DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

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Contact Person:

Uniform Issue List: 507.00-00
501.03-02
509.01-01
4940.00-00
4941.04-00
4942.03-05
4942.03-06
4943.00-00
4944.00-00
4945.04-06

Contact Number:
OP:E:EO:T2

Legend:
P =
R =
S =
T =

Dear Sir or Madam:

This is in reply to your rulings request of August 12, 1998, as modified by your letter of October 22, 1999, requesting rulings as to P's proposed transfer of three-fourths of its assets to R, S, and T pursuant to section 507(b)(2) of the Internal Revenue Code.

P, R, S, and T are exempt from federal income tax under section 501(c)(3) of the Code and are private foundations under section 509(a) of the Code. Their governing bodies are controlled by the same individuals.

P will transfer three-fourths of its assets to R, S, and T, each of which will receive one-fourth of P's assets. P will continue to operate for exempt purposes. P has no expenditure responsibility grants outstanding under section 4945(h) of the Code.

The following rulings are requested:

1. The transfer will not result in termination of P's status as a private foundation under section 507 of the Code;

2. The transfer will constitute a transfer described in section 507(b)(2) of the Code and no transferee will be treated as a newly created organization.

3. The transfer will not constitute either a willful flagrant act (or failure to act) or one of a series of repeated acts (or failures to act) giving rise to liability for tax under Chapter 42 of the Code, and will not result in the imposition of any tax under Section 507(c) of the Code.

4. Each transferee will succeed to twenty-five percent of the aggregate tax benefit of P determined as the amount of such aggregate tax benefit multiplied by the portion of P's assets (based on fair market value) which will be transferred in the transfer.

5. The transfer will not result in the imposition of any tax under section 4940 of the Code.

6. The transfer will not constitute an act of self-dealing within the meaning of section 4941(d) of the Code and will not result in the imposition of any tax under section 4941 of the Code.

7. The portion of the transfer with respect to which section 4942(g)(3) of the Code is satisfied will constitute a qualifying distribution of P under section 4942(g) of the Code.

8. The transfer will not result in the imposition of any tax under section 4943 of the Code.

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9. The transfer will not result in the imposition of any tax under section 4944 of the Code as an investment jeopardizing P's exempt purpose.

10. The transfer will not constitute a taxable expenditure under section 4945(d) of the Code, and P will not be required to exercise expenditure responsibility within the meaning of section 4945(h) of the Code with respect to any portion of the assets transferred in the transfer.

11. The reasonable legal, accounting and other expenses, incurred by P in connection with obtaining the rulings requested herein, will not constitute taxable expenditures for purposes of section 4945 of the Code.

Section 501(c)(3) of the Code provides for the exemption from federal income tax of nonprofit organizations that are organized and operated exclusively for charitable and/or the other exempt purposes stated in that section.

Section 509(a) of the Code provides that certain organizations, exempt from federal income tax under section 501(c)(3), are further classified as private foundations subject to the private foundation provisions of the Code.

Section 507 of the Code provides that a private foundation can terminate its private foundation status under section 509(a) of the Code.

Section 507(c) of the Code imposes a termination tax on a private foundation that terminates under section 507(a) of the Code its status as a private foundation under section 509(a) of the Code.

Section 507(b)(2) of the Code and section 1.507-3(a)(1) of the Income Tax Regulations provide that, in a transfer of assets from one private foundation to one or more private foundations pursuant to any reorganization, any transferee foundation shall not be treated as a newly created organization, but shall succeed to the transferor foundation's aggregate tax benefits under section 507(d) of the Code.

Section 507(d) of the Code provides that a private foundation's aggregate tax benefits refer to the value of its exemption from federal income tax and of the deductions taken by its donors during its existence.

Section 1.507-3(c)(1) of the regulations provides that a transfer under section 507(b)(2) of the Code includes a transfer of assets from one private foundation to another private foundation pursuant to any reorganization, including any significant disposition of 25% or more of the transferor private foundation's assets.

Section 1.507-3(a)(5) of the regulations provides that a transferor private foundation is required to meet its charitable distribution requirements under section 4942 of the Code, even for any tax year in which it makes a transfer of its assets pursuant to section 507(b)(2) of the Code to another private foundation.

Section 1.507-3(a)(7) of the regulations provides that a transferee foundation must assume the transferor foundation's outstanding expenditure responsibility as shown in Example 2 of section 1.507-3(a)(9) of the regulations, and that a transferor private foundation is not required to exercise expenditure responsibility under section 4945(h) of the Code for tax years after the year of the transfer "where the transferor has disposed of all of its assets during any period in which the transferor has no assets."

