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

200140084

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date:
JUL 10 2001

Contact Person:

Identification Number:

Telephone Number:

T:EO:B2

Employer Identification Number:

LEGEND

X =
Y =

UIL Nos.
501.03-00
507.00-00
507.05-00
4940.00-00
4941.04-00
4942.03-05
4944.00-00
4945.04-05

Dear Sir or Madam:

We have considered your ruling request dated January 16, 2001 requesting a ruling regarding a proposed transfer of assets under section 507(b)(2) of the Internal Revenue Code.

X is a trust. Y is a corporation . The Trust and the Corporation are both private foundations described in sections 501(c)(3) and 509(a) of the Code. The same persons effectively control both the Trust and the Corporation.

In order that the Trust may operate in corporate form, and in order to realize administrative cost savings and eliminate duplication of effort, the Trust proposes to transfer all of its assets to the Corporation, and then terminate.

Y requests the following rulings:

1. The transfer of all of the assets of the Trust to the Corporation ("Final Distribution") will not result in the termination of the Trust's private foundation status pursuant to section 507(a) of the Code, and will not result in the imposition of any termination tax under section 507(c), because the transfer constitutes a reorganization between private foundations within the meaning of section 507(b)(2).

2, If the Trust makes the Final Distribution to the Corporation at least one day before it notifies the IRS of its intent to terminate its private foundation status under section 507(a)(1) of the Code, no tax will be due from the Trust pursuant to section 507(c) because the Trust will then have no assets.

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3. Under section 507(b)(2) of the Code and section 1.507-3(a)(1) of the Income Tax Regulations, the Corporation will not be treated as a newly created organization as a result of the Final Distribution from the Trust to the Corporation.

4. The Final Distribution will not adversely affect the tax-exempt status of the Trust or the Corporation under section 501(c)(3) of the Code, and neither the Trust nor the Corporation will be subject to federal income tax under Subtitle A with respect to the Final Distribution.

5. Under section 1.507-3(a)(9) of the regulations, the Corporation will be treated as if it were the Trust for purposes of chapter 42 of the Code (sections 4940 et seq.) and sections 507 through 509. All of the Trust's aggregate tax benefits as defined in section 507(d)(1) will be carried over to the Corporation.

6. The Final Distribution from the Trust to the Corporation will not result in tax on investment income under section 4940 of the Code. After the Trust makes the Final Distribution to the Corporation, the Trust's excise tax liability under section 4940 for its final year may be satisfied by the Corporation, and any refund to which the Trust is entitled may be used by the Corporation to offset its excise tax under section 4940.

7. The Final Distribution from the Trust to the Corporation will not be an act of self-dealing under section 4941 of the Code.

8. The Final Distribution from the Trust to the Corporation will result in the Corporation being treated as if it were the Trust for purposes of section 4942 of the Code, so that:

(a) the Trust's distribution requirements under section 4942 for the year of the transfer may be fulfilled by the Corporation;

(b) all qualifying distributions made by the Trust during its taxable year in which the Final Distribution occurs may be treated as if made by the Corporation in its tax year of receipt of the Trust's assets, and all qualifying distributions made by the Corporation following the date of the Final Distribution shall satisfy the distribution requirements of the Trust for periods prior to making the Final Distribution to the Corporation:

(c) the Corporation may reduce its required distributions under section 4942, including those for the Corporation's tax year of the Final Distribution, by the amount, if any, of the Trust's excess qualifying distributions carryover under section 4942(i) as of the time of the Final Distribution; and

(d) the Trust will not be required to comply with the record keeping requirements of section 4942(g)(3)(B) with regard to its Final Distribution to the Corporation.

9. The proposed Final Distribution from the Trust to the Corporation will not constitute an investment by the Trust or the Corporation which jeopardizes the exempt purposes of either the Trust or the Corporation under section 4944 of the Code.

10. The proposed Final Distribution from the Trust to the Corporation will not constitute a taxable expenditure under section 4945(d) of the Code, and neither the Trust nor the Corporation will be required to exercise expenditure responsibility with respect to the Final Distribution. To the extent that the Trust has any obligation which requires the exercise of expenditure responsibility under section 4945 at the time of the Final Distribution, the Corporation will exercise expenditure responsibility with respect to such obligations.

