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Washington, DC 20224

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4941.00-00, 4942.00-00,
4945.00-00, 4958.00-00

Person To Contact: _____, ID No. _____

Telephone Number: _____

Refer Reply To:
CC:TEGE:EOEG:EO3
PLR-128836-17

Date:
March 20, 2018

Legend

Foundation =
Trust =
Date 1 =
State =
A =
B =
Will =
Date 2 =
Court =

Dear _____:

This is in response to the letter dated September 20, 2017, in which your representative requested rulings under sections 501, 507, 509, 4940, 4941, 4942, 4945, and 4958 of the Internal Revenue Code with respect to the change in your foundation status from a non-functionally integrated Type III supporting organization to a private foundation.¹

Facts and Representations

¹ The Internal Revenue Code of 1986, as amended, to which all subsequent section references are made unless otherwise indicated.

Foundation was established on Date 1 in State as a non-profit corporation by A and B. Foundation was recognized as a tax-exempt organization described under § 501(c)(3), and was classified as a supporting organization pursuant to § 509(a)(3)(B)(iii). In its role as a Type III supporting organization, Foundation provides grants to nine designated beneficiary organizations. Foundation's articles of incorporation provide that in order to receive distributions from Foundation, an organization must be "an organization exempt from federal income tax under section 501(c)(3) which is not a private foundation by reason of being described in section 509(a)(1) or 509(a)(2) of the Code, or an organization described in sections 170(c)(1), 2055(a)(1) and 2522(a)(1) of the Code." None of the beneficiaries can be disqualified persons within the meaning of Treas. Reg. § 53.4958-3(a)(1) and (d)(1). Foundation's nine designated beneficiary organizations are all described in § 170(b)(1)(A) and in either § 509(a)(1) or § 509(a)(2).

Foundation's board of directors is made up of nine individuals. Three of the directors must be selected by the governing bodies of the designated beneficiaries. Three of the remaining six directors are individuals who would not be disqualified persons, as described in section 4946(b)(1). The remaining three directors are members of A and B's family within the meaning of § 4946(d).

Foundation's assets are mostly made up of cash and investments. Foundation's assets are held in two separate funds. The first fund contains assets that were initially contributed to Foundation by A and B and any undistributed earnings. There are no specific restrictions placed on this general fund. Foundation's second fund contains assets assigned to Foundation by B from Trust. The assets in the second fund from the trust are subject to the restrictions from A's will (Will) and must be kept separate from the assets contained in the first general fund.

Pursuant to Will, Trust was created for the benefit of B during B's lifetime. Will provides that upon the death of B, a portion of Trust's remaining assets will be transferred to Foundation. Will also provides that distributions in any year from Trust are limited to the greater of the residuary estate income from that year or five percent of the residuary estate total as of the first day of that year, and that any distribution from Trust must be specifically divided with a particular percentage of the distribution going to each of the nine designated beneficiaries. Will also provides that any assets assigned from Trust to Foundation by B that are in Foundation's second fund are subject to these same distribution requirements listed in Will. Accordingly, any distributions made by Foundation from the second fund are subject to the distribution requirements provided in Will.

The IRS issued final regulations in 2012 for Type III supporting organizations. Among other things, the final regulations provide additional notice requirements that a Type III supporting organization must provide to each of its supported organizations. After considering the new requirements that Type III supporting organizations are subject to, Foundation determined that it could be run more efficiently as a private foundation

instead of as a supporting organization. After Foundation is reclassified as a private foundation, it will no longer meet the notice and other requirements under § 509(a)(3) and Treas. Reg. § 1.509(a)-4.

Foundation sought a judicial modification of Trust in State to allow for Foundation's change in status to a private foundation. As part of the judicial proceedings, Foundation also sought to modify Trust to eliminate the restrictions placed on distributions from Trust by Will. Pursuant to the distribution provisions provided in Will, some of the nine designated beneficiaries receive 2.5% or less of the annual distributions from the Foundation's second fund. Foundation believes it can further its exempt purpose better by focusing the annual distributions on the designated beneficiaries that receive the larger portions of the annual distribution provisions pursuant to Will. However, this adjustment requires the modification to Trust. Foundation provided notice of these proceedings to the Attorney General of State, and the Attorney General declined to participate in them.

