200016027

Internal Revenue Service

Department of the Treasury

Washington, DC 20224

Contact Person:

Telephone Number:

In Reference to:

Date: JAN 21 2000

Significant Index Nos.
507.03-00
4940.00-00
4941.00-00
4942.00-00
4944.00-00
4945.00-00

OP:E:EO:T3

Legend:
L=
M=
N=

Dear Sir or Madam:

This is in response to M's request for certain rulings under sections 501(c)(3), 507, 4940, 4941, 4942, 4944, and 4945 of the Internal Revenue Code of 1986 submitted by M's authorized legal representative relating to M's termination and charitable fund agreement with N.

M has been recognized as exempt under section 501(c)(3) of the Code and classified as a private operating foundation under section 4942(j)(3) of the Code. M's purposes include making distributions and grants to other organizations described in section 501(c)(3).

N has been recognized as exempt under section 501(c)(3) of the Code and classified as a publicly supported organization described in sections 509(a)(1) and 170(b)(1)(A)(vi) of the Code. N has been classified as a community trust described in section 1.170A-9(e)(10) of the Income Tax Regulations. N has been in existence for more than 60 calendar months. N is organized to provide grants to public charities described in section 501(c)(3) in the geographic areas in which it operates.

M proposes to transfer all of its assets to N pursuant to a plan of distribution approved by M's board of directors. M states that there will not be any group of persons that has control over both M and N either before or after the transfer of assets.

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M also represents that after the transfer has been completed M will terminate its operations and corporate existence.

The proposed transfer will be made pursuant to a charitable fund agreement between L, M, and N. Under the agreement the assets transferred by M to N will be held in a donor fund maintained by N to further or carry out the religious, charitable, educational, literary, and/or scientific purposes as stated in N's governing instruments. The agreement will permit M's representative to specify the exempt organizations to be recipients of grants from the donor fund maintained by N on M's behalf.

The agreement defines exempt organizations as those organizations that are tax-exempt under section 501(c)(3) of the Code, contributions to which are deductible under section 170(c)(1)or (2)(B).

M represents that section 3(c) of the charitable fund agreement with N will be amended to provide that the donor fund shall have a duration of ten years during which time all of the assets transferred from M will be distributed. The agreement also provides that recommendations made by M that would benefit the L privately, or L's family members, or that are determined after investigation by N not to further exempt purposes, will not be honored.

Section 5 of the charitable fund agreement provides that contributions to funds held and maintained by M are irrevocable and nonrefundable, and are the property of N. Section 5 further states that N retains full and unlimited control over whether or not to follow specifications and/or recommendations given by a donor. M also represents that section 5 will also include amendments to make it clear that all property and income derived from the investment of the funds become part of the general fund of N.

Section 507(a) of the Code provides that, except as provided in section 507(b), the status of any private foundation shall be terminated only if such organization notifies the Secretary of its intent to accomplish such termination or, with respect to such organization, there have been either willful or repeated acts or a willful and flagrant act, giving rise to liability for tax under Chapter 42, and the Secretary notifies the organization that because of such act the organization is liable for the tax imposed by section 507(c), and either the organization pays the tax or the entire amount of the tax is abated under section 507(g).

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Section 507(c) of the Code imposes an excise tax on each terminating private foundation equal to the lower of the aggregate tax benefit resulting from such termination or the value of its net assets.

Section 507(b)(1)(A) of the Code provides that the status as a private foundation of any organization, with respect to which there have not been either willful repeated acts (or failures to act) or a willful and flagrant act (or failure to act) giving rise to liability for tax under chapter 42, shall be terminated if such organization distributes all of its net assets to one or more organizations described in section 170(b)(1)(A) (other than clauses (vii) and (viii)) each of which has been in existence and so described for a continuous 60 calendar months immediately preceding such distribution.

Section 4940 of the Code provides for the imposition of a tax on the net investment income of private foundations.

Section 4941(d)(1)(E) of the Code states that the term "self dealing" means any direct or indirect transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a private foundation.

Section 4942(a) of the Code imposes an excise tax on the undistributed income (as defined in paragraph (a) of Sec. 53.4942(a)-2) of a private foundation for any taxable year which has not been distributed before the first day of the second (or any succeeding) taxable year following such taxable year (if such first day falls within the taxable period as defined in paragraph (c)(1) of this section). For purposes of section 4942 the term "distributed" means distributed as qualifying distributions under section 4942(g).

Section 4944(a)(1) of the Code imposes a tax on a private foundation that invests any amount in such manner as to jeopardize the carrying out of any of its exempt purposes.

Section 4945(d)(4) of the Code provides that the term "taxable expenditure" means any amount paid or incurred by a private foundation as a grant to an organization unless such organization is described in paragraph (1), (2), or (3) of section 509(a) or is an exempt operating foundation, or the private foundation exercises expenditure responsibility with respect to such grant.