11. Under sections 1.507-1(b)(9) and 1.507-3(a)(9)(1) of the regulations, the Trust will not be required to file its annual information return required by section 6033 of the Code for any taxable year following the taxable year in which the proposed Final Distribution occurs, if during the subsequent taxable years the Trust has neither legal nor equitable title to any assets and engages in no activity. Upon the Trust's termination, the Trust will file its final information return as required by section 6043(b).

Section 507(a) of the Code provides that except as provided in 507(b), the status of any organization as a private foundation shall be terminated only if--

(1) such organization notifies the Secretary of its intent to accomplish such termination (at such time and in such manner as the Secretary may by regulations prescribe), or

(2) (A) with respect to such organization, 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, and (B) the Secretary notifies such organization that, by reason of section 507(a)(2)(A), such organization is liable for the tax imposed by section 507(c),

and either such organization pays the tax imposed by section 507(c) (or any portion not abated under section 507(g)) or the entire amount of such tax is abated under section 507(g).

Section 507(b)(2) of the Code provides that in the case of a transfer of assets of any private foundation 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 newly created organization.

Section 4940 of the Code imposes an excise tax on the net investment income (including capital gain net income) of private foundations.

Section 4940(c)(4)(A) of the Code provides that for purposes of determining capital gain net income, there shall be taken into account only gains and losses from the sale or other disposition of certain property.

Section 4941(d)(1) of the Code defines "self-dealing" as certain direct or indirect transactions between a disqualified person and a private foundation.

Section 4942 of the Code generally imposes a tax on private foundations for failure to distribute annually a certain minimum percentage of the fair market value of certain property owned by it, and allows a carryover to future years of excess qualifying distributions.

Section 4944 of the Code generally imposes a tax on private foundations which invest any amount in a manner which jeopardizes the carrying out of their exempt purposes.

Section 4945(d) of the Code defines a "taxable expenditure" as certain amounts paid or incurred by a private foundation.

Section 1.507-1(b)(6) of the regulations provides that if a private foundation transfers all or part of its assets to one or more other private foundations pursuant to a transfer described in section 507(b)(2) of the Code and section 1.507-3(c) of the regulations, such transferor foundation will not have terminated its private foundation status under section 507(a)(1) of the Code.

Section 1.507-1(b)(7) of the regulations provides that neither a transfer of all of the assets of a private foundation nor a significant disposition of assets by a private foundation shall be deemed to result in a termination of the transferor private foundation under section 507(a) unless the transferor private foundation elects to terminate pursuant to section 507(a)(1) or section 507(a)(2) is applicable.

Section 1.507-1(b)(9) of the regulations provides that where a private foundation transfers all of its net assets, neither such foundation nor its foundation managers will be required to file an annual information return under section 6033 for any taxable year following the taxable year in which the last of such transfers occurred, if at no time during the subsequent taxable years in question the foundation has legal or equitable title to any assets or engages in any activity.

Section 1.507-3(a)(1) of the regulations provides that in the case of a significant disposition of assets to one or more private foundations within the meaning of section 1.507-3(c), the transferee organization shall not be treated as a newly created organization, but as possessing those attributes and characteristics of the transferor organization which are described in section 1.507-3(a)(2), (3), and (4).

Section 1.507-3(a)(5) of the regulations provides that except as provided in section 1.507-3(a)(9), 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 recordkeeping 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)(7) of the regulations provides that except as provided in section

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1.507-3(a)(9), where the transferor has disposed of all of its assets, during any period in which the transferor has no assets, section 4945(d)(4) and (h) shall not apply to the transferee or the transferor with respect to any "expenditure responsibility" grants made by the transferor. However, the exception contained in this subparagraph shall not apply with respect to any information reporting requirements imposed by section 4945 and the regulations thereunder for any year in which any such transfer is made.

Section 1.507-3(a)(9)(i) of the regulations provides that if a private foundation transfers all of its assets to one or more private foundations which are effectively controlled (within the meaning of section 1.482-1(a)(3) of the regulations), directly or indirectly, by the same person or persons which effectively controlled the transferor private foundation, then 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 (with certain exceptions in section 1.507-3(a)(9)(ii) of the regulations). However, where proportionality is appropriate, such a transferee private foundation shall be treated as if it were the transferor in the proportion which the fair market value of the assets (less encumbrances) transferred to such transferee bears to the fair market value of the assets (less encumbrances) of the transferor immediately before the transfer.

