TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

200228028

UIL Numbers: 4941.04-00
4947.02-00
4946.01-00

Date: APR 16 2002

T: EO: B3

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Legends:

Trust =
Company =
B =
C =
D =
year 1 =
x =

Dear Sir or Madam:

This is in reference to your ruling request dated September 25, 2001 concerning the federal income and excise tax consequences of proposed payments by the Trust to a corporation for certain services described below.

The Trust is a net income charitable remainder unitrust with a makeup provision. The co-trustees are C and D, and income beneficiary is B, the son of C and D. The remainder beneficiaries are those charitable organizations described in section 170(b)(1)(A), 170(c), 2055(a), and 2522(a) of the Internal Revenue Code ("Code") as shall be designated at a later time. The value of the Trust's assets as of January 1, year 1, was approximately x. The assets held by the Trust consist of public equity and bond portfolios. The Trust is a split-interest trust described in section 4947(a)(2).

Company is a corporation owned entirely by C and D. The Trust represents that Company generally functions as an investment management and general service corporation to various business entities owned by C and D. The Company also provides services to the Trust and several other unitrusts.

The Trust's investments in stocks and bonds are generally managed by a number of separate investment management firms that are not directly or indirectly related to the Trust, Company, B, or any member of B's family, and are not otherwise disqualified persons with respect to the Trust under section 4946 of the Code. The Trust pays fees directly to the respective managers in exchange for investment management services. The fee arrangements vary depending on the manager and the asset type, but none of such fees exceed the range of fees ordinarily charged by commercial institutions for comparable services in the geographic area in which such services are performed.

Currently, Company performs the following functions for the Trust without charge: (1) strategic portfolio planning, investment counsel, and asset allocation; (2) analysis, purchase and sale of securities; (3) selection, supervision and oversight of investment managers that are unrelated third parties; (4) selection, supervision and oversight of property management services (e.g. janitorial, maintenance, etc.), provided by unrelated third parties; (5) selection, supervision and monitoring of legal, tax and accounting services provided by unrelated third parties; (6) selection, supervision and monitoring of other management and administrative services provided by third parties; (7) bookkeeping and accounting services; and (8) cash flow planning, including management of transfers among the Trust's investments, and distributions to the income beneficiary.

In the future, Company intends to provide investment management, tax, accounting and/or legal services directly to the Trust, rather than arrange for and manage such services to be provided by others.

In connection with Company's selection, supervision and oversight of services provided by third parties, Company will arrange for the services to be provided by the third parties, enter into contracts with the third parties for such services, and pay the third parties for such services, all as the Trust's agent. The Trust will reimburse Company for expenses incurred on the Trust's behalf (including payment to unrelated third parties with no mark-up by Company), and the Trust will pay Company a fee for its administrative services.

The Trust proposes to pay reasonable fees to Company for the above services rendered (or to be rendered in the future) to the Trust by Company. Company's fee for its management of investment assets may be computed in various ways. In some cases, consistent with the custom in the asset management industry, Company's fee for its management of investment assets will be computed as a percentage of the value of the assets managed. Regardless of how they are computed, none of the fees paid by the Trust to Company for services described above will exceed the range of fees ordinarily charged by commercial institutions for comparable services in the geographic area in which such services are performed, and none of such fees will exceed "reasonable compensation" for such services.

The Trust has requested a ruling that payments of reasonable fees to Company by Trust for the investment management and administrative services described above will not constitute direct or indirect acts of self-dealing under section 4941.

Chapter 42 of the Code subjects private foundations described in section 509(a) and

disqualified persons described in section 4946 to certain excise tax provisions including section 4941.

Section 4941(a) of the Code imposes an excise tax on each act of self-dealing between a disqualified person and a private foundation.

Section 4947(a)(2) of the Code provides that the self-dealing excise tax imposed by section 4941 of the Code applies equally with respect to split-interest trusts as if such trust were a private foundation.

Section 4941(d)(1) of the Code provides, in part, that the term "self-dealing" means any direct or indirect (A) sale or exchange, or leasing, of property between a private foundation and a disqualified person; (B) lending of money or other extension of credit between a private foundation and a disqualified person;...(E) transfer to, or use by or for the benefit of, a disqualified person of the assets of a private foundation.

Section 4946(a)(1) of the Code provides, in part, that the term "disqualified person" means, with respect to a private foundation, a person who is –

(A) a substantial contributor to the foundation;

(B) a foundation manager;

(C) an owner of more than 20 percent of (i) the total combined voting power of a corporation...which is a substantial contributor to the foundation,...;

(D) a member of the family of any individual described in subparagraphs (A), (B), or (C);

(E) a corporation in which persons described in subparagraph (A), (B), (C), or (D) own more than 35 percent of the total combined voting power.