Section 1.507-3(a)(9)(i), Example 2, of the regulations describes an example where a transferee foundation must assume the transferor foundation's outstanding expenditure responsibility under section 4945(h) of the Code and where the transferor private foundation, having disposed of all of its assets to its transferees and having no other assets during the period, is not required to exercise responsibility under section 4945(h) of the Code for subsequent tax years.

Section 1.507-4(b) of the regulations provides that the tax on termination of private foundation status imposed by section 507(c) of the Code does not apply to a transfer of assets pursuant to section 507(b)(2) of the Code.

Sections 1.507-1(b)(7) and 1.507-3(d) of the regulations provide that a transferor foundation's transfer of assets under section 507(b)(2) of the Code will not constitute a termination of the transferor foundation's status as a private foundation.

Section 4940 of the Code imposes tax on the investment income of a private foundation.

Section 4941 of the Code imposes tax on acts of self-dealing between a private foundation and any of its disqualified persons under section 4946 of the Code.

Section 53.4946-1(a)(8) of the Foundation and Similar Excise Taxes Regulations provides that, for purposes of self-dealing under section 4941 of the Code, an exempt organization under section 501(c)(3) of the Code is not a disqualified person.

Section 4942 of the Code requires that a private foundation must expend qualifying distributions under section 4942(g) of the Code for the conduct of exempt purposes.

Section 4942(g)(1)(A) of the Code and section 53.4942(a)-3(a)(2)(i) of the regulations provide that a "qualifying distribution" is any amount, including that portion of reasonable and necessary administrative expenses, paid to accomplish one or more purposes described in section 170(c)(2)(B), other than any contribution to: (i) an organization controlled directly or indirectly by the transferor foundation or one or more disqualified persons with respect to the foundation, except as provided in section 4942(g)(3) of the Code, or (ii) any private foundation that is not an operating foundation under section 4942(j)(3) of the Code, except as provided in section 4942(g)(3) of the Code.

Sections 4942(g)(3) of the Code and section 53.4942(a)-3(c)(1) of the regulations require that, in order for a transferor private foundation to have a qualifying distribution, including reasonable and necessary administrative expenses thereof, under section 4942(g)(1)(A) of the Code for its contribution to: (i) a private foundation which is controlled by it or its disqualified persons or (ii) a private foundation which is not an operating foundation under section 4942(j)(3), such transferor private foundation must have adequate records, as required by section 4942(g)(3)(B) of the Code, to show that the transferee foundation subsequently made a qualifying distribution that was equal to the amount of the transfer received, that was paid out of the transferee's own corpus within the meaning of section 4942(h) of the Code, and that was expended by the transferee before the close of its first tax year after its tax year in which it received the grant.

Section 4943 of the Code imposes tax on a private foundation's holding of any excess business holdings as defined in that section.

Section 4944 of the Code imposes tax on a private foundation's making of any jeopardizing investment.

Section 4945 of the Code imposes tax on a private foundation's making of any "taxable expenditure" under section 4945(d)(4) of the Code.

Section 4945(d)(4) of the Code requires that, in order for its grant not to be a taxable expenditure, a transferor private foundation must exercise "expenditure responsibility" under section 4945(h) of the Code on any grant to another private foundation that is not also an "exempt operating foundation" under section 4940(d)(2) of the Code.

Section 4945(h) of the Code on expenditure responsibility requires that the grantor private foundation must make pre-grant inquiry and obtain post-grant reports from the grantee private foundation as to the grantee's uses of the grant.

Section 53.4945-5(c)(2) of the regulations provides that, if a private foundation makes a grant to another private foundation for endowment or other capital purposes, the grantor foundation must obtain reports from the grantee foundation on the uses of the principal and the income, if any, from the grant funds. The grantee must make such reports annually for its tax year in which the grant is made and for its immediately succeeding two tax years. Only if it is reasonably apparent to the grantor, before the end of such grantee's second succeeding tax year, that neither the principal nor the income from the grant funds has been used for any purpose which would result in liability for tax under section 4945 of the Code, may the grantor then allow the grantee's reports to be discontinued.

Section 53.4945-6(b)(2) of the regulations provides that a private foundation's payment of the reasonable costs for services rendered is not a taxable expenditure under section 4945 of the Code.

Analysis

P will transfer three-fourths of its assets to R, S, and T. Your requested rulings are discussed below:

1.

Under section 1.507-4(b) of the regulations, P's transfer of assets to private foundations R, S, and T pursuant to section 507(b)(2) of the Code will not be a termination under section 507 of the Code of P's status as a private foundation under section 509(a) of the Code.

2.

