



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Release Number: **201311035**

Release Date: 3/15/2013

Date: December 18, 2012

Uniform Issue List:

4943.00-00

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Trust A =
Trust B =
Corporation =
Brother 1 =
Brother 2 =
Voting Trust =
Foundation =

Dear

This is in response to your ruling request dated June 7, 2012, requesting a ruling that your ownership of Corporation non-voting stock will be permitted holdings and will not constitute excess business holdings under I.R.C. § 4943.

FACTS

You have been recognized as an organization exempt under § 501(a) because you are described in § 501(c)(3) and are classified as a supporting organization within the meaning of § 509(a)(3). You maintain and operate donor advised funds as defined in § 4966(d)(2)(A).

Brother 1 and Brother 2 (collectively the "Brothers") are founders of Corporation. Both of the Brothers have made gifts of Corporation non-voting stock to you that is held in donor advised funds maintained by you. Each of the Brothers has advisory privileges over his own respective donor advised fund. Each of the Brothers also has transferred all of his Corporation voting stock to Brother 1, who is the trustee (Trustee) of the Voting Trust in exchange for voting trust certificates. The Voting Trust confers on the Trustee the right to vote all voting stock held by the Trustee and otherwise act for the beneficial owners of the stock, subject to the Trustee's fiduciary duties to those beneficial owners as holders of the voting trust certificates.

The Brothers have each created a revocable trust agreement, Trust A and Trust B (hereafter "the Revocable Trusts") and have transferred all their shares of stock of Corporation, subject to the terms of the Voting Trust, to the Trustee of the Revocable Trusts. You state that under the

proposed transaction, Trustee under the Revocable Trusts will transfer beneficial ownership of no less than percent of Corporation voting stock subject to the terms of the Voting Trust to Foundation upon the receipt of a favorable ruling. Foundation is exempt under § 501(a) because it is described in § 501(c)(3) and is classified as a public charity within the meaning of §§ 509(a)(1) and 170(b)(1)(A)(vi). After the transfer of Corporation voting stock to the Foundation, Brothers will hold no more than percent of Corporation voting stock, directly or indirectly, in a non-fiduciary capacity. You will not hold any direct or indirect interest in the voting stock of Corporation.

RULING REQUESTED

Upon transfer of the beneficial ownership of percent of Corporation voting stock to Foundation, the Corporation non-voting stock held by you in donor advised funds will be permitted holdings and will not constitute excess business holdings within the meaning of § 4943.

LAW

I.R.C. § 507(c)(2) imposes on each organization which is referred to in subsection (a) a tax equal to the lower of -

(1) the amount which the private foundation substantiates by adequate records or other corroborating evidence as the aggregate tax benefit resulting from the section 501(c)(3) status of such foundation, or

(2) the value of the net assets of such foundation.

I.R.C. § 509(a)(1) provides that the term private foundation means a domestic or foreign organization described in § 501(c)(3) other than an organization described in § 170(b)(1)(A) other than in clauses vii and viii.

I.R.C. § 4943(a)(1) imposes on the excess business holdings of any private foundation in a business enterprise during any taxable year which ends during the taxable period a tax equal to 10 percent of the value of such holdings.

I.R.C. § 4943(c)(1) provides that, in general, the term excess business holdings means, with respect to the holdings of any private foundation in any business enterprise, the amount of stock or other interest in the enterprise which the foundation would have to dispose of to a person other than a disqualified person in order for the remaining holdings of the foundation in such enterprise to be permitted holdings.

I.R.C. § 4943(c)(2)(A) 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.

I.R.C. 4943(d)(1) provides that in computing the holdings of a private foundation, or a disqualified person (as defined in §4946) with respect thereto, in any business enterprise, any stock or other interest owned, directly or indirectly, by or for a corporation, partnership, estate, or trust shall be considered as being owned proportionately by or for its shareholders, partners, or beneficiaries.

I.R.C. § 4943(e)(1) provides that for purposes of this section, a donor advised fund (as defined in § 4966(d)(2)) shall be treated as a private foundation.

I.R.C. § 4943(e)(2)(A) provides that in applying this section to any donor advised fund (as so defined), the term "disqualified person" means, with respect to the donor advised fund, any person who is described in § 4966(d)(2)(A)(iii).

