

**Office of Chief Counsel
Internal Revenue Service
memorandum**

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subject: Amount Involved in a Section 4941 Self-Dealing Loan - Interest and the Effect of the
Period of Limitations

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent.

ISSUE

You have asked whether, for purposes of the section 4941(a)(1)¹ excise tax on a self-dealing loan, interest that accrues² on the loan during years for which the section 6501 period of limitation has closed (a “closed year”) is included in the loan balance to compute the amount involved for the deemed acts of self-dealing that occur in years for which the period of limitations is still open (an “open year”).

CONCLUSION

Interest that accrues during closed years is included in the loan balance to compute the amount involved for the deemed acts of self-dealing in open years. Section 6501 generally prohibits the assessment of amounts of tax more than three years after the filing of a return. Although the Service may not assess the section 4941 excise tax for acts of self-dealing that occurred in closed years, any accrued interest and principal

¹ Unless otherwise noted, all section references are to the Internal Revenue Code of 1986, as amended.

² References to accrued interest in this memo assume that the disqualified person has not paid the accrued interest.

payments from closed years affect the loan balance going forward and must be accounted for to determine the amount involved for deemed acts of self-dealing that occur in open years.

FACTS

A private foundation makes a loan to a disqualified person described in section 4946(a), which constitutes an act of self-dealing under section 4941(d)(1)(B). Unpaid interest is to be added to the loan balance each year. The disqualified person does not make any payments of interest or principal. By the time the loan is addressed during an examination, the period of limitations has expired for the initial act of self-dealing that occurred on the date the loan was made and for several of the earliest deemed acts of self-dealing within the taxable period.³

LAW AND ANALYSIS

Section 4941(a)(1) imposes an excise tax on each act of self-dealing between a disqualified person and a private foundation. The rate of tax is equal to 10% of the amount involved with respect to the act of self-dealing for each year (or part thereof) in the taxable period.

Section 4941(e)(1) defines “taxable period” as the period beginning with the date on which the act of self-dealing occurs and ending on the earliest of (1) the date of mailing of a notice of deficiency with respect to the section 4941(a)(1) tax, (2) the date on which the section 4941(a)(1) tax is assessed, or (3) the date on which correction of the act of self-dealing is completed.

Section 4941(e)(2) defines the term “amount involved” as, in general, the greater of the amount of money and the fair market value of the other property given or the amount of money and the fair market value of the other property received with respect to an act of self-dealing. In the case of taxes imposed by section 4941(a), the fair market value is determined as of the date on which the act of self-dealing occurs.

Section 6501(a) provides that, generally, the amount of any tax imposed shall be assessed within three years after the filing of a return.

Section 6501(l)(1) provides that for purposes of any tax imposed by chapter 42 (other than section 4940), the return referred to in section 6501 is the return filed by the private foundation for the year in which the act (or failure to act) giving rise to liability for such tax occurred.

³ In general, a separate period of limitations applies to each deemed act of self-dealing beginning when the private foundation files its Form 990-PF for the foundation’s taxable year in which the deemed act of self-dealing occurred. See section 6501(l)(1).

Treas. Reg. § 53.4941(e)-1(b)(2)(ii) provides that where the use of money or other property is involved, the amount involved shall be the greater of the amount paid for such use or the fair market value of such use for the period for which the money or other property is used.

Section 53.4941(e)-1(b)(3) provides that, in the case of taxes imposed by section 4941(a), the fair market value of the property or the use thereof is determined as of the date on which the act of self-dealing occurred.

Section 53.4941(e)-1(b)(4), Ex. 2 illustrates that when the amount involved is determined based on the fair market value of the use of money, it is computed by multiplying the loan balance on the date the act of self-dealing occurred, the fair market interest rate on that date, and the period of use.

Section 53.4941(e)-1(e)(1)(i) provides that if a transaction relates to the leasing of property, the lending of money or other extension of credit, other use of money or property, or payment of compensation, the transaction will generally be treated as giving rise to an act of self-dealing on the day the transaction occurs, plus an act of self-dealing on the first day of each taxable year or portion of a taxable year which is within the taxable period and which begins after the taxable year in which the transaction occurs.