Section 4941(d)(2)(C) of the Code provides in relevant part that the "furnishing of goods, services or facilities by a disqualified person to a private foundation shall not be an act of self-dealing if the furnishing is without charge..."

Section 4941(d)(2)(E) of the Code provides in part that "payment of compensation (and the payment or reimbursement of expenses) by a private foundation to a disqualified person for personal services which are reasonable and necessary to carrying out the exempt purpose of a private foundation shall not be an act of self-dealing if the compensation for payment or reimbursement is not excessive."

Section 53.4941(d)-1(b)(5) of the Foundation and Similar Excise Tax Regulations ("foundation regulations") provides, for purposes relative to acts of indirect self-dealing under section 4941(d) of the Code, two basic tests for determining whether an organization is "controlled" by a private foundation. Control exists (i) if the foundation or one or more of its foundation managers, acting only in such capacity, may, only by aggregating their votes or positions of authority require the organization to engage in a transaction which if engaged in with the private foundation would constitute self-dealing; or (ii) in the case of a transaction between the organization and a disqualified person, if such disqualified person, together with one or more persons who are disqualified persons by reason of such person's relationship within the meaning of section 4946(a)(1)(C) through (G) to such disqualified person, may, only be aggregating their votes or positions of authority with that of the private foundation require the organization to engage in such a transaction.

Section 52.4941(d)-2(d)(3) of the foundation regulations provides, in part, that "[t]he furnishing of goods, services, or facilities by a disqualified person to a private foundation shall not be an act of self-dealing if they are furnished without charge ... Similarly, the furnishing of services (even though such services are not personal in nature) shall be permitted if such furnishing is without charge."

Section 53.4941(d)-2(e) of the foundation regulations provides, in part, that "[t]he payment of compensation by a private foundation to a disqualified person shall constitute an act of self-dealing..."

Section 53.4941(d)-3(c)(1) of the foundation regulations provides, in part, that "[t]he payment of compensation by a private foundation to a disqualified person for the performance of personal services which are reasonable and necessary to carry out the exempt purposes of the private foundation shall not be an act of self-dealing if such compensation is not excessive..." The term "personal services" includes the services of a broker serving as an agent for the private foundation, but not the services of a dealer who buys from the private foundation and sells to third parties.

Section 53.4941(d)-3(c)(2) of the foundation regulations, contains examples which indicate that legal services, investment counseling services, and general banking services may constitute personal services. Example 2 provides the following example of permitted personal services:

"C, a manager of private foundation X, owns an investment counseling business. Acting in his capacity as an investment counselor, C manages X's investment portfolio for which he receives an amount which is determined to be not excessive. The payment of such compensation to C shall not constitute an act of self-dealing."

Section 53.4941(d)-2(c)(4) of the foundation regulations provides, in pertinent part, that under section 4941(d)(2)(E) the performance by a bank or trust company which is a disqualified person of trust functions and certain general banking services for a private foundation is not an act of self-dealing, where the banking services are reasonable and necessary to carrying out the exempt purposes of the private foundation, if the compensation paid to the bank or trust company, taking into account the fair interest rate for the use of the funds by the bank or trust company, for such services is not excessive.

As indicated by section 4941(d)(1)(D) of the Code and regulations thereunder, direct or indirect payment of compensation (or the payment or reimbursement of expenses) by a trust to a disqualified person constitutes an act of self-dealing. C and D are disqualified persons under section 4946(a)(1)(E) with respect to the Trust because they created and funded the Trust, and because they currently serve as co-trustees of the Trust. The Company is a disqualified person under section 4946(a)(1)(E) with respect to the Trust because it is owned entirely by C and D, the parents of B.

However, section 4941(d)(2)(E) of the Code provides an exception to section 4941(d)(1)(D). This provision and section 53.4941(d)-3(c) of the foundation regulations provide that the payment of compensation to a disqualified person by a trust for the performance of personal services which are reasonable and necessary to carry out the exempt purpose of the trust will not constitute self-dealing if the compensation is not excessive.

Under the proposed transaction, the fees, represented as not excessive, that the Trust will pay to Company is for accounting, investment and management services that the Trust has represented are necessary to carry out the exempt purposes of the Trust. These services fall within Example 2 of section 53.4941(d)-3(c) of the Foundation regulations and within the meaning of "trust functions" as used in section 53.4941(d)-2(c)(4), which describe services for which compensation can be provided without constituting acts of self-dealing.

Therefore, we rule that payments of reasonable fees to Company by Trust for the investment management and administrative services described above will not constitute direct or indirect acts of self-dealing under section 4941.

Also, in this ruling, we have not determined whether the compensation paid is reasonable. We merely have accepted your representations. This ruling is limited to the applicability of section 4941 to the issue ruled on herein. This ruling is based on the understanding that there will be no material changes in the facts upon which it is based.

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

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

(signed) Robert C Harper, Jr.

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