As part of the judicial proceedings, Foundation offered to each of the designated beneficiaries receiving the smaller percentage shares of the annual distributions a series of payments in exchange for the smaller designated beneficiaries relinquishing their rights to the mandatory distributions from Foundation's second fund. Most of the smaller designated beneficiaries accepted this offer. The smaller designated beneficiaries that accepted the payout offer are referred to as the "relinquishing beneficiaries". All the remaining designated beneficiaries that will continue to receive annual distributions from Foundation will be referred to as the "remaining beneficiaries." Foundation entered into a settlement agreement with all the designated beneficiaries outlining the terms of the payments to the relinquishing beneficiaries and the continued distribution of funds to the remaining beneficiaries.

Pursuant to the settlement agreement, the relinquishing beneficiaries agree that they will no longer be designated beneficiaries of Foundation's second fund in exchange for two payment amounts, determined from the relinquishing beneficiaries' percentage amount given under Trust and the fair market value of Foundation's second fund as of the trust conversion date and as of the final distribution date. The calculations of the payment amounts were made to provide a reasonable estimate of the amount that the relinquishing beneficiaries would have otherwise received from Foundation's second fund. Foundation represents that it does not wish to terminate its private foundation status in tandem with any of the grants to the relinquishing beneficiaries pursuant to the settlement agreement and has not indicated any contrary intent to the Secretary. Foundation further represents that no portion of any payment amount may be used for lobbying, influencing the outcome of elections, for grants to individuals other than for education scholarships, or in any other manner for non-charitable purposes.

Pursuant to the settlement agreement, the remaining beneficiaries agree that their percentage shares of Foundation's second fund will be recalculated to reflect the

equivalent shares of distributions made after Foundation's first and second funds are combined. These shares will be recalculated again when Trust terminates upon B's death. The calculations for the new distribution amounts are based on the remaining beneficiaries' percentage amounts given under Trust and the fair market value of Foundation's second fund as of the trust conversion date and the final distribution date and the fair market value of all the net assets held by Foundation as of the trust conversion date and the final distribution date. These calculations are intended to represent the same distributions that the remaining beneficiaries would have received if Foundation did not combine its first and second funds.

On Date 2, the Court granted Foundation's request to modify Trust. The date of the Court's judgment is effective upon the receipt by Foundation of a private letter ruling from the IRS.

Rulings Requested, Law, and Analysis

Requested Ruling 1:

Both the proposed conversion of Foundation to a private foundation and the transactions discussed in the settlement agreement will further one or more exempt purposes described in § 501(c)(3).

Revenue Procedure 2017-3, 2017-1 I.R.B. 130, section 3.01(32) provides that the Internal Revenue Service will not issue a ruling on whether an organization is or continues to be described in § 170(b)(1)(A) (other than clause (v)) or § 170(c)(2), including, for example, whether changes in an organization's activities or operations will affect or jeopardize the organization's status as an organization described in those sections. Section 3.01(71) provides that the Internal Revenue Service will not issue a ruling on whether an organization is or continues to be exempt from taxation under § 501(a) as an organization described in §§ 501(c) or 501(d), including, for example, whether changes in an organization's activities or operations will affect or jeopardize the organization's exempt status. Section 3.01(74) provides that the Internal Revenue Service will not issue a ruling on whether an organization is or continues to be described in § 509(a) including, for example, whether changes in an organization's activities or operations will affect or jeopardize the organization's status as a public charity described in § 509(a)(1)-(4).

Rev. Proc. 2017-5, 2017-1 I.R.B. 230, provides procedures for obtaining determination letters on public charity status. Section 7 provides that a tax-exempt organization should file Form 8940 for miscellaneous determinations, including a reclassification of foundation status from public charity to private foundation.

