



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Release Number: **201303021**
Release Date: 1/18/2013
Date: October 22, 2012

Uniform Issue List:
4943.00-00
4946.00-00

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Legend:

<u>Corporation</u>	=
<u>Founder</u>	=
<u>Wife</u>	=
<u>Children</u>	=
<u>Grandchildren</u>	=
<u>Trust 1</u>	=
<u>X1</u>	=
<u>Trust 2</u>	=
<u>Trust 3</u>	=
<u>Trust 4</u>	=
<u>Family and Charitable Trusts</u>	=

Dear

This is in response to your ruling request dated September 21, 2011, requesting a ruling that your ownership of Corporation non-voting stock will not give rise to excise tax on excess business holdings under § 4943 of the Internal Revenue Code ("Code").

FACTS

You have been recognized as an organization exempt under § 501(a) of the Code because you are described in § 501(c)(3) and are classified as a private foundation within the meaning of § 509(a). Founder, his spouse ("Wife"), and business entities they own have donated a substantial amount of money to you. You state that as a result, Founder, Wife, and Corporation are substantial contributors with respect to you.

You represent that Founder, family members, and various trusts for family members currently

own all of the voting shares and most of the non-voting shares of Corporation.

You state that under Trust 1 and Trust 4, of which Founder and Wife are the settlors, you will receive X1 non-voting shares of Corporation stock. You will not hold any direct or indirect interest in the voting shares of Corporation.

You state that under the proposed transaction, Founder and Wife have created revocable trusts and that they will transfer their Corporation voting shares to the trustee under Trust 2 and Trust 3 upon receipt of a favorable ruling. Thereafter, the voting shares so transferred will be divided into four separate irrevocable trusts ("collectively referred to as the Family and Charitable Trusts"). Each of the Family and Charitable Trusts will have both charitable and non-charitable beneficiaries. Each of the Family and Charitable Trusts will not own more than 20 percent of the Corporation voting shares. After the transfers of the Corporation voting shares to the Family and Charitable Trusts, Founder's children ("Children") will each own directly less than 20 percent of Corporation voting shares.

The non-charitable beneficiaries of the Family and Charitable Trusts will be Children and grandchildren of Founder and Wife ("Grandchildren"). Children and Grandchildren will have less than a 35-percent beneficial interest in each of the trusts, which will consist solely of an income interest.

The charitable beneficiaries of the Family and Charitable Trusts will have more than a 65-percent beneficial interest in each. Upon termination of each of the Family and Charitable Trusts, each of the trusts' charitable beneficiaries will receive 100 percent of the trust assets as the only remainder beneficiaries of each trust.

RULINGS REQUESTED

You requested the following rulings:

1. That Corporation non-voting shares to be held directly by you will be permitted holdings and will not be excess business holdings within the meaning of § 4943 of the Code.
2. That for purposes of § 4943 of the Code, the Family and Charitable Trusts described above are not disqualified persons with respect to you within the meaning of § 4946.

LAW

Section 4943(a)(1) of the Code imposes a tax on the excess business holdings of any private foundation in a business enterprise during any taxable year which ends during the taxable period. The tax is equal to 10 percent of the value of such holdings.

Section 4943(c)(1) of the Code defines the term "excess business holdings" as the amount of stock in a corporation that a foundation would have to dispose of to a person other than a disqualified person in order for the remaining holdings of the foundation in the corporation to be permitted holdings.

Section 4943(c)(2) of the Code limits the holdings of a private foundation in a corporation to 20 percent of the voting stock of the business enterprise, reduced by the percentage of the voting stock owned by all disqualified persons.

Section 4943(c)(2)(A) of the Code provides that the permitted holdings of any private foundation in an incorporated business enterprise are:

- (i) 20 percent of the voting stock, reduced by
- (ii) The percentage of the voting stock owned by all disqualified persons.

In addition, in any case in which all disqualified persons together do not own more than 20 percent of the voting stock of an incorporated business enterprise, nonvoting stock held by the private foundation shall also be treated as permitted holdings.

Section 4943(d)(1) provides that in computing the "business holdings" of a private foundation, or a disqualified person with respect thereto, in any business enterprise, any stock or other interest owned, directly or indirectly, by or for a trust shall be considered as being owned proportionately by or for its beneficiaries.

