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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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4940.00-00
4941.04-00
4942.03-05
4944.00-00
4945.04-06
6033.02-01

Contact Person:

Identification Number:

Telephone Number:

T:EO:B2

Legend:
X =
Y =

Dear

This is in reply to your rulings request of July 19, 2001, concerning X's proposed transfer of all of its assets to Y pursuant to section 507(b)(2) of the Internal Revenue Code.

X and Y are nonprofit charitable corporations that 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. X and Y are controlled by the same individuals. X will transfer all of its assets to Y to reduce administration costs. After the transfer, X will dissolve under state law. X's scholarships, already awarded to students but payable in the future, will be paid by Y. X expects to have no expenditure responsibility grants outstanding under section 4945(h) of the Code at the time of the transfer but, if so, Y agrees to assume such expenditure responsibility on behalf of X.

The following rulings are requested:

1. X's transfer of all of its assets to Y will qualify as a transfer pursuant to section 507(b)(2) of the Code, will not constitute 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 of the Code, will not terminate the status of X as a private foundation described in section 509(a) of the Code and exempt from federal income taxation under section 501(a) of the Code, and will not result in the imposition on X of any termination tax under section 507(c) of the Code.

2. X's transfer of all of its assets to Y will not adversely affect the tax-exempt status of Y under sections 501(a) and 509(a) of the Code.

3. If X notifies the Internal Revenue Service that X intends to terminate its private foundation status pursuant to section 507(a)(1) of the Code at least one day after X's transfer of all of its remaining assets to Y, no termination tax under section 507(c) of the Code will be imposed on X.

4. X's transfer of all of its assets to Y will not subject X to any excise tax on net investment income under section 4940 of the Code.

5. The provisions of section 4940 of the Code will apply to Y in the tax year of X's transfer of all of its assets to Y and in any subsequent tax year as if Y were X. Therefore, Y will report the net investment income of X for the tax year of the transfer and will pay any excise tax imposed by section 4940 of the Code with respect to such net investment income.

6. X's transfer of all of its assets to Y will not constitute an act of self-dealing under section 4941 of the Code and will not subject any foundation manager or other disqualified person of X or any foundation manager or other disqualified person of Y to the imposition of tax under section 4941 of the Code.

7. X's transfer of all of its assets to Y will be counted toward the satisfaction of the distribution requirements of X under section 4942 of the Code to the extent that the amounts transferred meet the requirements of section 4942(g) of the Code.

8. X will not be required to comply with the recordkeeping requirements of section 4942(g)(3)(B) of the Code with respect to the transfer of all of its assets to Y.

9. The distribution requirements of section 4942 of the Code will apply to Y in the tax year of the transfer of all of the assets of X to Y and in any subsequent year as if Y were X. Therefore, Y will succeed to the distribution requirements of X for the tax year of the transfer. Y will take into account, for purposes of determining Y's distribution requirements under section 4942 of the Code: X's excess qualifying distributions, if any, with respect to each year preceding the tax year of the transfer; X's undistributed income, if any, with respect to the tax year of the transfer and each preceding year; X's minimum investment return for the tax year of the transfer; and any qualifying distributions made by X during the tax year of the transfer either prior to, or as a result of, the transfer.

10. X's transfer of all of its assets to Y will not constitute jeopardizing investments with respect to X or Y within the meaning of section 4944 of the Code.

11.a. X's transfer of all of its assets to Y will not constitute a taxable expenditure and will not subject X to the imposition of any tax under section 4945 of the Code.

11.b. X will not be required to exercise expenditure responsibility under section 4945(h) of the Code with respect to the transfer to Y except for information return requirements for the year of the transfer.

11.c. Although X does not have any outstanding grants that require the exercise of expenditure responsibility within the meaning of section 4945(h) of the Code and X does not have any plans to make any future grants that would require expenditure responsibility, if, notwithstanding the foregoing, X makes any grants that require expenditure responsibility prior to the transfer of all of its assets to Y, Y will exercise expenditure responsibility for all such grants. Such expenditure responsibility by Y will begin after the transfer by X of all of its assets to Y. Any expenditure responsibility requirements imposed on X with respect to grants made to organizations other than Y will not subject X or Y to the imposition of any tax under section 4945 of the Code, provided that Y exercises such expenditure responsibility.