Section 53.4941(e)-1(e)(1)(ii), Ex. 2 illustrates that where a continuing act of self-dealing, such as a lease, occurs over a four-year period, there are four separate acts of self-dealing, four amounts involved, and four taxable periods.

A self-dealing loan is generally treated for purposes of section 4941 as giving rise to an act of self-dealing on the date the loan occurs (the "initial act of self-dealing") plus an act of self-dealing on the first day of each taxable year or portion of a taxable year that is within the taxable period.⁴ (These additional acts of self-dealing are referred to in this memo as "deemed acts.") For each deemed act, there is a separate taxable period beginning on the date the deemed act occurred and a separate amount involved. See § 53.4941(e)-1(e)(1)(ii), Ex. 2.

The section 4941(a)(1) excise tax is equal to 10% of the amount involved with respect to an act of self-dealing for each year (or part thereof) in the taxable period. The amount involved in an act of self-dealing involving the use of money (such as a loan) is the greater of the amount paid for such use (i.e., the interest paid) or the fair market value of such use for the period used. Under the facts presented, no amount of interest was paid by the disqualified person for use of the loan. Accordingly, the amount involved for each act of self-dealing must be computed based on the fair market value of use of the

⁴ The relevant taxable year for determining when a deemed act of self-dealing occurs is the taxable year of the disqualified person rather than that of the private foundation. See Rev. Rul. 75-391, 1975-2 CB 446. As noted above, however, the filing of Form 990-PF for the foundation's taxable year in which the deemed act occurs starts the limitations period for the deemed act.

outstanding loan balance due to the private foundation, which includes the principal remaining on the loan and any accrued but unpaid interest. The fair market value of such use is computed by multiplying the loan balance on the date the act of self-dealing occurred, the fair market interest rate on that date, and the period of use. See § 53.4941(e)-1(b)(3) and (4), Ex. 2.

To compute the amount involved for a deemed act of self-dealing, the loan balance as of the date the deemed act occurred must be determined, taking into account any accrued interest on the loan and payments of principal up to that date.⁵ The amount involved for a deemed act of self-dealing is determined as of the date the deemed act occurred and is not affected by expiration of the period of limitations for an earlier act of self-dealing.

The effect of section 6501 is that the Service may not assess amounts of tax for acts of self-dealing that occurred in closed years. However, the loan balance, including accrued but unpaid interest, is not an amount of tax. Section 6501 does not prevent accrued interest and payments of principal, regardless of whether they were incurred or made in open or closed years, from affecting the loan balance used in determining the amount involved.⁶

Consequently, interest that accrues on a loan during closed years is included in the loan balance to compute the amount involved for a deemed act of self-dealing that occurs in an open year.

Please call Christopher Hyde at 202-317-5800 if you have any further questions.

⁵ See Rev. Rul. 2002-43, 2002-28 IRB 85; see also Rev. Rul. 2006-38, 2006-29 IRB 80. Although these revenue rulings apply to prohibited transactions under section 4975, they illustrate general principles used to calculate the amount involved, because the amount involved in both rulings is determined by the application of § 53.4941(e)-1, which governs both section 4941 and section 4975. See Temp. Reg. § 141.4975-13. Although Rev. Rul. 2006-38 states that it does not apply to self-dealing violations under section 4941, we believe this caveat is directed to the fact that the section 6621(a)(2) underpayment rate used to calculate the amount involved when an employer does not timely pay elective deferrals to a qualified plan may not be appropriate for self-dealing violations under section 4941. Rev. Rul. 2006-38 is cited here only to the extent it applies and illustrates the general principles of Treas. Reg. § 53.4941(e)-1.

⁶ It is well recognized that with respect to net operating losses, the Service may make adjustments to items originating in years otherwise barred by the period of limitations under section 6501 in order to determine the tax for an open year to which those items are carried. See *Mennuto v. Commissioner*, 56 T.C. 910, 923 (1971) (“[T]he critical element is that the deficiency being determined is for a year on which the period of limitations has not run.”).