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

Date: MAR 14 2001

S.I.N. 0507.00-00
S.I.N. 4940.00-00
S.I.N. 4941 .OO-00
S.I.N. 4942.00-00
S.I.N. 4944.00-00
S.I.N. 4945.00-00
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Contact Person:
XXXXXXXXXXXXXXX
ID Number:
XXXXXXXXX
Telephone Number:
XXXXXXXXXXXXX

T:EO:B3

Employer Identification Number: xx-xxxxxxx

Legend:

T= XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX
C= XXXXXXXXXXXXXXXXXXXXXXXXXXXX
B= XXXXXXXXXXXXXXXXXX
D= XXXXXXXXXXXXXXXXX
E= XXXXXXXXXXXXX
F= XXXXXXXXXXXXXX
G= XXXXXXXXXXXXX
x=xxxxxxX
y= XXXXXXXXXX

By letter dated July 20, 2000, T and C requested certain rulings under sections 507, 4940, 4941, 4942, 4944 and 4945 of the Internal Revenue Code, in connection with a proposed transaction.

Facts:

T was established by B, the niece of F, pursuant to a written trust agreement with D, its trustee. T is recognized as exempt from federal income tax under section 501(c)(3) of the Code and has been held to be a private foundation within the meaning of section 509(a) of the Code. T was funded with a nominal amount and received approximately 1.5x under the will of B. T made a large distribution to a qualified charity in 1993. Substantially all of T's remaining assets were distributed to other charitable organizations in 1995. As of December 31, 1999, T's remaining assets were less than y.

C is a corporation and received all of its contributions from E, the widow of F. C made qualifying distributions in 1999 and had assets in excess of $190x at the end of 1999.

C has an eleven-person Board of Directors including D and G, his daughter. G is the president of C and D is the vice-president of C. It is represented that D and G effectively control both T and C. C is recognized as exempt from federal income tax under section 501(c)(3) of the Code and has been held to be a private foundation within the meaning of section 509(a) of the Code.

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It is represented that neither T nor C have committed any willful or flagrant acts (or failure to act) that would give vise to liability to **tax** under Chapter 42. Also, it is represented that T will give notice of its intent to terminate within the meaning of section 507 of the Code after receiving the requested rulings.

Further, it is represented that T and C are effectively controlled by the same individuals.

T's Trustee and C's Board of Directors have agreed that T should transfer all of its assets to C. Such proposal was adopted because T's small size makes it impractical to operate. The transfer of T's assets to C will avoid the burdens and obstacles associated with continued operations. T's directors determined that T's purposes could be most efficiently carried out by C if T's assets were transferred to C. Further, T and C state that the proposed transaction will eliminate needless extra expenses associated with the operation of two foundations. Specifically, the proposed transaction will allow more funds to be committed to gifls and grants for exempt purposes.

T represents that, upon the transfer of its assets and its dissolution and liquidation, T will notify the Service of such termination, liquidation and transfer.

It is represented that C will assume liability for any excise tax owed by T on its investment income for the year of the distribution and any subsequent year.

Also, it is represented that T will not treat any amount of the transferred assets as a qualifying distribution under Code section 4942(g).

It is represented that neither T nor C have committed any willful or flagrant acts (or failure to act) that would give vise to liability to tax under Chapter 42.

Law and Rationale:

A Ruling #1, Ruling #2, Ruling #3, Ruling #4, Ruling #18, Ruling #19 and Ruling #20

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

Section 507 of the Code provides that a section 501 (c)(3) exempt organization's classification as a private foundation may be terminated in the ways described respectively in sections 507(a)(l), 507(a)(2), 507(b)(l)(A), and 507(b)(l)(B). Section 507 also concerns, under section 507(b)(2). the transfer of assets by one private foundation to another private foundation(s),

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

Section 507(c) of the Code imposes on each organization referred to in section 507(a) a tax equal to the lower of (1) the amount which the foundation substantiates by adequate records as the aggregate tax benefit resulting from the section 501 (c)(3) status of the foundation, or (2) the value of net assets of such foundation.

Section 1.507-l(b)(l) of the Income Tax Regulations provides in part that a private foundation that wishes to terminate its private foundation status must submit a statement to the district director of its intent to terminate its private foundation status and that such statement must set forth in detail the computation and amount of tax imposed under section 507(c).

Section 1.507-3(a)(l) of the regulations provides that in the transfer of assets from one private foundation to another private foundation pursuant to a reorganization or liquidation. the transferee private foundation shall not be treated as a newly created organization.