I.R.C. § 4946(a)(1) 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,
- (H) only for purposes of section 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.

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

I.R.C. § 4966(d)(2)(A) provides that the term "donor advised fund" means a fund or account--

(i) which is separately identified by reference to contributions of a donor or donors,
(ii) which is owned and controlled by a sponsoring organization, and
(iii) with respect to which a donor (or any person appointed or designated by such donor) has, or reasonably expects to have, advisory privileges with respect to the distribution or investment of amounts held in such fund or account by reason of the donor's status as a donor.

Treas. Reg. § 53.4943-1 provides that generally, under § 4943, 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.

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

Treas. Reg. § 53.4943-3(a) 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.

Treas. Reg. § 53.4943-3(b)(1)(i) 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.

Treas. Reg. § 53.4943-3(b)(2)(i) 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.

Treas. Reg. § 53.4943-8(a)(1) provides that for purposes of § 4943, in computing the holdings in a business enterprise of a private foundation, or a disqualified person (as defined in § 4946), any stock or other interest owned, directly or indirectly, by or for a corporation, partnership, estate or trust shall be considered as being owned proportionately by or for its shareholders, partners, or beneficiaries except as otherwise provided paragraphs (b), (c) and (d) of this section. Any interest in a business enterprise actually or constructively owned by a shareholder of a corporation, a partner of a partnership, or beneficiary of an estate or trust shall not be considered as constructively held by the corporation, partnership, trust or estate. Further, if any corporation, partnership, estate or trust has a warrant or other option to acquire an interest in a business enterprise, such interest is not deemed to be constructively owned by such entity until the option is exercised.

Treas. Reg. § 53.4943-8(b) 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.

Treas. Reg. § 53.4946-1 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.

Treas. Reg. § 53.4946-1(a)(5) 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.

Treas. Reg. § 53.4946-1(a) (7) provides that for purposes of §§ 170(b)(1)(E)(iii), 507(d)(1), 508(d), 509(a)(1) and (3), and Chapter 42, the term "disqualified person" shall not include an organization which is described in § 509(a)(1), (2), or (3), or any other organization which is wholly owned by such § 509(a)(1), (2), or (3) organization.

ANALYSIS

Section 4943 imposes an excise tax on the excess business holdings of a private foundation. 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). 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, Brother 1 and Brother 2 have contributed Corporation non-voting stock to you that is held in donor advised funds maintained by you. The donor advised funds maintained by you are described in § 4966(d)(2)(A) and, as such, are treated as private foundations for purposes of applying the excess business holding rules under § 4943. See I.R.C. 4943(e)(1). Thus, Brother 1 and Brother 2 are disqualified persons with respect to you as described under § 4943(e)(2)(A).

Section 4943(c)(2) provides that, in any case in which all disqualified persons together do not own more than percent of the voting stock of a corporation, nonvoting stock held by a private foundation shall be treated as permitted holdings. Section 53.4943-3(b)(2)(i) 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 percent of the voting stock of the corporation. In this case, after the transfer of Corporation voting stock from the Revocable Trusts to Foundation, disqualified persons as described above will not own more than percent of the voting stock of Corporation for the purposes of § 4943(c)(2)(A).

Furthermore, § 4943(d)(1) provides that the stock held by the Revocable Trusts and Voting Trust will be considered to be owned proportionately by their beneficiaries. In this case, Foundation will be treated as beneficially owning 80 percent of Corporation voting stock. See § 53.4943-8(b). In addition, since Foundation is not a disqualified person with respect to you because it is an organization described in § 509(a)(1), disqualified persons (Brother 1 and Brother 2) will hold no more than percent of Corporation stock. Therefore, Corporation non-voting stock to be held by you will be treated as permitted holdings for purposes of § 4943(c)(2) and § 53.4943-3(b)(2), because disqualified persons will not own more than percent of Corporation voting stock.

RULING

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

Upon the transfer of the beneficial ownership of percent of Corporation voting stock to Foundation, 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.

This ruling will be made available for public inspection under § 6110 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. I.R.C. § 6110(k)(3) 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