Under section 507(b)(2) of the Code and section 1.507-3(c)(1) of the regulations, a transfer under section 507(b)(2) of the Code includes a transfer of assets from one private foundation to one or more other private foundations pursuant to any reorganization, including any disposition of 25% or more of the transferor foundation's assets. P will be making such a reorganization transfer of its assets by its disposition of three-fourths of its assets to R, S, and T, and, thus, P's transfer of three-fourths of its assets will be a transfer under section 507(b)(2) of the Code.

Under section 507(b)(2) of the Code and section 1.507-3(a)(1) of the regulations, P's transfer of assets pursuant to that section 507(b)(2) of the Code will not result in either P or its transferees being considered a newly created organization.

3.

Because P's transfer of assets will be made for exempt purposes to exempt organizations under section 501(c)(3) of the Code, P's transfers will not be either a willful and flagrant act (or failure to act) or one of a series of repeated acts (or failures to act) giving rise to liability for tax under Chapter 42 of the Code and will not result in tax under section 507(c) of the Code.

4.

Under section 1.507-3(a)(2) of the regulations, each transferee R, S, and T will succeed to twenty-five percent of the aggregate tax benefit of P, determined as the total amount of the aggregate tax benefit of P multiplied by the proportion of P's assets based on fair market value which will be transferred to each transferee in the transfer.

5.

Under section 4940 of the Code, P's transfer of assets will not result in tax on investment income under that section.

6.

Under section 4941 of the Code, P's transfer of assets will not be an act of self-dealing because the transfer will be for exempt purposes to organizations exempt from federal income tax under section 501(c)(3) of the Code, which are not disqualified persons under section 4946 of the Code for purposes of section 4941 of the Code, pursuant to section 53.4946-1(a)(8) of the regulations.

7.

Under section 4942(g)(3) of the Code, P will have a qualifying distribution pursuant to that section to the extent, if any, that P and its transferees will satisfy the specific requirements, including redistribution requirements, under that section 4942(g)(3) of the Code.

8.

Under section 4943 of the Code, P's transfer of assets will not involve or result in any excess business holdings or tax under that section.

9.

Under section 4944 of the Code, P's transfer of assets is made for exempt purposes to exempt organizations under section 501(c)(3) of the Code and will not be a jeopardizing investment or result in tax under that section.

10.

P's transfer of three-fourths of its assets to R, S, and T will not be a taxable expenditures under section 4945 of the Code so long as P exercises the capital endowment grant expenditure responsibility required by section 4945(h) of the Code and section 53.4945-5(c)(2) of the regulations.

11.

Under section 53.4945-6(b)(2) of the regulations, a private foundation's payment of its reasonable costs for services rendered is not a taxable expenditure under section 4945 of the Code. Thus, P's payment of the legal, accounting, and other expenses, if reasonable in amount, incurred to implement its transfers, will not be taxable expenditures under section 4945 of the Code.

Accordingly, we rule that:

1. P's transfer of three-fourths of its assets to R, S, and T will not result in termination under section 507 of the Code of P's status as a private foundation under section 509(a) of the Code.

2. P's transfer will be a transfer under section 507(b)(2) of the Code and so neither R, S, nor T will be treated as a newly created organization.

3. P's transfer will not be either a willful and flagrant act (or failure to act) or one of a series of repeated acts (or failures to act) giving rise to liability for tax under Chapter 42 of the Code and, thus, will not result in tax under section 507(c) of the Code.

4. Each transferee R, S, and T will succeed to twenty-five percent of the aggregate tax benefit of P, determined as the amount of such aggregate tax benefit of P multiplied by the proportion of P's assets based on fair market value which will be transferred to each transferee in the transfer.

5. P's transfer will not result in tax on investment income under section 4940 of the Code.

6. P's transfer will not be an act of self-dealing under section 4941(d) of the Code and will not result in tax under section 4941 of the Code.

7. Any portion of P's transfer that meets section 4942(g)(3) of the Code will constitute a qualifying distribution of P under section 4942(g) of the Code.

8. P's transfer will not result in tax on excess business holdings under section 4943 of the Code.

9. P's transfer will not be a jeopardizing investment under section 4944 of the Code.

10. P's transfer of three-fourths of its assets will not be a taxable expenditure under section 4945 of the Code, provided that P will exercise expenditure responsibility under section 4945(h) of the Code and section 53.4945-5(c)(2) of the regulations with respect to its transfer of three-fourths of its assets to R, S, and T.

11. P's legal, accounting, and other expenses for this ruling and transfer, if reasonable in amount, will not be taxable expenditures under section 4945 of the Code.

Because this ruling letter could help to resolve any questions about your status, please keep it in your permanent records and include a copy in your annual return on Form 990-PF.

This ruling letter 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.

Sincerely,

(signed) Garland A. Carter

Garland A. Carter
Manager, Exempt Organizations
Technical Group 2

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