Accordingly, because Foundation is required to file Form 8940 to change its classification, we are not ruling regarding whether the proposed conversion of Foundation or the transactions discussed in the settlement agreement affect Foundation's status or classification.

Requested Ruling 2:

Neither the proposed conversion of the Foundation to a private foundation nor the transactions discussed in the settlement agreement will give rise to excise taxes under § 4958 to Foundation.

Section 4958(a)(1) imposes on each excess benefit transaction a tax equal to 25 percent of the excess benefit (the "first tier tax"). This tax must be paid by any disqualified person, as defined in § 4958 (f)(1), with respect to such transaction.

Section 4958(a)(2) provides that if a tax is imposed by § 4958(a)(1), and there is knowing participation in the excess benefit transaction by an organization manager, there shall be imposed on such manager an excise tax equal to 10 percent of the excess benefit, unless such participation is not willful and is due to reasonable cause.

Section 4958(b) provides that where an initial tax is imposed, but the excess benefit involved in such transaction is not corrected within the taxable period, an additional tax equal to 200 percent of the excess benefit involved is imposed and must be paid by any disqualified person with respect to such transaction (the "second tier tax"). There is no corresponding additional tax imposed on a foundation manager.

Section 4958(c), in part, defines "excess benefit transaction" as any transaction in which an economic benefit is provided by an "applicable tax-exempt organization" directly or indirectly to or for the use of any disqualified person if the value of the economic benefit provided exceeds the value of the consideration (including the performance of services) received for providing such benefit.

Section 4958(e) defines "applicable tax-exempt organization" as an organization described in either § 501(c)(3) or § 501(c)(4) of the Code or an organization which was so described at any time during the five-year period ending on the date of the excess benefit transaction. Such term does not include a private foundation as defined in § 509(a).

Section 4958(f)(1) defines "disqualified person" to include (A) any person who was, at any time during the five-year period ending on the date of such transaction, in a position to exercise substantial influence over the affairs of the organization, (B) a member of the family of a disqualified person, and (C) a 35-percent controlled entity.

Treas. Reg. § 53.4958-3(a)(1) defines “disqualified person” as any person who was in a position to exercise substantial influence over the affairs of the applicable tax-exempt organization at any time during the five-year period ending on the date of the transaction.

Treas. Reg. § 53.4958-3(d)(1) provides that a person is deemed not to be in a position to exercise substantial influence over the affairs of an applicable tax-exempt organization if the organization is described in § 501(c)(3) and exempt from tax under § 501(a).

An excess benefit transaction occurs when a charity provides an economic benefit directly or indirectly to or for the use of any disqualified person. Foundation states that none of the beneficiaries are disqualified persons within the meaning of Treas. Reg. § 53.4958-3(a)(1) and (d)(1). Therefore, because none of the beneficiaries are disqualified persons, the proposed reclassification and payments to be made pursuant to the settlement agreement will not give rise to an excise tax liability to Foundation pursuant to § 4958.

Requested Ruling 3:

Payments made to the relinquishing beneficiaries and the remaining beneficiaries pursuant to the settlement agreement after Foundation’s conversion date will not be self-dealing under § 4941.

Section 4941(a)(1) imposes taxes on each act of self-dealing between a disqualified person (as defined in § 4946(a)) and a private foundation. Taxes are imposed on both the self-dealers involved in an act of self-dealing and on any foundation managers who knowingly participate in an act of self-dealing. Even though § 4941 does not impose a tax on a private foundation when an act of self-dealing occurs, a foundation with respect to which there has been an act of self-dealing is required to report it to the IRS on its annual information return, which is the Form 990-PF in this case.

Section 4941(d)(1)(E) provides that the term “self-dealing” includes any direct or indirect transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a private foundation.

Section 4946(a)(1) defines the term “disqualified person” as a person who is a substantial contributor to the private foundation, a foundation manager, an owner of more than 20 percent of the total combined voting power of either a corporation, the profit interest of a partnership, or the beneficial interest of a trust or unincorporated enterprise which is a substantial contributor to the private foundation, a member of the family of any individual described previously, a corporation, partnership, or trust of which persons described previously own more than 35 percent, or a government official.