In Example (2) of Section 1.507-3(a)(9)(iii) of the regulations, A and B are the trustees of the P charitable trust, a private foundation, and are the only substantial contributors to P. On July 1, 1973, in order to facilitate accomplishment of diverse charitable purposes, A and B create and control the R Foundation, the S Foundation and the T Foundation and transfer the net assets of P to R, S, and T. As of the end of 1973, P has an outstanding grant to Foundation W and has been required to exercise expenditure responsibility with respect to this grant under sections 4945(d)(4) and (h) of the Code. Under these circumstances, R, S, and T shall each be treated as if they are P in the proportion the fair market value of the assets transferred to each bears to the fair market value of the assets of P immediately before the transfer. Since R, S, and T are treated as P, absent a specific provision for exercising expenditure responsibility with respect to the grant to W, each of them is required to exercise expenditure responsibility with respect to such grant. If, as a part of the transfer to R, P assigned, and R assumed, P's duties with respect to the expenditure responsibility grant to W, only R would be required to exercise expenditure responsibility with respect to the grant to W. Since R, S, and T are treated as P rather than as recipients of "expenditure responsibility" grants, there are no expenditure responsibility requirements which must be exercised under sections 4945(d)(4) and (h) with respect to the transfers of assets to R, S, and T.

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

Section 1.507-3(c)(1) of the regulations provides that for purposes of section 507(b)(2) of the Code, the terms "other adjustment, organization, or reorganization" shall include any partial liquidation or any other significant disposition of assets to one or more private foundations, other than transfers for full and adequate consideration or distributions out of current income.

Section 1.507-3(c)(2) of the regulations provides that the term "significant disposition of assets to one or more private foundations" includes any disposition for a taxable year where the aggregate of the dispositions to one or more private foundations for the taxable year is 25% or more of the fair market value of the net assets of the distributing foundation at the beginning of the taxable year.

Section 1.507-3(d) of the regulations provides that unless a private foundation voluntarily gives notice pursuant to section 507(a)(1) of the Code, a transfer of assets described in section 507(b)(2) of the Code will not constitute a termination of the transferor's private foundation status under section 507(a)(1) of the Code. Such transfer must, nevertheless, satisfy the requirements of any pertinent provisions of chapter 42.

Section 53.4941(d)-2(f)(2) of the Foundations and Similar Excise Taxes Regulations provides that the fact that a disqualified person receives an incidental or tenuous benefit from the use by a foundation of its income or assets will not, by itself, make such use an act of self-dealing. For example, a grant by a private foundation to a section 509(a)(1), (2), or (3) organization will not be an act of self-dealing merely because one of the section 509(a)(1), (2), or (3) organization's officers, directors, or trustees is also a manager of the foundation.

Section 53.4945-5(b)(7) of the regulations cross-references 1.507-3(a)(7) and (9) of the regulations for rules relating to the extent to which the expenditure responsibility rules contained in sections 4945(d)(4) and (h) of the Code 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) of the Code 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 53.4945-6(c)(3) of the regulations generally provides that if a private foundation makes a section 507(b)(2) transfer of assets to any person, the transferred assets will not be considered used exclusively for purposes described in section 170(c)(2)(B) of the Code unless the assets are transferred to a fund or organization described in section 501(c)(3) of the Code.

Section 53.4946-1(a)(8) of the regulations provides that, for purposes of section 4941 of the Code only, the term "disqualified person" shall not include an organization which is described in section 501(c)(3) (other than an organization described in section 509(a)(4)).

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Each of the requested rulings is discussed in turn below.

1. Under section 1.507-3(c)(1) of the regulations, 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 any other reorganization, including a significant disposition of 25% or more of the transferor foundation's assets. Because the Trust will transfer all of its assets to the Corporation as a donation for no consideration, the Trust's Final Distribution will be a significant disposition of its assets under section 1.507-3(c)(1) of the regulations, and thus will be a transfer under section 507(b)(2) of the Code.

Under section 1.507-3(d) of the regulations, the Trust's Final Distribution to the Corporation pursuant to section 507(b)(2) of the Code will not terminate the Trust's private foundation status under section 509(a), because the Trust will not at the time of the transfer notify the IRS that it intends to terminate its status as a private foundation pursuant to section 507(a)(1).

Under section 1.507-4(b) of the regulations, the Trust's Final Distribution to the Corporation pursuant to section 507(b)(2) of the Code will not result in termination tax under Section 507(c) on either the Trust or the Corporation.

