



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

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

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UIL: 4941.04-00

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Legend:

B =  
D =  
F =  
Former Spouse =  
Corporation =  
Foundation =

Dear :

We have considered your ruling request dated November 2, 2007, concerning the excise tax consequences under section 4941 of the Internal Revenue Code ("Code") related to a proposed transfer of assets, in the manner and for the purposes described below.

Foundation has been recognized as an organization exempt under section 501(c)(3) of the Code and is classified as a private foundation within the meaning of section 509(a). B's Former Spouse was the founder of both Foundation and Corporation. B also made substantial contributions to Foundation. B had the right, so long as she lived, either to be a director of Foundation or to appoint another to serve in her place as a director, subject, however, to her right to rescind that appointment and either to resume her service as a director or to appoint another to serve in her place. During her lifetime, B appointed her daughter, D, to serve in her place as a director of Foundation. B's daughter D, and her son F, are personal representatives of the estate of B.

Corporation is a holding company which conducts business through a number of wholly-owned subsidiaries. E has two classes of stock, voting and nonvoting. F owns all shares of voting common stock and is also a director of Foundation. Corporation has made substantial contributions to the Foundation.

Upon B's death, B devised the residue of her estate to Foundation. This residue included the ownership of certain timber properties. The land was acquired as investment property and was

originally held as an undivided 50 percent tenancy-in-common interest with Former Spouse. The land holdings of both B and Former Spouse were subject to substantially identical option agreements (singularly referred to herein as "Option Agreement") which granted Corporation the right to acquire these holdings at any time up until the estate of the optionor terminated, at the then-current fair market value, as determined by an independent appraiser.

After Former Spouse died, leaving the residue of Former Spouse's estate to Foundation, Corporation exercised its rights under the Option Agreement with Former Spouse and acquired the land holdings from Former Spouse's estate. These holdings were then still held as a tenancy-in-common interest with B. Following acquisition of Former Spouse's property, Corporation entered into a series of exchange transactions with B, so that Corporation and B would each own the entire interest in approximately half the property, instead of undivided interests in the whole. We ruled in separate rulings that the transaction between Corporation and the estate of Former Spouse was not an act of self-dealing, pursuant to section 53.4941(d)-1(b)(3) of the Foundation and Similar Excise Tax Regulations ("regulations").

Corporation exercised the option granted to it by the Option Agreement with B through a third party intermediary, an assignee of the Corporation. Pursuant to the Option Agreement, the price paid by the assignee of the Corporation, to the estate of B was above the fair market value of the land, determined as of the date of the exercise of the option. This fair market value was determined by an agreed upon independent appraiser. During this process, the estate of B was guided by a committee of members of the board of the Foundation, each of whom is independent of Corporation. In exchange for the land being transferred to an assignee of the Corporation pursuant to the Option Agreement the estate of B received all cash, in an amount represented to be above fair market value.

You state that the appropriate state Attorney General acknowledged that it had received a copy of the petition filed by you seeking approval of the sale and that the Attorney General did not file any objections to that petition. You also represent that the transaction was approved by the probate court with jurisdiction over B's estate.

Requested Rulings:

The personal representatives of the estate of B, for themselves and the estate, Corporation, and the Foundation, for itself and its managers, request a ruling that pursuant to section 53.4941(d)-1(b)(3) of the regulations, the estate's sale of the land holdings of B to an assignee of the Corporation pursuant to the terms and provisions of the Option Agreement for the price determined as specified in the Option Agreement, followed by the assignee's transfer of the property to Corporation, will not be an act of self-dealing under section 4941 of the Code by any of the parties, the estate of B, the personal representatives of the estate, Corporation, the Foundation, or the Foundation's managers.

Law:

Section 501(c)(3) of the Code exempts from federal income tax organization organized and operated exclusively for charitable or educational purposes.

Section 507(d)(2)(A) of the Code defines a substantial contributor as any person who contributed or bequeathed an aggregated amount of more than \$5,000 to a private foundation, if such amount is more than 2 percent of the total contributions and bequests received by the foundation before the close of the taxable year of the foundation in which the contribution or bequest is received by the foundation from such person.