Section 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));

Section 170(b)(1)(A)(ii) includes an educational organization which normally maintains a regular facility and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on.

Treas. Reg. § 1.509(a)-2(a) provides that organizations described in § 170(b)(1)(A) (other than in clauses (vii) and (viii)) are excluded from the definition of “private foundation” by § 509(a)(1).

Treas. Reg. § 53.4946-1(a)(7) provides that for purposes of chapter 42 and certain other purposes, an organization described in § 509(a)(1), (2), or (3) is not a disqualified person. Treas. Reg. § 53.4946-1(a)(8) provides that for purposes of section 4941, the term “disqualified person” does not include organizations that are described under § 501(c)(3).

Foundation states that all of its beneficiaries are described under § 509(a)(1) or § 509(a)(2). Accordingly, the relinquishing and the remaining beneficiaries are not disqualified persons to Foundation, and transfers to them are not subject to the self-dealing tax of § 4941.

Requested Ruling 4:

Payments made by Foundation to the relinquishing beneficiaries and the remaining beneficiaries pursuant to the settlement agreement after the date Foundation converts to a private foundation will be treated as qualifying distributions under § 4942(g) at such times as the payments are actually paid to the beneficiary.

Section 4942(a) generally imposes a tax on the undistributed income of a private foundation (other than an operating foundation under § 4942(j)(3)) for any taxable year, that has not been distributed before the first day of the second (or any succeeding) taxable year following such taxable year.

Section 4942(c) defines undistributed income for any taxable year as the amount by which the distributable amount for such taxable year exceeds the qualifying distributions made out of such distributable amount for such taxable year.

Section 4942(g)(1) defines qualifying distribution as (A) any amount paid to accomplish one or more purposes described in § 170(c)(2)(B), other than any contribution to (i) an organization controlled by the foundation or one or more disqualified persons, or (ii) a private foundation which is not an operating foundation, except as otherwise provided; or (B) any amount paid to acquire an asset used directly in carrying out one or more purposes described in § 170(c)(2)(B).

Section 170(c)(1) provides that the term “charitable contribution” means a contribution or gift to or for the use of a state, a possession of the United States, or any political subdivision of any of the foregoing, or the United States or the District of Columbia, but only if the contribution or gift is made for exclusively public purposes. Section 170(c)(2)(B) further defines a charitable contribution to include a contribution to a corporation, trust or community chest, fund or foundation that is organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes.

Treas. Reg. § 53.4942(a)-3(a)(1) provides that the amount of a qualifying distribution of property is the fair market value of such property as of the date such qualifying distribution is made. The amount of an organization’s qualifying distribution will be determined solely on the cash receipts and disbursements method of accounting described in § 446.

Treas. Reg. § 53.4942(a)-3(a)(2) defines the term qualifying distribution, in relevant part, as any amount (including program related investments and reasonable and necessary administrative expenses) paid to accomplish one or more purposes described in § 170(c)(1) or § 170(c)(2)(B), other than any contribution to a private foundation which is not an operating foundation or to an organization controlled (directly or indirectly) by the contributing private foundation or one or more disqualified persons with respect to such foundation.

Under § 4942, a qualifying distribution includes any amount paid to accomplish one or more purposes described in § 170(c)(1) or § 170(c)(2)(B) other than a distribution to a private foundation. All of the beneficiaries to the settlement agreement payments are organizations that are described under § 170(c)(1) or § 170(c)(2)(B). Furthermore, Foundation’s articles of incorporation specifically provide that in order to receive distributions from Foundation, an organization must be an organization exempt under § 501(c)(3) and described in § 509(a)(1) or § 509(a)(2), or is an organization described in § 170(c)(1). Accordingly, because all of the payments made by Foundation pursuant to the settlement agreement are paid to accomplish purposes described in § 170(c)(1) or § 170(c)(2)(B), the payments would constitute qualifying distributions as of the dates that the payments are actually made to the beneficiaries.