Section 4945(d)(5) of the Code provides that the term "taxable expenditure" does not include amounts paid or incurred

by a private foundation as a grant to another organization for purposes specified in section 170(c)(2)(B).

Section 4945(h) of the Code provides that the expenditure responsibility referred to in subsection (d)(4) means that the private foundation is responsible to exert all reasonable efforts to establish adequate procedures to see that the grant is spent solely for the purpose for which made, to obtain full and complete reports from the grantee on how the funds are spent, and to make full and detailed reports with respect to such expenditures to the Secretary.

Section 4946(a)(1) of the Code provides, in part, that the term "disqualified person" shall not include any organization which is described in section 501(c)(3) (other than an organization described in section 509(a)(4)).

Section 4946(a)(1)(B) of the Code defines a disqualified person to include with respect to a private foundation a foundation manager.

Section 4946(b)(1) of the Code states that the term foundation manager includes a trustee of a foundation having the authority or responsibility over the activities of the foundation.

Section 1.507-2(a)(1) of the Foundation and Similar Excise Taxes Regulations provides that under section 507(b)(1)(A) a private foundation, with respect to which there have not been either willful repeated acts (or failures to act) or a willful and flagrant act (or failure to act) giving rise to liability for tax under chapter 42, may terminate its private foundation status by distributing all of its net assets to one or more organizations described in section 170(b)(1)(A) (other than in clauses (vii) and (viii)) each of which has been in existence and so described for a continuous period of at least 60 calendar months immediately preceding such distribution. Since section 507(a) does not apply to such a termination, a private foundation which makes such a termination is not required to give the notification described in section 507(a)(1). A private foundation which terminates its private foundation status under section 507(b)(1)(A) does not incur tax under section 507(c) and, therefore, no abatement of such tax under section 507(g) is required.

Section 1.507-2(a)(6)(i) of the regulations provides that an organization which terminates its private foundation status under section 507(b)(1)(A) is required to file a return under the provisions of section 6043(b).

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Section 1.507-2(a)(7) of the regulations provides that a private foundation will meet the requirement that it 'distribute all of its net assets' within the meaning of section 507(b)(1)(A) only if it transfers all of its right, title, and interest in and to all of its net assets to one or more organizations referred to in section 507(b)(1)(A).

Section 1.507-2(a)(8)(i) of the regulations provides that in order to effectuate a transfer of 'all of its right, title, and interest in and to all of its net assets' within the meaning of paragraph (a)(7) of this section, a transferor private foundation may not impose any material restriction or condition that prevents the transferee organization referred to in section 507(b)(1)(A) (herein sometimes referred to as the 'public charity') from freely and effectively employing the transferred assets, or the income derived therefrom, in furtherance of its exempt purposes. Whether or not a particular condition or restriction imposed upon a transfer of assets is 'material' (within the meaning of paragraph (a)(8) of this section) must be determined from all of the facts and circumstances of the transfer. Some of the more significant facts and circumstances to be considered in making such a determination are:

(A) Whether the public charity (including a participating trustee, custodian, or agent in the case of a community trust) is the owner in fee of the assets it receives from the private foundation;

(B) Whether such assets are to be held and administered by the public charity in a manner consistent with one or more of its exempt purposes;

(C) Whether the governing body of the public charity has the ultimate authority and control over such assets, and the income derived therefrom; and

(D) Whether, and to what extent, the governing body of the public charity is organized and operated so as to be independent from the transferor.

Section 1.507-2(a)(8)(vi)(A) of the regulations provides, in part, that the presence of any of the following factors will be considered as preventing the transferee 'from freely and effectively employing the transferred assets, or the income derived therefrom, in furtherance of its exempt purposes' (within the meaning of paragraph (a)(8)(i) of this section):

(1) With respect to distributions made after April 19, 1977, the transferor private foundation, a disqualified person with

respect thereto, or any person or committee designated by, or pursuant to the terms of an agreement with, such a person (hereinafter referred to as 'donor'), reserves the right, directly or indirectly, to name (other than by designation in the instrument of transfer of particular section 509(a)(1), (2), or (3) organizations) the persons to which the transferee public charity must distribute, or to direct the timing of such distributions (other than by direction in the instrument of transfer that some or all of the principal, as opposed to specific assets, not be distributed for a specified period) as, for example, by a power of appointment.

Section 53.4940-1(f)(1) of the regulations provides that a distribution of property for purposes described in section 170(c)(1) or (2)(B) which is a qualifying distribution under section 4942 shall not be treated as a sale or other disposition of property.

Section 4942-3(a)(2)(i) of the regulations provides that the term 'qualifying distribution' means any amount (including program-related investments, as defined in section 4944(c), and reasonable and necessary administrative expenses) paid to accomplish one or more purposes described in section 170(c)(1) or (2)(B) of the Code.

Section 53.4945-6(b)(v) of the regulations provides that under section 4945(d)(5) the term 'taxable expenditure' includes any amount paid or incurred by a private foundation for any purpose other than one specified in section 170(c)(2)(B). Any payment which constitutes a qualifying distribution under section 4942(g) or an allowable deduction under section 4940 is not treated as a taxable expenditure.