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

Section 4941(d)(1) of the Code defines self-dealing as including a sale or exchange of property or the extension of credit between a foundation and a disqualified person whether done directly or indirectly.

Section 4946(a)(1) of the Code defines the term "disqualified persons" with respect to a private foundation as including a substantial contributor to the foundation, a foundation manager, and an owner of more than 20 percent of the total combined voting power of a corporation which is a substantial contributor to the foundation. It also includes a member of the family of any individual described above. In addition it includes a trust or estate in which persons described in above hold more than 35 percent of the beneficial interest.

Section 4946(b) of the Code defines the term foundation manager as including an officer, director, or trustee of a foundation or an individual having powers or responsibilities similar to those of officers, directors, or trustees of the foundation.

Section 4946(d) of the Code states that the term "a member" of the family of a disqualified person includes the spouse, children of and grandchildren of a disqualified person.

Section 53.4941(d)-1(a) of the regulations provides, in general, that for the purposes of section 4941, the term "self-dealing" means any direct or indirect transaction described in section 53.4941(d)-2 of the regulations.

Section 53.4941(d)-1(b) of the regulations provides that certain transactions described in section 53.4941(d)-2 as indirect self-dealing are excepted from the definition of "indirect self-dealing."

Section 53.4941(d)-1(b)(3) of the regulations provides that the term indirect self-dealing shall not include a transaction with respect to a private foundation's interest or expectancy in property (whether or not encumbered) held by an estate (or revocable trust, including a trust which has become irrevocable on a grantor's death), regardless of when title to the property vests under local law, if -

- (i) The administrator or executor of an estate or trustee of a revocable trust either -

(a) Possess a power of sale with respect to the property,  
 (b) Has the power to reallocate the property to another beneficiary, or  
 (c) Is required to sell the property under the terms of any option subject to which the property was acquired by the estate (or revocable trust);

(ii) Such transaction is approved by the probate court having jurisdiction over the estate (or by another court having jurisdiction over the estate (or trust) or over the private foundation);

(iii) Such transaction occurs before the estate is considered terminated for federal income tax purposes pursuant to paragraph (a) of section 1.641(b)-3 of this chapter (or in the case of a revocable trust, before it is considered subject to section 4947);

(iv) The estate (or trust) receives an amount which equals or exceeds the fair market value of the foundation's interest or expectancy in such property at the time of the transaction taking into account the terms of any option subject to which the property was acquired by the estate (or trust); and

(v) With respect to transaction occurring after April 16, 1973, the transaction either -

(a) results in the foundation receiving an interest or expectancy at least as liquid as the one it gave up,

(b) results in the foundation receiving an asset related to the active carrying out of its exempt purposes, or

(c) is required under the terms of any option which is binding on the estate (or trust).

Section 53.4941(d)-1(b)(8) of the regulations, Example (4), describes a situation where a substantial contributor to a private foundation bequeaths one-half of his estate to his spouse and one-half to the private foundation. The estate includes a one-third interest in a partnership, the remaining two-thirds of the partnership are owned by a disqualified person to the private foundation. The one-third interest was subject to an option agreement when it was acquired by the estate. The sale of the one-third interest in the partnership to the disqualified person did not constitute an act of self-dealing because the transaction satisfied the requirements set forth in section 53.4941(d)-1(b)(3).

Section 53.4941(d)-2(a)(1) of the regulations provides that, in general, the sale or exchange of property between a private foundation and a disqualified person shall constitute an act of self-dealing.

#### Analysis:

Generally transactions between a disqualified person and a foundation are subject to the self-dealing rules set forth in section 4941 of the Code. Section 4941(d)(1)(a) defines "self-dealing" to include "any direct or indirect . . . sale or exchange, or leasing, of property between a private foundation and a disqualified person." Under section 53.4941-1(d)-1 of the regulations the sale by an estate of property in which a private foundation has an expectancy under a will can be an act of indirect self-dealing. If the transaction described above were determined to be an act of self-dealing, it would subject the self-dealing persons to an excise tax on "each act of self-dealing between a disqualified person and a private foundation" pursuant to section 4941(a)(1). However, in order to apply section 4941 we must first determine if there are disqualified persons

in the transaction with the private foundation.