Section 1.507-3(a)(2)(i) of the regulations provides that a transferee organization to which this paragraph applies shall succeed to the aggregate tax benefit of the transferor organization. Such amount shall be an amount equal to the amount of such aggregate tax benefit multiplied by a fraction the numerator of which is the fair market value 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 shall be determined as of the time of the transfer.

Section 1.507-3(c)(l) 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 another private foundation pursuant to a reorganization, merger or liquidation.

Section 1.507-3(d) of the regulations provides that a transfer of assets under section 507(b)(2) of the Code will not constitute a termination of the transferor's private foundation status.

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

C's Board of Directors and T's Trustee have concluded that the proposed merger would eliminate needless extra expenses associated with the operation of two foundations. The transfers of assets from T to C will be a transfer of assets described in section 507(b)(2) of the Code because the transfer of funds will be from one private foundation to another pursuant to a merger, as stated in section 1.507-3(c)(1) of the regulations. Under section 1.507-3(d), there is no private foundation termination tax in the case of section 507(b)(2) transfers from one private foundation to one or more other private foundations. Also, since T will make a significant distribution of its assets to C, within the meaning of section 507(b)(2) of the Code, the proposed transfers will not result in the imposition of the foundation termination tax under section 507(c). If T, subsequent to the merger, files a voluntary notice of intent to terminate its private foundation status pursuant to section 507(a)(l), such filing will not result in any termination tax under section 507(c) because the value of T's assets at that time will be zero.

C and T are effectively controlled by the same individuals within the meaning of section 1.482-I (a)(3) of the regulations.

B. Ruling **#5, Ruling #6 and Ruling #7**

Section 1.507-3(a)(2)(iii) of the regulations, Example (1), provides that:

> Pursuant to a transfer described in section 507(b)(2), F, a private foundation, transfers to G, a

private foundation, all of its assets which have a fair market value of $400,000. Immediately before the transfer F's aggregate tax benefit was $200,000, and G's aggregate tax benefit was $300,000. After the transfer G's aggregate tax benefit is $500,000 ($200.000 +$300,000).

Section 1.507-3(a)(8) of the regulations provides that certain tax provisions, listed therein, will carry over to a transferee private foundation that is given a Code section 507(b)(2) transfer of assets from a transferor private foundation.

Section 1.507-3(a)(9)(i) of the regulations provides that if a private foundation transfers all of its net assets to one or more private foundations which are effectively controlled (within the meaning of Sec. 1,482-l (a)(3)), directly or indirectly, by the same person or persons which effectively controlled the transferor private foundation, for purposes of chapter 42 (section 4940 et seq.) and part II of subchapter F of chapter 1 of the Code (sections 507 through 509) such a transferee private foundation shall be treated as if it were the transferor.

Section 1.507-3(a)(9)(iii) of the regulations, Example (1). describes a situation where the trustees of X charitable trust, a private foundation, formed Y charitable corporation, also a private foundation, in order to facilitate the conduct of their activities. The trustees of X are also the directors of Y. Y has the same charitable purpose as X. All of the assets of X are transferred to Y, and Y continues to carry on X's charitable activities. Under such circumstances, Y shall be treated as if it were X for purposes of subdivision (i) of this subparagraph. Thus, for example, Y will be permitted to take advantage of any special rules or savings provisions with respect to chapter 42 to the same extent as X could have if X continued in existence.

Section 1.507-3(a)(7) of the regulations provides that, except as provided in section 1.507-3(a)(9), where the transferor private foundation has disposed of all of its assets, sections 4945(d)(4) and 4945(h) of the Code shall not apply to the transferor or transferee foundations with respect to any "expenditure responsibility" grants made by the transferor foundation, except for any information reporting requirements imposed by section 4945 for any year in which any such transfer is made

Section 4945 of the Code imposes a tax upon a private foundation's making of any taxable expenditure as defined in section 4945(d).

Section 4945(h) of the Code defines expenditure responsibility in terms of the grantor private foundation requiring proper reports from the grantee private foundation on the grantee's uses of the grant. In pertinent part, section 53.4945-5(b)(7) of the Foundation and Similar Excise Tax regulations refers to the rules of section 1.507-3(a)(7) of the regulations, cited above.

Sections 53.4945-6(c)(3) and 1.507-3(b) of the regulations allow a private foundation to make section 507(b)(2) transfers of its assets to organizations exempt under section 501(c)(3) of the Code, not excluding private foundations, without the transfers being taxable expenditures.