Section 4946(a)(1) of the Code provides, in part, that for purposes of this subchapter, the term "disqualified person" means, with respect to a private foundation, a person who is--

- (A) a substantial contributor to the foundation,
- (B) a foundation manager (within the meaning of subsection (b)(1)),
- (C) an owner of more than 20 percent of--
 - (i) the total combined voting power of a corporation,
 - (ii) the profits interest of a partnership, or
 - (iii) the beneficial interest of a trust or unincorporated enterprise, which is a substantial contributor to the foundation,
- (D) a member of the family (as defined in subsection (d)) of any individual described in subparagraph (A), (B), or (C),
- (E) a corporation of which persons described in subparagraph (A), (B), (C), or (D) own more than 35 percent of the total combined voting power,
- (F) a partnership in which persons described in subparagraph (A), (B), (C), or (D) own more than 35 percent of the profits interest,
- (G) a trust or estate in which persons described in subparagraph (A), (B), (C), or (D) hold more than 35 percent of the beneficial interest, and
- (H) only for purposes of § 4943, a private foundation--
 - (i) which is effectively controlled (directly or indirectly) by the same person or persons who control the private foundation in question, or
 - (ii) substantially all of the contributions to which were made (directly or indirectly) by the same person or persons described in subparagraph (A), (B), or (C), or members of their families (within the meaning of subsection (d)), who made (directly or indirectly) substantially all of the contributions to the private foundation in question.

Section 4946(a)(2) of the Code provides that for purposes of paragraph (1), the term "substantial contributor" means a person who is described in § 507(d)(2).

Section 4946(d) of the Code provides that for purposes of subsection (a)(1), the family of any individual shall include only his spouse, ancestors, children, grandchildren, great grandchildren, and the spouses of children, grandchildren, and great grandchildren.

Section 53.4943-1 of the Foundation and Similar Excise Taxes Regulations ("foundation regulations") provides that generally, under § 4943 of the Code, the combined holdings of a private foundation and all disqualified persons (as defined in § 4946(a)) in any corporation conducting a business which is not substantially related to the exempt purpose of the foundation are limited to 20 percent of the voting stock in such corporation.

Section 53.4943-2(a) of the foundation regulations imposes an initial excise tax on the excess business holdings of a private foundation.

Section 53.4943-3(a) of the foundation regulations provides that the term excess business holdings means, with respect to the holdings of any private foundation in any business enterprise, the amount of stock in the enterprise the foundation or disqualified person would have to dispose of to a person other than a disqualified person in order for the remaining holdings of the foundation in the enterprise to be permitted holdings.

Section 53.4943-3(b)(1)(i) of the foundation regulations provides that except as otherwise provided in § 4943(c)(2) and (4), the permitted holdings of any private foundation in an incorporated business enterprise are 20 percent of the voting stock in such enterprise reduced (but not below zero) by the percent of voting stock in such enterprise actually or constructively owned by all disqualified persons.

Section 53.4943-3(b)(2)(i) of the foundation regulations provides that, in general, in addition to those holdings permitted by paragraph (b)(1) of that section, the permitted holdings of a private foundation in an incorporated business enterprise shall include any share of nonvoting stock in such enterprise held by the foundation in any case in which all disqualified persons hold no more than 20 percent of the voting stock in such enterprise. All equity interests which do not have voting power attributable to them shall, for purposes of § 4943, be classified as nonvoting stock.

Reg. §53.4943-3(c)(4)(ii) of the foundation regulations provides, in part, that for purposes of section 4943, the beneficial interest of a private foundation or any disqualified person in a trust shall be the beneficial remainder interest of such foundation or person determined as provided in paragraph (b) of § 53.4943-8.

Reg. §53.4943-8(b) of the foundation regulations provides, in part, that any interest actually or constructively owned by an estate or trust is deemed constructively owned, in the case of an estate, by its beneficiaries or, in the case of a trust, by its remainder beneficiaries. Thus, if a trust owns 100 percent of the stock of a corporation A, and if, on an actuarial basis, W's life

interest in the trust is 15 percent, Y's life interest is 25 percent, and Z's remainder interest is 60 percent, under this paragraph (b), Z will be considered to be the owner of 100 percent of the stock of corporation A.

Section 53.4946-1 of the foundation regulations provides that for purposes of Chapter 42 and the regulations thereunder, the following are disqualified persons with respect to a private foundation:

(i) All substantial contributors to the foundation, as defined in § 507 (d)(2) and the regulations thereunder.

(ii) All foundation managers of the foundation as defined in § 4946 (b)(1) and paragraph (f)(1)(i) of that section,

(iii) An owner of more than 20 percent of:

(a) The total combined voting power of a corporation,

(b) The profits interest of a partnership,

(c) The beneficial interest of a trust or unincorporated enterprise,

which is (during such ownership) a substantial contributor to the foundation, as defined in § 507(d)(2) and the regulations thereunder,

(iv) A member of the family, as defined in § 4946(d) and paragraph (h) of this section, of any of the individuals described in subdivision (i), (ii), or (iii) of this subparagraph,

(v) A corporation of which more than 35 percent of the total combined voting power is owned by persons described in subdivision (i), (ii), (iii), or (iv) of this subparagraph,

(vi) A partnership of which more than 35 percent of the profits interest is owned by persons described in subdivision (i), (ii), (iii), or (iv) of this subparagraph, and

(vii) A trust, estate, or unincorporated enterprise of which more than 35 percent of the beneficial interest is owned by persons described in subdivision (i), (ii), (iii), or (iv) of this subparagraph.