11.d. Y's assumption and payment of the remaining obligations on the scholarship grants already awarded by X will not constitute taxable expenditures and will not subject Y to the imposition of any tax under section 4945 of the Code.

12. X will not be required to comply with the periodic reporting, return and notice provisions of section 6033 of the Code for any tax year subsequent to that in which all assets are distributed by X to Y, provided that X does not receive any assets and does not engage in any activity at any time after such distribution.

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

Section 509(a) of the Code describes organizations exempt from federal income tax under section 501(c)(3) of the Code are private foundations subject to the provisions of Chapter 42 of the Code.

Section 507(a)(1) of the Code and section 1.507-1(b)(1) of the Income Tax Regulations provide that a private foundation may voluntarily terminate its private foundation status by submitting to the Internal Revenue Service a statement of its intention to voluntarily terminate its private foundation status pursuant to section 507(a)(1) and by paying any termination tax under section 507(c) of the Code.

Section 507(c) of the Code impose excise tax on a private foundation which voluntarily terminates its private foundation status under section 507(a)(1). This section 507(c) tax is equal to the lower of: (a) the aggregate tax benefits that have resulted from the private foundation's exempt status under section 501(c)(3) or (b) the value of the net assets of the private foundation.

Section 507(b)(2) of the Code concerns the transfer of assets by one private foundation to one or more other private foundations, and provides that each transferee private foundation shall not be treated as a newly created organization.

Section 1.507-3(c)(1) of the regulations indicates that 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 a significant disposition of 25% or more of the transferor foundation's assets.

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

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

Section 1.507-1(b)(9) of the regulations provides that a private foundation which transfers all of its net assets is not required to file annual information returns required by section 6033 of the Code for subsequent tax years after its tax year of such transfer when it has no assets or activities.

Section 1.507-3(a)(5) of the regulations indicates 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 to another private foundation pursuant to section 507(b)(2) of the Code.

Section 1.507-3(a)(7) of the regulations provides that, where a private foundation has transferred all of its assets to another private foundation in a transfer under section 507(b)(2) of the Code, it is not required to exercise expenditure responsibility under section 4945(h) of the Code with respect to such transfer.

Section 1.507-3(a)(8) of the regulations provides that certain tax provisions will carry over to a transferee private foundation that receives a transfer of assets from another private foundation pursuant to section 507(b)(2) of the Code.

Section 1.507-3(a)(9)(i) of the regulations provides that, if a private foundation transfers assets to one or more private foundations which are effectively controlled directly or indirectly within the meaning of section 1.482-1(i)(4) of the regulations by the same persons who effectively control the transferor foundation, each transferee foundation will be treated as if it were the transferor foundation, for purposes of sections 4940 through 4948 and sections 507 through 509 of the Code. Each transferee is treated as its transferor in the proportion which the fair market value of the transferor's assets transferred to the transferee bears to the fair market value of all of the transferor's assets immediately before the transfer.

Section 1.507-3(a)(9)(ii) of the regulations provides that a transfer of assets under section 507(b)(2) of the Code does not relieve the transferor private foundation from filing its own final tax year return as required by section 6043(b) of the Code.

Section 1.507-4(b) of the regulations provides that the tax on termination of private foundation status under section 507(c) of the Code does not apply to a transfer of assets under 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 any termination of the transferor foundation's private foundation status under section 509(a).

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

Section 4941 of the Code imposes excise tax on any act 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 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 annual qualifying distributions under section 4942(g) of the Code for the conduct of exempt purposes.

Revenue Ruling 78-387, 1978-2 C.B. 270, describes the carryover of a transferor private foundation's excess qualifying distributions under section 4942(i) of the Code where the transferor and the transferee foundations are controlled by the same persons under section 1.507-3(a)(9)(i) of the regulations. Under that regulation, the transferee is treated as the transferor so that the transferee can reduce its own distributable amount under section 4942 of the Code by its share of the amount, if any, of the transferor foundation's excess qualifying distributions under section 4942(i) of the Code.