Requested Ruling 5:

Payments made by Foundation to the relinquishing beneficiaries and the remaining beneficiaries pursuant to the settlement agreement after the date Foundation converts to a private foundation will not constitute taxable expenditures under § 4945(d).

Section 4945(a) imposes a tax on each “taxable expenditure” of a private foundation.

Section 4945(d) provides that the term “taxable expenditure” means any amount paid or incurred by a private foundation to carry on propaganda, or otherwise to attempt, to influence legislation, to influence the outcome of any specific public election or to carry on any voter registration drive, or as a grant to an individual for travel, study, or other similar purposes by such individual, or as a grant to an organization unless said organization is described in paragraph (1), (2), or (3) of § 509(a) or an exempt operating foundation (as defined in § 4940(d)(2)), or the private foundation exercises expenditure responsibility with respect to such grants in accordance with § 4945(h), or for any purpose other than one specified in § 170(c)(2)(B).

Section 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));

Treas. Reg. § 53.4945-5(a)(1) provides that the term taxable expenditure includes any amount paid or incurred by a private foundation as a grant to an organization (other than an organization described in § 509(a)(1), (2), or (3) (other than one described in § 4942(g)(4)(A)), unless the private foundation exercises expenditure responsibility with respect to such grant.

Treas. Reg. § 53.4545-5(a)(4) provides that for purposes of § 4945, an organization will be treated as a § 509(a)(1) organization if it is an organization described in § 170(c)(1) or § 511(a)(2)(B), even if it is not described in § 501(c)(3).

Foundation states all of the beneficiary organizations to the settlement agreement payments are described under § 509(a)(1) or § 509(a)(2). The settlement agreement further provides that no portion of any payment amount made pursuant to the agreement may be used for lobbying, influencing the outcome of elections, for grants to individuals other than for education scholarships, or in any other manner for non-charitable purposes. Accordingly, payments made to the relinquishing and the remaining beneficiaries pursuant to the settlement agreement are not taxable expenditures that are subject to tax under § 4945.

Requested Ruling 6:

Payments made by Foundation to the relinquishing beneficiaries and the remaining beneficiaries pursuant to the settlement agreement after the date Foundation converts to private foundation status will not result in a termination of Foundation’s private foundation status under § 507(a), and will not subject Foundation to any termination tax liability under § 507(c) of the Code.

Section 507(a) provides that, except as provided in subsection (b), the status of any organization as a private foundation shall be terminated only if (1) it notifies the Secretary of its intent to accomplish such a termination or (2) 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 the Secretary notifies such organization that it is liable for the tax imposed by § 507(c), and either such organization pays the tax (or any portion not abated under § 507(g)) or the entire amount of such tax is abated under § 507(g).

Section 507(b)(2) says that in the case of a transfer of assets of any private foundation to another private foundation pursuant to any liquidation or other adjustment, organization, or reorganization, the transferee foundation shall not be treated as a newly created organization.

Treas. Reg. § 1.507-1(a) provides that except as provided in § 1.507-2, the status of any organization as a private foundation shall be terminated only if: (1) such organization notifies the district director of its intent to accomplish such termination, or (2)(i) 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 a liability for tax under Chapter 42, and (ii) the Commissioner notifies such organization that, by reason of subdivision (i) of this subparagraph, such organization is liable for the tax imposed by § 507(c), and either such organization pays the tax imposed by § 507(c) or the entire amount of such tax is abated under § 507(g).

Treas. Reg. § 1.507-1(b)(6) provides that a transfer of all or part of a private foundation's assets to one or more private foundations pursuant to a transfer described in § 507(b)(2), such transferor foundation will not be deemed to have terminated its private foundation status under § 507(a)(1).

Treas. Reg. § 1.507(b)(7) provides that neither a transfer of all 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 § 507(a) unless the transferor private foundation elects to terminate pursuant to §§ 507(a)(1) or 507(a)(2).

Treas. Reg. § 1.507-3(c)(2) provides that the term "significant disposition of assets to one or more private foundations" shall include any disposition for a taxable year where the aggregate of the dispositions to one or more private foundations for the taxable year is twenty-five percent or more of the fair market value of the net assets of the foundation at the beginning of the taxable year.