Section 53.4946-1(a)(8) of the regulations provides that for purposes of section 4941 only, the term 'disqualified person' shall not include any organization which is described in section 501(c)(3) (other than an organization described in section 509(a)(4)).

M will transfer all of its net assets to N pursuant to a charitable fund agreement between L, M, and N. The proposed transfer has been approved by M's board of directors. M has been classified as a private operating foundation described in section 4942(j)(3) of the Code. N is a publicly supported organization described in section 170(b)(1)(A)(vi) which has been in existence for more than 60 calendar months. Under the agreement, N is required to use the funds transferred from M to accomplish charitable purposes described in sections 501(c)(3) and

170(c)(2)(B). The transfer is, therefore, described in section 507(b)(1)(A).

The transfer of all of M's net assets to N constitutes a transfer described in section 507(b)(1)(A) of the Code. N will freely and effectively employ the transferred assets within the meaning of section 1.507-2(a)(8)(i) of the regulations. The transfer will result in a termination of M's private foundation status. However, the tax imposed by section 507(c) will not be applicable to M pursuant to section 1.507-2(a)(1) of the regulations.

As indicated above, N will use the funds transferred from M to accomplish purposes described in sections 501(c)(3) and 170(c)(2)(B) of the Code. Therefore, the transfer constitutes a qualifying distribution described in section 4942. In addition, the legal, accounting, and other administrative costs associated with the transfer of assets constitutes a qualifying distribution pursuant to section 53.4942-3(a)(2)(i) of the regulations.

The transfer does not constitute a sale or disposition of property for purposes of the tax imposed by 4940 pursuant to section 53.4940-1(f)(1) of the regulations. Further, since the assets transferred will be used by N to accomplish M's charitable purposes, which are otherwise described in section 170(c)(2)(B), the transfer and incidental expenses, including expenses incurred by this private letter ruling request, will not constitute taxable expenditures described in section 4945 of the Code. In addition, since N is a publicly supported organization described in section 509(a)(1) and 170(b)(1)(A)(vi), M will not be required to exercise expenditure responsibility with respect to the assets transferred to N as required by 4945(h).

Funds will only be distributed by N from an account maintained by N after recommendations are made by M's representatives. The charitable fund agreement will provide that N is not bound by the representative's recommendation and will not honor any distribution recommendations made by M's representatives if such recommendations benefit L, or the family members of L. Further, since N is an organization recognized as exempt under section 501(c)(3) of the Code, N is not a 'disqualified person' within the meaning of section 4946 of the Code pursuant to section 53.4946-1(a)(8) of the regulations. Therefore, the transfer of assets from M to N will not constitute an act of self-dealing under section 4941 of the Code.

The transfer of assets from M to N constitutes a transfer described in 507(b)(1)(A). The assets transferred from M to N will be dedicated to section 170(c)(2)(B) purposes even if N

receives no recommendations from M as to grant recipients. The tax imposed on jeopardizing investments under section 4944 of the Code does not apply to the transfer.

After the transfer M will terminate its operations and corporate existence. M will be required to file its final return, a copy of its corporate dissolution, and otherwise comply with the Service's termination procedures pursuant to section 1.507-2(a)(6)(i) of the regulations.

Based on the above, we rule as follows:

1. The transfer of all of the assets of M to N will not affect the status of M as an organization described in section 501(c)(3) of the Code, and as an organization to which donations are deductible by donors to the extent provided by section 170.

2. The transfer of all of M's assets to N will terminate M's status as a private foundation pursuant to section 507(b)(1)(A) so that no tax will be imposed under section 507(c).

3. The transfer of all of M's assets to N will not constitute any sale or disposition of property within the meaning of section 4940, nor subject M to an excise tax under that section.

4. The transfer of all of M's assets to N will not constitute an act of self-dealing within the meaning of section 4941 of the Code, nor subject L to an excise tax under that section.

5. The transfer of all of M's assets to N will constitute a qualifying distribution under section 4942(g), and will not subject M to an excise tax under that section.

6. The transfer of all of M's assets to N will not constitute a jeopardizing investment within the meaning of section 4944, nor subject M to tax under that section.

7. The transfer of all of M's assets to N will not constitute a taxable expenditure within the meaning of section 4945, and M will not be required to exercise expenditure responsibility under section 4945(h) with respect to the transfer.

8. The legal, accounting and other expenses (including filing) incurred by M in connection with this ruling request will not constitute taxable expenditures under section 4945.

9. After M has ceased to exist as a separate legal entity and has filed a final return and otherwise complied with Service's

termination procedures, M will no longer be required to file form 990-PF information returns.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

We are informing your key District Director of this ruling.

Sincerely yours,

Robert C. Harper, Jr.
Manager, Exempt Organizations
Technical Group 3

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