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

Section 4945(d)(4) of the Code requires that, in order to avoid making a taxable expenditure, a transferor private foundation must exercise expenditure responsibility under section 4945(h) of the Code on its grants to another private foundation.

Section 4945(h) of the Code defines expenditure responsibility in terms of the grantor private foundation requiring pre-grant inquiry and post-grant reports as to the grantee private foundation on its uses of the grant.

Section 4945(d)(5) of the Code provides that a taxable expenditure includes any amount expended by a private foundation for purposes other than exempt purposes.

Sections 53.4945-6(c)(3) allows a private foundation to transfer its assets to exempt organizations under section 501(c)(3) of the Code, including private foundations, pursuant to section 507(b)(2) of the Code, without the transfers being taxable expenditures under section 4945 of the Code.

Analysis

1.

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) includes a transfer of assets from one private foundation to one or more other private foundations pursuant to any reorganization or liquidation, including any significant disposition of 25% or more of the transferor private foundation's assets. Because X will make such a disposition by transfer of all of its assets to Y, X's transfer of assets to Y will be a transfer under section 507(b)(2) of the Code.

Under section 507(a)(2)(A) of the Code, X's transfer to Y for exempt purposes under section 501(c)(3) of the Code will not constitute any act or failure to act which would result in tax under Chapter 42 of the Code.

Under section 1.507-4(b) of the regulations, X's transfer of its assets pursuant to section 507(b)(2) of the Code will not cause termination of X's private foundation status under section 509(a) of the Code and will not result in termination tax under section 507(c) of the Code.

2.

X's assets transferred to Y will remain dedicated to exempt purposes under section 501(c)(3) of the Code and, thus, X's transfer of assets to Y will not adversely affect the exemptions from federal income tax under section 501(c)(3) of the Code of X or Y.

3.

Section 507(c) of the Code imposes excise tax on a private foundation which voluntarily terminates its private foundation status pursuant to section 507(a)(1) of the Code. This tax under section 507(c) of the Code is equal to the lower of: (a) the aggregate tax benefits that have resulted from the foundation's exemption from federal income tax under section 501(c)(3) of the Code, or (b) the value of the net assets of the foundation. After X transfer all of its assets to Y, the value of X's assets will be zero when X notifies the Internal Revenue Service of its voluntary termination of private foundation status pursuant to section 507(a)(1) of the Code and, thus, such termination of X's private foundation status under section 509(a) of the Code pursuant to a notice under section 507(a)(1) of the Code will result in zero termination tax under section 507(c) of the Code.

4.

X's transfer of its assets will be for exempt purposes under section 501(c)(3) of the Code to Y which is exempt from federal income tax under section 501(c)(3) of the Code and will not be investment income or a disposition of property subjecting X or Y to tax on investment income under section 4940 of the Code.

5.

Section 1.507-3(a)(9)(i) of the regulations indicates that, if a transferor private foundation transfers assets to one or more private foundations which are controlled, directly or indirectly, by the same persons who control the transferor foundation, each transferee foundation will be treated as if it were the transferor foundation, for purposes of sections 4940 through 4948 and sections 507 through 509 of the Code. Each transferee is treated as the transferor in the proportion which the fair market value of the assets transferred to it bears to the fair market value of all of the assets of the transferor immediately before the transfer. Thus, X's investment income under section 4940 of the Code can be treated as that of its transferee Y, and transferor X's tax on such income under section 4940 of the Code can be paid by its transferee Y.

6.

Under section 53.4946-1(a)(8) of the regulations, transferee Y is not a disqualified person under section 4946 of the Code for purposes of section 4941 of the Code because Y is an organization exempt from federal income tax under section 501(c)(3) of the Code. Because X's transfer of assets to Y will not be a transfer to a disqualified person under section 4946 of the Code, T's transfer will not be an act of self-dealing under section 4941 of the Code.

7.

Section 4942(g)(3) of the Code provides that a transferor private foundation, in order to make a qualifying distribution for its grant to another private foundation, must have adequate records, as required by section 4942(g)(3)(B) of the Code, to show that the transferee private foundation, in fact, subsequently made qualifying distributions that were equal to the amount of the transfer received and that were paid out of the transferee's own corpus within the meaning of section 4942(h) of the Code. Such transferee foundation's qualifying distributions must be expended before the close of the transferee's first tax year after the transferee's tax year in which it received the transfer. Thus, X's transfer of its assets to Y will be counted toward the satisfaction of X's distribution requirements under section 4942 of the Code if, and to the extent that, such amounts transferred by X meet the requirements of section 4942(g)(3) of the Code.

8.

Under section 1.507-3(a)(5) of the regulations, X will not be required to meet recordkeeping requirements, if any, under section 4942(g)(3)(B) of the Code with respect to its transfer of all of its assets to Y.

9.

As in Revenue Ruling 78-387, described above, after X's transfer of all of its assets to Y, X's excess qualifying distributions, if any, under section 4942 of the Code may be used by X or by its transferee Y to reduce the distributable amount of X and/or Y under section 4942 of the Code by the amount, if any, of X's excess qualifying distributions carryover under section 4942(i) of the Code.

Under section 1.507-3(a)(9)(i) of the regulations, X's transfer of all of its assets to Y will allow transferee private foundation Y to be treated as its transferor X under section 4942 of the Code with respect to X's minimum investment return, undistributed income, and qualifying distributions

10.

Because X's transfer of assets will be made for exempt purposes under section 501(c)(3) of the Code to Y which is exempt from federal income tax under section 501(c)(3) of the Code, X's transfer to Y will not be a jeopardizing investment or result in tax under section 4944 of the Code.

11.a.

Section 53.4945-6(c)(3) of the regulations indicates that a private foundation can transfer assets pursuant to section 507(b)(2) of the Code to organizations exempt from federal income tax under section 501(c)(3) of the Code, including private foundations, without the transfers being taxable expenditures under section 4945 of the Code, provided that any expenditure responsibility requirements under section 4945(h) of the Code are met. Thus, X's transfer, which is a transfer of all of its assets that is not subject to the expenditure responsibility requirements of section 4945(h) of the Code, will be made to exempt transferee Y for exempt purposes under section 501(c)(3) of the Code and, thus, will not be a taxable expenditure or result in tax under section 4945 of the Code.

11.b.

Section 1.507-3(a)(7) of the regulations provides that, if a private foundation transfers all of its assets to one or more transferee private foundations pursuant to section 507(b)(2) of the Code, such transferor foundation does not incur any expenditure responsibility requirement under section 4945(h) of the Code with respect to such transfer of all of its assets pursuant to section 507(b)(2) of the Code. Thus, when X transfers all of its assets to Y, pursuant to section 507(b)(2) of the Code, X will not be required to exercise any expenditure responsibility under section 4945(h) of the Code with respect to its transfer of all of its assets to Y pursuant to section 507(b)(2) of the Code.

11.c.

As in section 1.507-3(a)(9)(iii), Example (2), of the regulations, X and Y can have an expenditure responsibility agreement between them whereby transferee Y agrees to assume X's expenditure responsibility, if any, under section 4945(h) of the Code with respect to outstanding expenditure responsibility grants, if any, of X. Thus, transferee private foundation Y can exercise any required expenditure responsibility under section 4945(h) of the Code for any expenditure responsibility grants that might be made by X prior to X's transfer of all of its assets to Y pursuant to section 507(b)(2) of the Code.

11.d.

Under section 1.507-3(a)(9)(i) of the regulations, X's transfer of all of its assets to Y will allow transferee private foundation Y to be treated as its transferor X. Thus, Y's assumption and payment of X's remaining obligations on scholarship grants already awarded by X will not constitute taxable expenditures and will not subject X or Y to tax under section 4945 of the Code.

12.

Under section 1.507-1(b)(9) of the regulations, X will not be required to meet the annual reporting requirements of section 6033 of the Code, for any tax years after the tax year of X's transfer of all of its assets to Y when X will have no assets or activities.

Accordingly, we rule that:

1 . X's transfer of all of its assets to Y will qualify as a transfer pursuant to section 507(b)(2) of the Code, will not constitute 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 of the Code, will not terminate the status of X as a private foundation described in section 509(a) of the Code and exempt from federal income taxation under section 501(a) of the Code, and will not result in the imposition on X of any termination tax under section 507(c) of the Code.

2. X's transfer of all of its assets to Y will not adversely affect the tax-exempt status of Y under sections 501(a) and 509(a) of the Code.

3. If X notifies the Internal Revenue Service that X intends to terminate its private foundation status pursuant to section 507(a)(1) of the Code at least one day after X's transfer of all of its remaining assets to Y, no termination tax under section 507(c) of the Code will be imposed on X.

4. X's transfer of all of its assets to Y will not subject X to any excise tax on net investment income under section 4940 of the Code.

5. The provisions of section 4940 of the Code will apply to Y in the tax year of X's transfer of all of its assets to Y and in any subsequent tax year as if Y were X. Therefore, Y will report the net investment income of X for the tax year of the transfer and will pay any excise tax imposed by section 4940 of the Code with respect to such net investment income.

6. X's transfer of all of its assets to Y will not constitute an act of self-dealing under section 4941 of the Code and will not subject any foundation manager or other disqualified person of X or any foundation manager or other disqualified person of Y to the imposition of tax under section 4941 of the Code.

7. X's transfer of all of its assets to Y will be counted toward the satisfaction of the distribution requirements of X under section 4942 of the Code to the extent that the amounts transferred meet the requirements of section 4942(g) of the Code.

8. X will not be required to comply with the recordkeeping requirements of section 4942(g)(3)(B) of the Code with respect to the transfer of all of its assets to Y.

9. The distribution requirements of section 4942 of the Code will apply to Y in the tax year of the transfer of all of the assets of X to Y and in any subsequent year as if Y were X. Therefore, Y will succeed to the distribution requirements of X for the tax year of the transfer. Y will take into account, for purposes of determining Y's distribution requirements under section 4942 of the Code: X's excess qualifying distributions, if any, with respect to each year preceding the tax year of the transfer; X's undistributed income, if any, with respect to the tax year of the transfer and each preceding year; X's minimum investment return for the tax year of the transfer; and any qualifying distributions made by X during the tax year of the transfer either prior to, or as a result of, the transfer.

10. X's transfer of all of its assets to Y will not constitute jeopardizing investments with respect to X or Y within the meaning of section 4944 of the Code.

11.a. X's transfer of all of its assets to Y will not constitute a taxable expenditure and will not subject X to the imposition of any tax under section 4945 of the Code.

11.b. X will not be required to exercise expenditure responsibility under section 4945(h) of the Code with respect to the transfer to Y except for information return requirements for the year of the transfer.

11.c. Although X does not have any outstanding grants that require the exercise of expenditure responsibility within the meaning of section 4945(h) of the Code and X does not have any plans to make any future grants that would require expenditure responsibility, if, notwithstanding the foregoing, X makes any grants that require expenditure responsibility prior to the transfer of all of its assets to Y, Y will exercise expenditure responsibility for all such grants. Such expenditure responsibility by Y will begin after the transfer by X of all of its assets to Y. Any expenditure responsibility requirements imposed on X with respect to grants made to organizations other than Y will not subject X or Y to the imposition of any tax under section 4945 of the Code, provided that Y exercises such expenditure responsibility.

11.d. Y's assumption and payment of the remaining obligations on the scholarship grants already awarded by X will not constitute taxable expenditures and will not subject Y to the imposition of any tax under section 4945 of the Code.

12. X will not be required to comply with the periodic reporting, return and notice provisions of section 6033 of the Code for any tax year subsequent to that in which all assets are distributed by X to Y, provided that X does not receive any assets and does not engage in any activity at any time after such distribution.

Because this rulings letter could help to resolve any questions, please keep it in your permanent records.

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

Sincerely,

Joseph Chasin
Acting Manager, Exempt Organizations
Technical Group 2