Section 53.4946-1(a)(5) of the foundation regulations provides that for purposes of subparagraph (1) (iii) (a) and (v) of this paragraph, the term "combined voting power" includes voting power represented by holdings of voting stock, actual or constructive (under § 4946(a)(3)), but does not include voting rights held only as a director or trustee.

Section 53.4946-1(h) of the foundation regulations provides that for the purposes of this section, the members of the family of an individual include only:

(1) His spouse,

- (2) His ancestors,
- (3) His lineal descendants, and
- (4) Spouses of his lineal descendants.

For example, a brother or sister of an individual is not a member of his family for purposes of this section. However, for example, the wife of a grandchild of an individual is a member of his family for such purposes. For purposes of this paragraph, a legally adopted child of an individual shall be treated as a child of such individual by blood.

ANALYSIS

Section 4943 of the Code imposes an excise tax on the excess business holdings of private foundations. Section 4943(c)(1) defines excess business holdings as the amount of stock in a corporation that a foundation would have to dispose of to a person other than a disqualified person in order for the remaining holdings of the foundation in the corporation to be permitted holdings. Section 4943(c)(2) provides that the permitted holdings of a foundation in a corporation are 20 percent of the voting stock, reduced by the percentage of the voting stock owned by all disqualified persons. In any case in which all disqualified persons together do not own more than 20 percent of the voting stock of a corporation, nonvoting stock held by a private foundation is treated as permitted holdings. Section 4943(c)(2)(A) and § 53.4943-3(b)(2) of the foundation regulations. In order to determine whether the Corporation non-voting shares to be held by you are permitted holdings under § 4943(c)(2)(A), we must first determine whether there are disqualified persons involved in the transaction.

In this case, Founder is a disqualified person with respect to you as described under § 4946(a)(1)(A) of the Code because he is a substantial contributor. Wife, Children, and Grandchildren are also disqualified persons under § 4946(d) with respect to Founder because they are family members of a substantial contributor within the meaning of § 4946(a)(1)(A) of the Code.

Section 4943(c)(2) of the Code provides that, in any case in which all disqualified persons together do not own more than 20 percent of the voting stock of a corporation, nonvoting stock held by the private foundation shall be treated as permitted holdings. Section 53.4943-3(b)(2)(i) of the foundation regulations provides that the permitted holdings of a private foundation include any share of nonvoting stock in a corporation when all disqualified persons hold, actually or constructively, no more than 20 percent of the voting stock in the corporation. In this case, after the transfer of Corporation voting stock from Trust 2 and Trust 3 to the Family and Charitable Trusts, disqualified persons as described above will not own more than 20 percent of the voting stock of Corporation for the purposes of § 4943(c)(2)(A).

Further, § 4946(a)(1)(G) of the Code states that the term “disqualified person” includes a trust of which more than 35 percent of the beneficial interest is owned by disqualified persons such as a

substantial contributor and family members of a substantial contributor. Under the Family and Charitable Trusts, Children and Grandchildren, who are disqualified persons as described above, will have less than a 35-percent beneficial interest in each of the Family and Charitable Trusts.

Furthermore, the stock held by the Family and Charitable Trusts will not be treated as being held by a disqualified person because § 4946(a)(1)(G) provides that a trust is not a disqualified person if disqualified persons do not hold over 35 percent of the beneficial interest. The Family and Charitable Trusts are not disqualified persons with respect to you because the Family and Charitable Trusts are trusts described in § 4946(a)(1)(G) of the Code in which persons described in § 4946(a)(1)(B) or 4946(d) do not hold more than a 35-percent beneficial interest. The assets of these trusts are considered, for purposes of section 4943, as owned by the charitable remaindermen—see Reg. §53.4943-8(b).

RULINGS

Based on your facts and representations, we rule as follows:

1. The Corporation non-voting shares to be held directly by you will be permitted holdings and will not be excess business holdings within the meaning of § 4943 of the Code.
2. The Family and Charitable Trusts as described above are not disqualified persons with respect to you within the meaning of § 4946 of the Code.

This ruling will be made available for public inspection under § 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 and, in particular, it does not address tax matters relating to grantor trusts, powers of appointment, or gift and estate taxation. 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 Shoemaker
Manager, Exempt Organizations
Technical Group 2

Enclosure
Notice 437