2. Under Section 507(e) of the Code, the value of the Trust's assets after the Final Distribution to the Corporation will be zero. Thus, the Trust's subsequent voluntary notice of termination of its private foundation status pursuant to Section 507(a)(1) will not result in tax under Section 507(c) of the Code. It is assumed that section 507(a)(2) will not apply at the time of the notice.

Under section 507(a)(1) of the Code, when the Trust notifies the Internal Revenue Service (at least one day after the Trust's Final Distribution to the Corporation) of its intent to voluntarily terminate its private foundation status pursuant to section 507(a)(1) of the Code, the Trust will terminate its private foundation status.

3. Under section 1.507-3(a)(1) of the regulations, the Trust's Final Distribution to the Corporation pursuant to section 507(b)(2) of the Code will not result in the Corporation being treated as a newly created organization.

4. Because the Trust's Final Distribution to the Corporation will be for exempt purposes to an organization exempt from federal income tax under section 501(c)(3) of the Code, the Trust's transfer will not adversely affect the exemptions of the Trust or the Corporation under section 501(c)(3) of the Code, and neither the Trust nor the Corporation will be subject to federal income tax under subtitle A of the Code with regard to the transfer.

5. Under section 1.507-3(a)(9) of the regulations, the Corporation is effectively controlled by the same persons who effectively control the Trust, and thus the transferee Corporation will be treated as if it were the transferor Trust for purposes of Chapter 42 and sections 507 through 509 of the Code.

Under section 1.507-3(a)(2)(i) of the regulations, upon the Trust's Final Distribution to the Corporation, the Corporation will succeed to the Trust's aggregate tax benefits under section 507(d) of the Code.

6. Because the Corporation is treated as the Trust under section 1.507-3(a)(9) of the regulations, the Trust's transfer of all of its assets to the Corporation is not a sale or disposition for purposes of Section 4940 of the Code. Moreover, the Trust will receive no taxable consideration for the disposition.

7. Section 4941(d)(1) of the Code generally defines acts of self-dealing as certain transactions between private foundations and disqualified persons. Section 53.4946-1(a)(8) of the regulations provides that for purposes of self-dealing, a section 501(c)(3) organization generally is not a disqualified person. Section 53.4941(d)-2(f)(2) of the regulations also indicates that a grant by a private foundation to a section 509(a)(1), (2), or (3) organization will not be an act of self-dealing merely because one of the section 509(a)(1), (2), or (3) organization's officers, directors, or trustees is also a manager of the foundation.

8. Under section 1.507-3(a)(9)(i) of the Regulations, the Trust's transfer will result in the Corporation being treated as if it were the Trust for purposes of section 4942 of the Code, so that:

a. The Trust's distribution requirements under section 4942 for its tax year of its transfer may be satisfied by the Corporation.

b. The Trust's qualifying distributions during its tax year of its transfer may be treated as made by the Corporation in its tax year of receipt of Trust's assets. The Final Distribution itself is not treated as a qualifying distribution under section 4942, because the Corporation is treated as the Trust.

c. As in Rev. Rul. 78-387, the Corporation may reduce its required distributions under section 4942, including those for the Corporation's tax year of the transfer, by the amount, if any, of the Trust's excess qualifying distributions carryover under section 4942(i) as of the time of the transfer.

d. Under section 1.507-3(a)(5) of the regulations, a foundation is not required to comply with the record-keeping requirements of section 4942(g)(3)(B) of the Code when it has no assets. However, the Final Distribution is not treated as a qualifying distribution (or other distribution) under section 4942, because the Corporation is treated as the Trust.

9. Under section 4944 of the Code, the Trust's donation will be made for exempt purposes, will not be an "investment" within the common meaning of the term, and will not result in tax under that section as to the Trust or Corporation.

10. A private foundation's donation of assets to another for endowment purposes is ordinarily treated as a grant to which expenditure responsibility applies. See section 53.4945-5(c)(2) of the regulations. One exception applies under section 1.507-3(a)(7) when the

grantor has no assets. Another exception, applicable here, applies under section 1.507-3(a)(9) where the transferee is treated as the transferor. See section 1.507-3(a)(9)(iii), Example (2). However, the Corporation must continue to exercise any outstanding expenditure responsibility of the Trust under section 4945(b) of the Code with respect to any grants made by the Trust prior to the Final Distribution.