The carryover provisions for a Code section 507(b)(2) transfer will be applicable. Similar to section 1.507-3(a)(2)(iii), Example (I), all of C's aggregate tax benefit, as defined in section 507(d) of the Code, will be carried over to T, including C's excess qualifying distribution carryover for the year 2000. In addition, under sections 1.507-3(a)(l) through (8), any other applicable carryover provisions will be applicable to C, the private foundation transferee.

There will be no taxable expenditures under section 4945 of the Code. Section 53.4945-5(c)(3) of the

regulations indicates that no tax on taxable expenditures is involved where there is a reorganization transfer of assets under section 507(b)(2), which is the case here. Also, T has no presently outstanding grants for which expenditure responsibility is being exercised.

C. Ruling #8, Ruling # 9, Ruling #13 and Ruling #14

Section 4942 of the Code requires that a private foundation must make qualifying distributions as defined in section 4942(g)) in amount equal to its distributable amount as defined in section 4942(d).

Section 4942(g)(1)(A) of the Code indicates, in pertinent part, that a private foundation does not make any qualifying distribution under section 4942(g) where the contribution is either: (i) to another organization that is controlled by the transferor or by one or more of the transferor's disqualified persons, or (ii) to any private foundation that is not an operating foundation under section 4942(j)(3), unless the requirements of section 4942(g)(3) are met.

Section 4942(g)(3) of the Code requires that the transferor private foundation, in order to have a qualifying distribution for its grant to another private foundation, must have adequate records to show that the transferee private foundation in fact makes a qualifying distribution that is equal to the amount of the transfer received and that is paid out of the transferee's own corpus within the meaning of section 4942(h). That transferee's qualifying distribution must be expended before the close of the transferee's first taxable year after the transferee's taxable year in which the section 507(b)(2) transfer was received.

Section 1507(a)-3(a)(5) of the regulations provides that except as provided in subparagraph (9) of this paragraph, a private foundation is required to meet the distribution requirements of section 4942 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 of such requirements to the extent the amount transferred meets the requirements of section 4942(g). However, where the transferor has disposed of all of its assets, the record keeping requirements of section 4942(g)(3)(B) shall not apply during any period in which it has no assets. Such requirements are applicable for any taxable year other than a taxable year during which the transferor has no assets.

Section 1.507-3(a)(9)(ii) of the regulations provides that Subdivision (i) of this subparagraph shall not apply to the requirements under sections 6033, 6056. and 6104 which must be complied with by the transferor private foundation, nor to the requirement under section 6043 that the transferor tile a return with respect to its liquidation, dissolution, or termination.

Under section 1.507-3(a)(5) of the regulations, even if a transferor transfers all of its assets to other private foundations, the transferor's obligation to expend for exempt purposes, as required by section 4942(g) of the Code, must still be met. T is responsible for meeting its qualifying distribution requirements under section 4942 of the Code. T represents that it will make sufficient qualifying distributions in the year 2000 to comply with the requirements of section 4942 of the Code.

T is subject to the record-keeping requirements of section 4942(g)(3)(B) of the Code for the tax year of the transfer of its assets to C. In the following tax year T's separate status will cease. Also, all of T's assets will vest in C, and C will succeed to the aggregate tax benefit of T. The record-keeping requirements of section 4942(g)((3)(B) will not be applicable to T in the following tax year because T will

have no assets. However, C will continue to be subject to the record-keeping requirements of section 4942(g)(3)(B).

D. Ruling # 10

Section 4941 of the Code imposes a tax upon any act of self-dealing between a private foundation and any of its disqualified persons as defined in section 4946.

Section 4944(a) of the Code provides for a tax on investments that jeopardize the carrying out of exempt purposes.

Section 53.4946-1 (a)(8) of the regulations provide 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).

There will be no acts of self-dealing under section 4941 of the Code. The transfers of assets are not acts of self-dealing because they are transfers of funds for exempt purposes to another section 501 (c)(3) organization, and, even if controlled by the same persons, the transferee is not considered a disqualified person pursuant to section 53.4946-l (a)(8) of the regulations. Also, the transfer of funds from T to C is a transfer of funds pursuant to a merger and is not an investment that is subject to section 4944 of the Code.

E. Ruling #11, Ruling #12 Ruling #15 and Ruling #17

Section 4940(e) of the Code provides for a reduction of section 4940 taxes where private foundations meet certain distribution requirements.