Foundation represents that it does not intend to terminate its private foundation status under either § 507(a) or (b) even if the distributions it makes to the beneficiaries exceeds twenty-five percent or more of the fair market value of Foundation's net assets, nor is there any indication that Foundation committed any willful repeated acts (or failures to act), or a willful and flagrant act (or failure to act), giving rise to a liability for tax under Chapter 42. Since Foundation will not elect to terminate pursuant to

§ 507(a) or (b), Foundation's private foundation status will not be terminated under § 507, and Foundation is not subject to a termination tax pursuant to § 507(c), provided that Foundation does not commit any willful repeated acts (or failures to act), or a willful and flagrant act (or failure to act) that gives rise to a liability for tax under Chapter 42.

Requested Ruling 7:

For the calendar year that includes the date that Foundation converts to a private foundation, Foundation's liability for the excise tax under § 4940 will apply only to net investment income earned during the part of that year during which Foundation was classified as a private foundation, and Foundation's distributable amount under § 4942 will be computed on the basis of only such part of that year.

Section 4940(a) imposes an excise tax on a private foundation's net investment income for the taxable year. Section 4940(c)(1) defines net investment income as the amount by which the sum of the gross investment income and the capital gain net income exceeds the deductions allowed under § 4940(c)(3). Section 4940(c)(2) provides, in part, that for purposes of § 4940, the term "gross investment income" means the gross amount of income from interest, dividends, rents, payments with respect to securities loans, and royalties.

Section 4942(a) generally imposes a tax on the undistributed income of a private foundation (other than an operating foundation under § 4942(j)(3)) for any taxable year, that has not been distributed before the first day of the second (or any succeeding) taxable year following such taxable year.

Section 4942(c) defines undistributed income for any taxable year as the amount by which the distributable amount for such taxable year, exceeds the qualifying distributions made out of such distributable amount for such taxable year.

Section 4942(d) provides that the term distributable amount means, with respect to any private foundation for any taxable year, an amount equal to the sum of the minimum investment return plus the income modifications described in § 4942(f)(2)(C), reduced by the sum of the taxes imposed on such private foundation for the taxable year under subtitle A and § 4940.

Section 4942(e)(1) defines the term 'minimum investment return' as 5 percent of the excess of the aggregate fair market value of a private foundation's assets other than those which are used (or held for use) directly in carrying out the foundation's exempt purpose, over the acquisition indebtedness with respect to assets whose fair market values are included in the calculation.

Treas. Reg. § 53.4942(a)-2(c)(5)(iii) provides that in any case in which a taxable year is a period less than 12 months, the applicable percentage to be applied under

§ 4942(e)(1) shall be equal to 5 percent multiplied by a fraction, the numerator of which is the number of days in such short taxable period and the denominator of which is 365.

Prior to Foundation's reclassification, Foundation is a public charity supporting organization described in § 509(a)(3). Excise taxes under § 4940 and § 4942 are applicable only to private foundations. Consequently, Foundation will only be subject to § 4940 and § 4942 taxes after it is reclassified as a private foundation. Thus, § 4940 taxes will apply only to the net investment income that Foundation receives after the reclassification. Furthermore, the distributable amount under § 4942 will be computed based on the short taxable period following Foundation's reclassification to private foundation status.

Requested Ruling 8:

Foundation will be required to file both a Form 990 to report activity occurring during the portion of the conversion year before the reclassification while Foundation is a Type III supporting organization, and a Form 990-PF to report activity occurring during the portion of the conversion year beginning after the reclassification when Foundation will be a private foundation.

Section 6001 provides that every person liable for a tax imposed by the Code, or for collection thereof, shall keep adequate records as the Secretary of the Treasury or his delegate may from time to time prescribe.