11. Under section 1.507-1(b)(9) of the regulations, the Trust will not be required to file any returns under section 6033 of the Code for any tax year subsequent to the tax year of the Final Distribution to the Corporation when the Trust will have no assets. The Trust must file its return required by section 6043(b) with respect to its dissolution.

Accordingly, we rule as follows:

1. The transfer of all of the assets of the Trust to the Corporation ("Final Distribution") will not result in the termination of the Trust's private foundation status pursuant to section 507(a) of the Code, and will not result in the imposition of any termination tax under section 507(c), because the transfer constitutes a reorganization between private foundations within the meaning of section 507(b)(2).

2, If the Trust makes the Final Distribution to the Corporation at least one day before it notifies the IRS of its intent to terminate its private foundation status under section 507(a)(1) of the Code, no tax will be due from the Trust pursuant to section 507(c) because the Trust will then have no assets.

3. Under section 507(b)(2) of the Code and section 1.507-3(a)(1) of the Income Tax Regulations, the Corporation will not be treated as a newly created organization as a result of the Final Distribution from the Trust to the Corporation.

4. The Final Distribution will not adversely affect the tax-exempt status of the Trust or the Corporation under section 501(c)(3) of the Code, and neither the Trust nor the Corporation will be subject to federal income tax under Subtitle A with respect to the Final Distribution.

5. Under section 1.507-3(a)(9) of the regulations, the Corporation will be treated as if it were the Trust for purposes of chapter 42 of the Code (sections 4940 et seq.) and sections 507 through 509. All of the Trust's aggregate tax benefits as defined in section 507(d)(1) will be carried over to the Corporation.

6. The Final Distribution from the Trust to the Corporation will not result in tax on investment income under section 4940 of the Code. After the Trust makes the Final Distribution to the Corporation, the Trust's excise tax liability under section 4940 for its final year may be satisfied by the Corporation, and any refund to which the Trust is entitled may be used by the Corporation to offset its excise tax under section 4940.

7. The Final Distribution from the Trust to the Corporation will not be an act of self-dealing under section 4941 of the Code.

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8. The Final Distribution from the Trust to the Corporation will result in the Corporation being treated as if it were the Trust for purposes of section 4942 of the Code, so that:

(a) the Trust's distribution requirements under section 4942 for the year of the transfer may be fulfilled by the Corporation;

(b) all qualifying distributions made by the Trust during its taxable year in which the Final Distribution occurs may be treated as if made by the Corporation in its tax year of receipt of the Trust's assets, and all qualifying distributions made by the Corporation following the date of the Final Distribution shall satisfy the distribution requirements of the Trust for periods prior to making the Final Distribution to the Corporation:

(c) the Corporation may reduce its required distributions under section 4942, including those for the Corporation's tax year of the Final Distribution, by the amount, if any, of the Trust's excess qualifying distributions carryover under section 4942(i) as of the time of the Final Distribution; and

(d) the Trust will not be required to comply with the record keeping requirements of section 4942(g)(3)(B) with regard to its Final Distribution to the Corporation, because the Final Distribution will not be treated as a distribution by the Trust for purposes of section 4942.

9. The proposed Final Distribution from the Trust to the Corporation will not constitute an investment by the Trust or the Corporation which jeopardizes the exempt purposes of either the Trust or the Corporation under section 4944 of the Code.

10. The proposed Final Distribution from the Trust to the Corporation will not constitute a taxable expenditure under section 4945(d) of the Code, and neither the Trust nor the Corporation will be required to exercise expenditure responsibility with respect to the Final Distribution. To the extent that the Trust has any obligation that requires the exercise of expenditure responsibility under section 4945 at the time of the Final Distribution, the Corporation must exercise expenditure responsibility with respect to such obligations.

11. Under sections 1.507-1(b)(9) and 1.507-3(a)(9)(1) of the regulations, the Trust will not be required to file its annual information return required by section 6033 of the Code for any taxable year following the taxable year in which the proposed Final Distribution occurs, if during the subsequent taxable years the Trust has neither legal nor equitable title to any assets and engages in no activity. Upon the Trust's termination, the Trust must file its final information return as required by section 6043(b).

Except as we have ruled above, we express no opinion as to the tax consequences of the transaction under the cited provisions of the Code or under any other provisions of the Code.

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

Because this letter could help resolve any future questions about the tax consequences of your activities, you should keep a copy of this ruling in your permanent records.

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,

/s/

Terrell M. Berkovsky
Manager, Exempt Organizations
Technical Group 2

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