

## SECTION 1. PURPOSE

The purpose of this revenue procedure is to set forth guidelines under which grant-making private foundations will not be considered to be responsible for substantial and material changes in the sources of financial support of recipient organizations that are described in sections 170(b)(1)(A)(vi) or 509(a)(2) of the Internal Revenue Code.

## SEC. 2. BACKGROUND

01. Generally, under section 1.170A-9(e)(4)(v)(b), 1.170A-9(e)(5)(iii)(c), 1.509(a)-3(c)(l)(iii), and 1.509(a)-3(e)-3 of the Income Tax Regulations, when an organization has received a ruling or determination letter, or an advance ruling or determination letter, that it has been classified as a publicly supported organization described in sections 170(b)(1)(A)(vi) or 509(a)(2) of the Code, the treatment of grants and contributions and the status of grantors and contributors to the organization under sections 170, 507, 545(b)(2), 556(b)(2), 642(c), 4942, 4945, 2055, 2106(a)(2), and 2522 will not be affected by a subsequent loss of classification as publicly supported organization until notice of loss of classification is published. However, a grantor or contributor may not rely on such an organization's classification if the grantor or contributor is responsible for or aware of a substantial and material change in the organization's sources of support that subsequently results in the organization's loss of classification as a publicly supported organization. For example, a substantial and material change in sources of support may result from the receipt of an unusually large contribution that does not qualify as an unusual grant under sections 1.170A-9(e)(6)(ii) or 1.509(a)-3(c)(3). See Sec. 2.01 of Rev. Proc. 81-6, 1981-1 C.B. 620.

02. If any taxable year there is a substantial and material change in an organization's sources of support, the computation period used to determine whether the organization meets the requirements of the section 170(b)(1)(A)(vi) or 509(a)(2) financial support tests consists of the taxable year in question and the four immediately preceding taxable years rather than the four immediately preceding taxable years. If an organization has been in existence for less than five taxable year, the computation period consists of the taxable year in question and the number of years preceding that taxable year that the organization has been in existence. This computation period is in lieu of the usual computation period rules. See sections 1.170A-9(e)-(4)(v) and 1.509(a)-3(c)(l)(ii) of the regulations and Sec. 2.02 of Rev. Proc. 81-6.

03. Gifts, grants and contributions made by a private foundation to another private foundation are not qualifying distributions under section 4942(g) of the Code unless the recipient is either (i) an operating foundation under section 4942(j)(3) or (ii) a pass-through foundation under section 4942(g)(3) from which the grantor obtains the records required by section 4942(g)(3)(B). Therefore, a private foundation may not be able to count a grant, for instance, as a qualifying distribution if the grant causes the recipient organization to lose its classification as a public charity.

04. Gifts, grants and contributions made by a private foundation to another private foundation are taxable expenditures under section 4945(d)(4) of the Code unless either (i) the recipient is an exempt operating foundation under section 4940(d)(2) or (ii) the grantor exercises expenditure responsibility under section 4945(h). Therefore, a private foundation may be subject to the section 4945(a) tax on taxable expenditures if it has not followed the expenditure responsibility requirements of section 4945(d)(4) in regard to a grant that causes the recipient organization to lose its classification as a public charity.

05. Rev. Proc. 81-6 set forth guidelines under which a grantor or contributor will not be considered to be responsible for substantial and material changes in a organization's sources of support. Generally, these guidelines provide that a grantor or contributor will not be considered to be responsible for a substantial and material change in an organization's support if the aggregate of gifts, grants, or contributions received from such grantor or contributor for a taxable year is 25 percent or less of the aggregate support received by the donee organization from all sources other than that donor for the four taxable years immediately preceding such taxable year, or, if the donee organization has been in existence for fewer than five taxable years, the number of years for which the organization has been in existence prior to the taxable year being tested.

06. In 1984, Congress directed the Treasury Department to amend its regulations to permit greater reliance by private foundations on Internal Revenue Service classifications of new organizations in the first five years of their existence and in any other circumstances in which Treasury concludes that greater reliance is appropriate. H.R. Conf. Rep. No. 861, 98th Cong., 2d Sess. 1090 (1984), 1984-3 (Vol. 2) C.B. 344, Pending the issuance of regulations implementing the above directions, the Internal Revenue Service will follow the guidelines set forth below.

### SEC. 3. GUIDELINES

01. Private foundations may continue to rely on the status of recipient organizations that have received rulings or determination letters to the extent provided in sections 1.170A-9(e)(4)(v)(b) and 1.509(a)-3(c)(I)(iii) of the regulations, and on the status of recipient organizations that have received advance rulings or determination letters to the extent provided in sections 1.170A-9(e)-(5)(iii)(c) and 1.509(a)-3(e)(3).

02. All grantors and contributors, including private foundations, may continue to rely on the guidelines set forth in Rev. Proc. 81-6.

03. In addition, a private foundation's gift, grant or contribution will not cause the private foundation to be considered to be responsible for, or aware of, a substantial and material change in the recipient organization's sources of support that results in the loss of the recipient organization's status under sections 170(b)(A)(vi) or 509(a)(2) of the Code if the following conditions are met at the time of the making of the gift, grant or contribution:

(1) The recipient organization has received a ruling or determination letter, or an advance ruling or determination letter, that it is described in sections 170(b)(1)(A)(vi) or 509(a)(2);

(2) Notice of a change of the recipient organization's status under sections 170(b)(1)(A)(vi) or 509(a)(2) has not been made to the public (such as by publication in the Internal Revenue Bulletin), and the private foundation has not acquired knowledge that the Internal Revenue Service has given notice to the recipient organization that it will be deleted from such status; and

(3) The recipient organization is not controlled directly or indirectly by the private foundation. A recipient organization is controlled by a private foundation for this purpose if the private foundation and disqualified persons (defined in section 4946(a)(1)(A) through (G)) with reference to the private foundation, by aggregating their votes or positions of authority may require the recipient organization to perform any act which significantly affects its operations or may prevent the recipient organization from performing such act.

#### SEC. 4 AREAS NOT COVERED BY THIS REVENUE PROCEDURE

01. This revenue procedure does not apply to situations in which gifts, grants, or contributions are made by persons other than private foundations.

02. This revenue procedure does not affect Rev. Proc. 81-7, 1981-1 C.B. 621, under which grants will be considered to be unusual grants.

#### SEC. 5 EFFECT ON OTHER DOCUMENTS

Rev. Proc. 81-6, 1981-1 C.B. 620, is amplified.

#### SEC. 6. EFFECTIVE DATE

This revenue procedure is effective for grants made after March 13, 1989.

#### DRAFTING INFORMATION

The principal author of this revenue procedure is V. Moore of the Office of Assistant Chief Counsel (Employee Benefits and Exempt Organizations). For further information regarding this revenue procedure contact Robert Fontenrose on (202) 566-4134.