Here, Corporation is a disqualified person with respect to the Foundation under section 4946(a)(1)(E) of the Code because it was a substantial contributor to the Foundation. Section 507(d)(2)(A) of the Code provides that a substantial contributor is any person who contributed an aggregate amount of more than \$5,000 to a private foundation, if such amount is more than 2 percent of total contributions. Corporation has contributed substantially more than \$5,000 which you state was more than 2% of total contributions.

Additionally, D and F, are disqualified persons with respect to the Foundation pursuant to section 4946(d) of the Code. That section states that the term "a member" of the family of a disqualified person includes the spouse, children of and grandchildren of a disqualified person. D and F are children of B, a disqualified person, as well as being the executors of B's estate and directors of Foundation. F is also the owner of all the voting stock of Corporation. Thus, D and F are disqualified persons with respect to the Foundation.

However, transactions during the administration of an estate regarding the foundation's interest or expectancy in property held by such estate are not self-dealing if all five conditions set forth in section 53.4941(d)-1(b)(3) of the regulations are met. Such exception to the self-dealing rules is commonly referred to as the "estate administration exception."

The first requirement of the estate administration exception is section 53.4941(d)-1(b)(3)(i) of the regulations, which provides in part, that the administrator of an estate is required to sell the property under the terms of any option subject to which the property was acquired by the estate. Here, B during her lifetime entered into an Option Agreement with Corporation to sell the property to Corporation in exchange for which B or her estate would receive fair market value of the assets transferred, as determined by an independent appraiser. Since the personal representatives of B's estate are required to sell the property under the terms of the Option Agreement, subject to which the property was acquired by the estate, the transaction meets this first requirement.

The second requirement as set forth in section 53.4941(d)-1(b)(3)(ii) of the regulations provides that the transaction must be approved by the probate court having jurisdiction over the estate. Here, you have represented that the sale transaction has been approved by the probate court having jurisdiction over the estate. Thus, the second condition has been met.

The third requirement, pursuant to section 53.4941(d)-1(b)(3)(iii) of the regulations, provides that such transaction occurs before the estate is considered terminated for Federal income tax purposes. Here, according to the facts you have represented that the transaction occurred prior to the estate being terminated for Federal income tax purposes. Additionally the Option Agreement specifically provided that the Corporation could exercise its option at any time up until the estate of the optionor terminated. Thus, this third condition has been met.

Fourth, section 53.4941(d)-1(b)(3)(iv) of the regulations provides that the estate receives an amount which equals or exceeds the fair market value of the foundation's interest or expectancy in such property at the time of the transaction taking into account the terms of any option subject to which the property was acquired by the estate. Here, the Option Agreement specifies that the purchase price will be the fair market value as determined by an independent appraisal.

The estate of B in exchange for selling the property interest pursuant to the Option Agreement received an amount greater than the appraised amount and received all cash in the transaction. Thus, the requirement of subsection (iv) of section 53.4941(d)-1(b)(3) of the regulations that the estate receives an amount which equals the fair market value of the Foundation's interest or expectancy in the property holdings at the time of the transaction was met.

The last requirement of the estate administration exception is that the transaction results in the foundation receiving an interest or expectancy at least as liquid as the one it gave up. Here, the estate (and thereby the Foundation) gave up real property in exchange for all cash. Thus, the estate received an interest at least as liquid as the one it gave up.

Since the transaction outlined above meets the requirements for the estate administration exception, the transaction will not be subject to the self-dealing rules set forth in section 4941 of the Code.

Ruling:

The sale by the estate of B and purchase of the interest by an assignee of Corporation pursuant to the terms and provisions of the Option Agreement will not be an act of self-dealing under section 4941 of the Code by the Estate of B.

In this ruling we have not determined whether the methodology used to determine fair market value of the assets is proper. We merely have accepted the given representation that the appraisal reflects fair market value. In this ruling we also have not determined whether the mechanism of the deferred like-kind exchange pursuant to section 1031 of the Code is proper.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

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 by others as precedent.

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes in these facts. This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept 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.

In accordance with the Power of Attorney currently on file with the Internal Revenue Service, we are sending a copy of this letter to your authorized representative.

Sincerely,

Ronald J. Shoemaker  
Manager, Exempt Organizations  
Technical Group 2

Enclosure  
Notice 437