the IRS set the spending requirement at 6 percent by 1975.

But the Howard Hughes Medical Institute never came close to realizing a 6 percent return on its investment in Hughes Aircraft.

The IRS explained that if it decided the medical institute was a private foundation and therefore required to spend an amount equal to 6 percent of its assets, it would apply retroactively.

All the millions the medical institute would have been required to spend — but had not — would have to be distributed at some time in the future.

But the final February regulations contain several significant changes from the ones proposed in 1971, including a grandfather clause that will preclude IRS from ordering retroactive payouts.

Although it will not be possible to place a value on the grandfather clause until the medical institute's

assets are firmly fixed, the savings can certainly be counted in the millions.

The final regulations also have reduced the amount of money a medical research organization must spend to qualify as a public charity from 6 percent to 3.5 percent of its assets. Private foundations still have to spend 6 percent of assets. Still, the Howard Hughes Medical Institute has failed to meet even the sharply reduced spending requirement of 3.5 percent.

In 1974, for example, the medical institute received \$3.5 million.

According to the medical institute's IRS return, the institute placed a value of \$190.6 million on its aircraft company holdings.

A return of 3.5 percent would have meant that the aircraft company should have paid the medical institute \$6.7 million to distribute for medical research — or nearly double the \$3.5 million actually contributed.

IRS officials and Hughes attorneys both refuse to discuss how the final government regulations for medical research organizations will be applied to the Hughes institute. But tax authorities say that what probably will occur next is this:

Assuming that the Hughes Medical Institute continues to operate as it has in the past, the IRS will officially label it a private foundation. This will make it subject to all the requirements covering medical research expenditures and investment taxes and the 35 percent stock ownership rule.

Thus, if the medical institute fails to earn an amount equal to 6 percent of its assets, which consist of the stock in Hughes Aircraft, it will be required to sell the stock necessary to make up the difference.

The financial picture could be complicated, though, by the final disposition of the rest of Hughes' estate — his gambling casinos, hotels, television station, helicopter company, vast landholdings and other properties.