Section 6033(a)(1) provides that except as provided in § 6033(a)(2), every organization exempt from tax under § 501(a) shall file an annual return, stating specifically the items of gross income, receipts and disbursements, and such other information for the purposes of carrying out the internal revenue laws as the Secretary may by forms or regulations prescribe, and keep such records, render under oath such statements, make such other returns, and comply with such rules and regulations as the Secretary may from time to time prescribe.

The instructions for the Form 990, "Return of Organization Exempt From Income Tax", provide that the Form 990 is filed by organizations described in section 501(c)(3) (other than private foundations). The instructions for the Form 990-PF, "Return of Private Foundation or Section 4947(a)(1) Nonexempt Charitable Trust Treated as a Private Foundation", provide that the Form 990-PF is filed by tax-exempt private foundations.

During the tax year that Foundation is reclassified, Foundation will be classified as a public charity under § 509(a)(3) for the portion of the year prior to the reclassification, and as a private foundation for the portion of the year after the reclassification. Public charities are required to file a Form 990. Private foundations are required to file a Form 990-PF. Accordingly, Foundation should file a Form 990 reflecting its activities for the portion of the tax year that it is a public charity under § 509(a)(3), and Foundation

should file a Form 990-PF reflecting its activities for the portion of the year after the reclassification when it is a private foundation.

Conclusion

Based on the foregoing, and assuming the accuracy of the facts and representations described herein, we rule as follows with respect to Foundation:

1. Pursuant to Rev. Proc. 2017-3 and Rev. Proc. 2017-5, we are not ruling regarding whether the proposed conversion of Foundation or the transactions discussed in the settlement agreement affect Foundation's tax-exempt status or classification.
2. Foundation's reclassification to a private foundation and the payments made to the beneficiaries pursuant to the settlement agreement will not constitute an excess benefit transaction under § 4958 to Foundation.
3. Foundation's reclassification to a private foundation and the payments made to the beneficiaries pursuant to the settlement agreement will not constitute self-dealing under § 4941.
4. Payments made by Foundation to the beneficiaries pursuant to the settlement agreement will be qualified distributions for Foundation under § 4942(g).
5. Payments made by Foundation to the beneficiaries pursuant to the settlement agreement will not constitute taxable expenditures under § 4945(d).
6. Payments made by Foundation to the beneficiaries pursuant to the settlement agreement will not result in a termination of Foundation's private foundation status under § 507(a), and will not subject Foundation to any termination tax liability under § 507(c).
7. For the tax year that Foundation reclassifies to a private foundation, Foundation's liability for § 4940 taxes will only apply to the net investment income that Foundation receives after the reclassification. Furthermore, the distributable amount of Foundation's income under § 4942 will be computed based on the short taxable period following Foundation's reclassification to a private foundation.
8. For the tax year that Foundation reclassifies to a private foundation, Foundation should file a Form 990, reflecting its activities for the portion of the tax year that it is a public charity under § 509(a)(3), and Foundation should file a Form 990-PF, reflecting its activities for the portion of the tax year after the reclassification when it is a private foundation.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party, as specified in Rev. Proc. 2017-1, 2017-1 I.R.B. 1. This office has not verified any of the material submitted in support of the request for ruling, and such material is subject to verification on examination. The Associate office will revoke or modify a letter ruling and apply the revocation retroactively if there has been a misstatement or omission of controlling facts; the facts at the time of the transaction are materially different from the controlling facts on which the ruling was based; or, in the case of a transaction involving a continuing action or series of actions, the controlling facts change during the course of the transaction. See Rev. Proc. 2017-1.

No ruling is granted as to whether Foundation qualifies as an organization described in § 501(c), and, except as expressly provided above, no opinion is expressed or implied concerning the federal income tax consequences of any other aspects of any transaction or item of income described in this letter ruling.

This letter is directed only to Foundation. Section 6110(k)(3) provides that it may not be used or cited by others as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

If you have any questions about this ruling, please contact the person whose name and phone number are shown in the heading of this letter.

Sincerely,

Don Spellmann
Senior Counsel
Exempt Organization Branch 3
(Tax Exempt & Government Entities)

Enclosure: Notice 437, Notice of Intention to Disclose
Redacted copy of this letter

cc: