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DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON. O.C. 20224

Date: DEC 1 9 2000

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Dear Sir or Madam:

This is in response to your letter dated September 20, 2000, in which you requested certain rulings with respect to a proposed transfer of assets from B to C.

B is exempt under section 501 (c)(3) of the Internal Revenue Code and is classified as a private foundation under section 509(a). C is exempt under section 501(c)(3) of the Code and is classified as a private foundation under section 509(a). C had no assets as of August 30. 2000.

D, a successful businessman from E who founded F, established a park (G ) on a large parcel of land. D created G as part of a boyhood dream to create a public park which would provide a tranquil oasis for the people of E. Throughout his life, D was dedicated to the care and development of G. D died many years ago.

In keeping with his dedication to G, D's Will expressed a desire that the trustees of B continue to support G as D had done during his lifetime. D did not, however, tie the hands of the trustees and provided some discretion in the trustees as to how B's funds could be distributed. Article IV of D's Will bequeathed a block of non-voting common stock of F to B, the income of which was to be used: "First, so far as may be necessary in the judgment of the trustees or of their corporate successor toward the cost of operating and maintaining G".

The Board of Directors of B, which has been comprised largely of direct descendants of D. has always honored B's dedication to G. G is the largest single grantee of B funds. Today, G

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consists of formal gardens, a carillon tower, tracks, sports fields and a substantial nature area.

As the D family has grown larger and more dispersed geographically, concern has developed among D directors about the continuing commitment of future directors to support G, especially in light of the latitude permitted by the language in D's Will. 'They fear that as time passes, directors who are less familiar with D's legacy will not be dedicated to the support of G as current and prior directors have been.

In light of these concerns, D's directors met in April of 1999 to discuss ways to ensure that D's legacy of support for G could be carried out on a permanent basis. In October of 1999, the directors, with advice of counsel, approved a method to accomplish this objective.

First, several of the directors of B formed C for the primary purpose of supporting G. Effective January 1, 2001, B directors intend to make a grant of approximately one-fourth of its total assets to C which will be restricted for the benefit of G. Because C's purpose is to support G and because the grant to C will be for that purpose, the directors of D can be sure that D's legacy of support for G will be carried out in perpetuity.

B represents that it will exercise expenditure responsibility over its grant to C. B also represents that it will comply with the rules regarding capital endowment grants to private foundations.

The transfer of assets from B to C will not involve any benefit to a disqualified person. B does not seek to have its status as a private foundation terminated and does not wish to be treated as a newly created organization.

Section 507(a) of the Code provides for the voluntary and involuntary termination of private foundation status. It states, in part, that except for transfers described in section 507(b), an organization's private foundation status will be terminated only if (1) the organization notifies the Service of its intent to terminate or (2) there have 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.

Section 507(b)(2) of the Code provides that when a private foundation transfers assets to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization or reorganization, the transferee foundation shall not be treated as a new organization.

Section 1.507-l(b)(7) of the Income Tax Regulations provides that neither a transfer of all of the assets of private foundation, nor a significant disposition of assets (as defined in section 1.507-3(c)(2)) by a private foundation (whether or not any portion of such disposition of assets is made to another private foundation), shall be deemed to result in a termination of the transferor private foundation under section 507(a) of the Code, unless the transferor private foundation elects to terminate pursuant to section 507(a)(l) or section 507(a)(Z) is applicable.

Section 1.507-3(a)(2) of the regulations provides that a transferee organization, in the case of a transfer described in section 507(b)(2) of the Code, shall succeed to the aggregate tax

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benefit of the transferor organization in an amount equal to the amount of such aggregate tax benefit of the transferor organization , multiplied by a fraction the numerator of which is the fair market of the assets (less encumbrances) transferred to such transferee and the denominator of which is the fair market value of the assets of the transferor (less encumbrances) immediately before the transfer. Fair market value is determined at the time of transfer.

Section 1.507-3(a)(5) of the regulations provides that, except as provided in section 1.507-3(a)(9) (which only relates to 507(b)(2) transfers where all net assets are transferred to one or more controlled private foundation), a private foundation is required to meet the distribution requirements of section 4942 of the Code for any taxable year in which it makes a section 507(b)(2) transfer of all or part of its net assets to another private foundation. Such transfer shall itself be counted toward satisfaction to the extent the amount transferred meets the requirements of section 4942(g).

Section 1.507-3(b) of the regulations provides that in order for a transfer of assets, pursuant to any liquidation, merger, redemption, recapitalization. or other adjustment, organization or reorganization, not to be a taxable expenditure, it must be to an organization described in section 501(c)(3) (other than an organization described in section section 509(a)(4) or treated as described in section 501(c)(3) under section 4947.

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

Section 4942 of the Code requires a private foundation to make specified distributions of income for each taxable year, including the year in which it transfers substantial assets to another private foundation under section 507(b)(2). Section 1.507-3(a)(5) of the regulations allows the transferor foundation to count the assets transferred under section 507(b)(2) toward its section 4942 distribution requirement to the extent that the transferee foundation itself makes qualifying distributions from corpus under section 4942(g) by the end of the transferee's first taxable year after the year in which it receives the transfer.

Section 4942(g)(l)(A) of the Code defines qualifying distribution as (A) 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 by the foundation or one or more disqualified persons or (ii) a private foundation which is not an operating foundation, except as otherwise provided; or (B) any amount paid to acquire an asset used directly in carrying out one or more purposes described in section 170(c)(2)(B).

Section 4942(g)(3) of the Code requires that a grantor private foundation, in order to nave a qualifying distribution for its grant to another private foundation, which is not an operating foundation under section 4942(j)(3) of the Code, must have adequate records, as required by section 4942(g)(3)(6) of the Code, to show that the grantee private foundation, in fact, subsequently made qualifying distributions that were equal to the amount of the grant and that were paid out of the grantee's own corpus within the meaning of section 4942(h) of the Code. Such grantee foundation's qualifying distributions out of corpus must be expended before the

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close of the grantee's first tax year after its tax year in which it received the grant

Section 4945(d)(4) of the Code defines the term taxable expenditure to include any amount paid or incurred by a private foundation as a grant to an organization unless (A) the organization is described in subparagraphs (1), (2). or (3) of section 509(a) of the Code or is an exempt operating foundation as defined in section 4940(d)(2) of the Code, or (B) the private foundation exercises expenditure responsibility with to such grant in accordance with section 4945(h) of the Code. The exercise of expenditure responsibility requires the foundation that makes the transfer to keep detailed records of the way the payment is spent by the recipient foundation.

Section 4945(h) of the Code provides that expenditure responsibility referred to in subsection (d)(4) means that the private foundation is responsible to exert all reasonable efforts and to establish adequate procedures (1) to see that the grant is spent solely for the purpose for which made, (2) to obtain full and detailed reports with respect to such expenditures, and (3) to make full and detailed reports to the Secretary

Section 53.4942(a)-3(c)(l) of the Foundation and Similar Excise Taxes Regulations states that a transfer from one private foundation to another private foundation will be a qualifying distribution under section 4942(g) of the Code if (i) Not later than the close of the first taxable year in which such contribution is received, such donee organization makes a distribution equal to the full amount of such contribution and such contribution and such distribution is a qualifying distribution (within the meaning of paragraph (a) of this section, without regard to this paragraph) which is treated under paragraph (d) of this section as a distribution out of corpus (or would be so treated if such section 501(c)(3) organization were a private foundation which is not an operating foundation; and (ii) The private foundation making the contribution obtains adequate records or other sufficient evidence from such donee organization (such as a statement by an appropriate officer, director,or trustee of such organization) showing (except as otherwise provided in this subparagraph) (a) that the qualifying distribution described in subdivision (i) of this subparagraph has been made by such organization, (b) the names and addresses of the recipients of such distribution and the amount received by each, and (c)that the distribution is treated as distribution out of corpus under paragraph (d) of this section (or would be so treated if the donee organization were a private foundation which is not a operating foundation).

Section 53.4945-5(b)(7)(i) of the regulations refers to the rules relating to the extent to which the expenditure responsibility rules contained in section 4945(d)(4) and (h), and this section apply to transfers of assets described in section 507(b)(2).

Section 53.4945-5(c)(2) of the regulations provides that if a private foundation makes a grant described in section 4945(d)(4) to a private foundation which is exempt from taxation under section 501(a) for endowment, for the purchase of capital equipment, or for other capital purposes, the grantor foundation shall require reports from the grantee on the use of the principal and income (if any) from the grant funds. The grantee shall make such reports annually for its taxable year in which the grant was made and the immediately succeeding two taxable years.

Section 53.4945-6(b)(2) of the regulations provides that any expenditures for unreasonable

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administrative expenses, including compensation, consultant fees, and other fees for services rendered, will ordinarily be taxable expenditures under section 4945(d)(5) unless the foundation can demonstrate that such expenses were paid or incurred in the good faith belief that they were reasonable and that the payment or incurrence of such expenses in such amounts was consistent with ordinary business care and prudence. The determination whether an expenditure is unreasonable shall depend upon the facts and circumstances of the particular case.

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)).

Based on the above facts, following the transfer from B to C, B will continue to conduct its charitable activities. C will also conduct its charitable activities.

Because B is not terminating its existence and because there has been no willful, repeated or flagrant act giving rise to liability under Chapter 42. no tax will be imposed on B under section 507(c) as a result of the transfer of assets from B to C.

Since a transfer of assets as described in section 507(b)(2) will not cause a termination of an organization's private foundation status, the transfer from B to C will not terminate B's status as a private foundation under section 507(b)(l).

Because B and C will continue to conduct their individual charitable activities following the transfer of assets from B to C, the proposed transfer of assets will not adversely affect the exempt status of B or C.

B's transfer of assets to C will not be a taxable expenditure under section 4945(d), provided B exercises expenditure responsibility over the grants made to C pursuant to section 4945(d)(4).

Because B, as an organization described in section 501(c)(3) of the Code, is not a disqualified person or substantial contributor with respect to C, the transfer of assets to C will not constitute an act of self-dealing within the meaning section 4941 of the Code. Moreover, for purposes of self-dealing, the directors of B who have voted in favor of a transfer of assets to C are not considered substantial contributors and, hence, disqualified persons by virtue of their votes.

Provided B obtains the documentation required by section 4942(g)(3) of the Code, B will be able to treat as a qualifying distribution the amount of corpus which C transfers to G as well as the amount C spends on administrative expenses out of corpus for the year of B's transfer and the year following the transfer.

Provided the expenses incurred by B and C in the transfer of assets to C meet the "good faith" standard of section 53.4945-6(b)(2), such expenses will not constitute taxable expenditures under section 4945 and will be considered qualifying distributions under section 4942.

Accordingly, based on the information furnished, we rule as follows:

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1. The transfer of assets of B to C will qualify as a transfer pursuant to section 507(b)(2) of the Code and will neither result in the termination of B's private foundation status under section 507(b)(l). nor subject B to the tax imposed by section 507(c) of the Code.

2. The proposed transfer of assets by B to C will not adversely affect the exempt status of B or C under section 501(c)(3) of the Code.

3. Provided B exercises expenditure responsibility over the transferred funds pursuant to section 53.4945-5(c)(2) of the regulations, the proposed transfer of assets by B to C will not be a taxable expenditure by B under section 4945(d).

4. B will not be deemed to have engaged in an act of self-dealing giving rise to excise tax under section 4941 as a result of the transfer by B of one-fourth of its assets to C.

5. The reasonable expenditures for expenses incurred by B and C in connection with this ruling request and in effectuating the proposed transfer of assets will not constitute taxable expenditures under section 4945(d)(5) of the Code and will be considered qualifying distributions under section 4942.

6. B's transfer of assets to C may be counted toward satisfaction of B's own distribution requirements under section 4942(g) of the Code to the extent that the requirements of section 4942(g)(3) of the Code are met.

7. B will not be considered a disqualified person or a substantial contributor with respect to C as a result of the transfer.

8. Members of the Board of Directors of B who vote for the proposed transfer will not be considered disqualified persons or substantial contributors with respect to C as a result of the vote.

We are informing the Ohio TE/GE office of this action. Please keep a copy of this ruling in your organization's permanent records.

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.

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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,

Gerald V. Sack
Manager. Exempt Organizations
Technical Group 4

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