Section 53.4940-1(a) of the regulations imposes an excise tax of 2 percent of the net investment income of a tax-exempt private foundation. This tax will be reported on the form the foundation is required to file under section 6033 for the taxable year and will be paid annually at the time prescribed for filing such annual return.

Section 53.4945-5(c)(2) of the regulations provides that "[i]f 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 the 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 2 taxable years. Only if it is reasonably apparent to the grantor that, before the end of such second succeeding taxable year, neither the principal, the income from the grant funds, nor the equipment purchased with the grant funds has been used for any purpose which would result in liability for tax under section 4945(d), the grantor may then allow such reports to be discontinued."

Sections 53.4945-6(c)(3) and 1.507-3(b) of the regulations allow a private foundation to make section 507(b)(2) transfers of its assets to organizations exempt under section 501 (c)(3) of the Code, not excluding private foundations, without the transfers being considered to be taxable expenditures.

Section 53.4945-5(c)(2) of the regulations provides that "[i]f 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 the 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 2 taxable years. Only if it is reasonably apparent to the grantor that, before the end of such second succeeding taxable year, neither the principal, the income from the grant funds, nor the equipment purchased with the grant funds has been used for any purpose which would result in liability for tax under section 4945(d), the grantor may then allow such reports to be discontinued."

Section 4942(g)(l)(A) of the Code provides that a qualifying distribution by a private foundation for exempt purposes includes any reasonable and necessary administrative expenses. That section further states, where a transferee is a private foundation which is not an operating foundation under section 4942(j) or is controlled by one or more of the transferor's disqualified persons, a transfer, including the reasonable and necessary administrative expenses, will be a qualifying distribution only to the extent that **the** further requirements of section 4942(g)(3) are met. Thus, T's transfer, and the legal, accounting and other expenses of this ruling and transfer to C, if reasonable in amount, will be qualifying distributions **under section** 4942(g)(l)(A) to the extent that T meets section 4942(g)(3), including having adequate records required under section 4942(g)(3)(B) to show that its transferee C has timely met the distribution out of corpus requirements of section 4942(g)(3).

As provided in Section 4940(e)(6) of the Code, a private foundation which is a successor to another private foundation, section 4940 (e) shall be applied by taking into accountthe experience of such other foundation during a merger. In this case, C will take into account T's qualifying distributions and the assets for each of the **five** tax **years** in the base period. C's qualifying distributions and assets will be adjusted by T's qualifying distributions and assets in each of the five tax years of the base period.

F. Ruling # 16

Section 53.4942(a)-2(c)(2)(i) and (iii) of the regulations state that the following are not to be included in determining the minimum investment return:

> (i) Any future interest (such as a vested or contingent remainder, whether legal or equitable) of a foundation in the income or corpus of any real or personal property, other than a future interest created by the private foundation, after December 31, 1969, until all intervening interests in, and rights to the actual possession or enjoyment of, such property have expired, or, although not actually reduced to the foundation's possession, until such future interest has been constructively received by the foundation, as where it has been credited to the foundation's account, set apart for the foundation, or otherwise made available so that the foundation may acquire it at any time or could have acquired it if notice of intention to acquire had been given;

Section 53.4942(a)-2(c)(3) of the regulations provides generally that the assets used (or held for use) in carrying out the exempt purpose of a foundation is used (or held for use) directly in carrying out the foundation's exempt purpose.

Both T and C will compute their distributable amount and their minimum investment return respectively using the guidelines set **out** in sections 53.4942(a)-2(c)(2) and (c)(3) of the regulations

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Conclusions:

Accordingly, based upon the representations submitted, we conclude that:

(1) The transfer of all of T's assets to C will constitute a transfer described in section 507(b)(2) of the Code, will not cause C to be treated as a newly created organization, will not terminate T's private foundation status, and will not cause the imposition of a termination tax under section 507(c) of the Code.

(2) The transfer of all of T's assets to C will not affect either organization's exemption under section 501(c)(3) of the Code.

(3) Upon the transfer of all of T's assets to C, C will succeed to T's aggregate tax benefit under section 507(d) of the Code.

(4) Upon the transfer of all of T's assets to C, C will be treated as if it were T for purposes of Chapter 42 of the Code (sections 4940 et seq) and Chapter 1, Subchapter F. part II of the Code (sections 507 through 509).

(5) Upon the transfer of all of T's assets to C, C will be responsible for any liabilities under Chapter 42 of the Code to the extent that T does not satisfy those liabilities.

(6) The transfer of all of T's assets to C will not constitute a taxable expenditure under section 4945 of the Code, and T will not be required to exercise expenditure responsibility or to comply with the information reporting requirements of section 4945, either for the tax year in which the transfer is made or for any subsequent year, with respect to the transfer to C.

(7) Payments by C, if any, to organizations described in sections 509(a)(l), (2), or (3) of the Code, of grants awarded but not yet disbursed by T will not constitute taxable expenditures by C under section 4945 of the Code.

(8) The legal, accounting, and other necessary expenses incurred to implement the transfer, if reasonable in amount, will be paid to accomplish a purpose described in section 170(c)(1) or 170(c)(2)(B) of the Code. Thus, the expenses, if reasonable, will constitute qualifying distributions under section 4942 of the Code and not taxable expenditures under section 4945 of the Code as to T or C.

(9) T will not be required to comply with the record-keeping requirements of section 4942(g)(3)(B) of the Code because of its transfer of all of its assets to C. Also, T will not be required to file any tax information statement or returns under section 6033 of the Code for any tax year subsequent to its tax year in which the transfer is completed.

(10) The transfer of all of T's assets to C will not constitute an act of self-dealing under section 4941 of the Code or an investment that jeopardizes charitable purposes under section 4944 of the Code.

(11) The transfer of all of T's assets to C will not trigger any gross investment income or capital gain net income under section 4940 of the Code. The tax bases and holding periods of the assets transferred by T will carry over to C for purposes of section 4940 of the Code.

(12) Following the transfer of all of T's assets to C, C may retain its calendar tax year and also its cash basis method of accounting for Form 990-PF reporting purposes.

(13) When T transfers its assets to C, T's undistributed income under section 4942(c) of the Code, if any, for T's tax year that ended on the December 31 immediately preceding the date of transfer should be distributed by C on or before the next December 31, the same date that was required by section 4942 of the Code for T.

(14) After T transfers all of its assets to C, T's excess qualifying distributions carryover under section 4942(i) of the Code, if any, may be used by C to reduce C's distributable amount under section 4942 of the Code.

(15) After T transfers all of its assets to C, T's excise tax liability under section 4940 of the Code for its final tax year may be subject to satisfaction by C, and any refund to which T is entitled may be used by C to offset its section 4940 excise tax. No taxes under Chapter 42 of the Code will be imposed on T or C for C's payment of any excise tax liability of the Trust.

(16) T, whose tax years end on December 31, will, for purposes of its final Form 990-PF return, compute its minimum investment return by multiplying the fair market value of its assets held during such last tax year, other than those assets excluded by sections 53.4942(a)-2(c)(2) and (3) of the Regulations, by a prorating percentage detenined by multiplying five percent by a fraction whose numerator will be the number of days in the tax year of T, up to and including the date of transfer, and whose denominator will be either 365 or 366, the number of days in the full tax year of T.

C, whose tax years end on December 31, will compute its minimum investment return (with respect to the assets received from T) for C's tax year in which the transfer occurs by multiplying the fair market value of each asset that C receives from T, other than those assets excluded by sections 53.4942(a)-2(c)(2) and (3) of the Regulations, by a fraction whose numerator will be the number of days in C's tax year that C holds the asset and whose denominator will be either 365 or 366, the number of days in the full tax year of C.

T's distributable amount for the period in its tax year through the date when the transfer of its assets is completed, using the minimum investment return as computed above, will be added to C's distributable amount, as computed above, for C's tax year in which the assets transfer is completed. This combined distributable amount will be in C's distributable amount for its tax year in which the assets transfer is completed.

(17) Under section 4940(e) of the Code, the amount of qualifying distributions made, and the assets for each of the five tax years in the base period and for the tax year for which the section 4940(e) calculation is made, will be adjusted by increasing the amount of C's qualifying distributions and assets for each such year by the qualifying distributions made by T during its tax year, and the assets of T for its tax year, which ends concurrently with C's tax year.

(18) If T notifies the Service, at least one day after all of its net assets are transferred to C, that T intends to terminate its private foundation status, that notice will be effective to terminate the private foundation status of T under section 507(a)(l) of the Code.

(19) This ruling request and the provisions of this letter do not constitute notice of an intent to

terminate the private foundation status of the Trust.

(20) If the value of the net assets of T equal zero at the time T notifies the Service that it intends to terminate its private foundation status and dissolves, T will not be liable for any termination tax under section 507(c) of the Code.

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. We are sending a copy of this ruling letter to your attorney.

Sincerely yours,

/S/

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

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