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Internal Revenue Service

Department of the Treasury

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No Third Party Contacts

Contact Person

Telephone Number

Reference to OP:E:EO:T:3

Date

NOV 24 1998

Legend:

X =
Y =
Z =

A =
B =
C =

X =

Dear Sir or Madam:

This refers to your rulings request concerning section 507(b)(2) of the Internal Revenue Code (the "Code").

X is exempt under section 501(c)(3) of the Code and a private foundation under 509(a). X owns marketable assets having a value of approximately x dollars. X has made several significant pledges to a number of public charities described in section 170(b)(1)(A)(i)(vi) of the Code. X has no outstanding grants which require X to exercise expenditure responsibility.

X was incorporated by A. A has died and his two sons, B and C, currently serve as directors of X.

Y and Z were recently formed for the same purpose as X of providing financial support to organizations exempt under section 501(c)(3) of the Code. B incorporated Y and is its sole member. C incorporated Z and is its sole member. Y and Z are recognized as exempt under section 501(c)(3) of the Code and are private A

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foundations under section 509(a).

For efficiency of operation, it is proposed that the assets of X be equally distributed between Y and Z. Furthermore, it is anticipated that all of the pledges to public charities made by X be also equally assumed by Y and Z.

X has not provided a notification that it intends to terminate its private foundation status, nor has it ever received a notification that its status as a private foundation has been terminated.

Section 507(a)(1) of the Code provides that, except as provided in section 507(b), the status of an organization as a private foundation shall be terminated if the organization notifies the Secretary in the manner prescribed in the Income Tax Regulations of its intent to accomplish such termination and the organization either pays the tax imposed by section 507(c) (or any portion not abated under section 507(g)) or the tax is abated under section 507(g).

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

Section 507(c) of the Code imposes a tax on each organization which terminates its private foundation status under section 507(a).

Section 1.507-1(b)(6) of the Income Tax Regulations (the "regulations") provides that if a private foundation transfers all or part of its assets to one or more other private foundations pursuant to a transfer described in section 507(b)(2) of the Code, such transferor foundation will not have terminated its private foundation status under section 507(a)(1).

Section 1.507-3(a)(1) of the regulations provides that in the case of a significant disposition of assets to one or more private foundations within the meaning of paragraph (c) of this section, the transferee organization shall not be treated as a newly created organization. A transferee organization to which this paragraph applies shall be treated as possessing those attributes and characteristics of the transferor organization which are described in subparagraphs (2), (3), and (4) of this paragraph.

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Section 1.507-3(a)(2)(i) of the regulations provides that a transferee organization to which this paragraph applies shall succeed to the aggregate tax benefit of the transferor organization.

Section 1.507-3(a)(4) of the regulations provides that if a private foundation incurs liability for one or more of the taxes imposed under Chapter 42 (or any penalty resulting therefrom) prior to, or as a result of, making a transfer of assets described in section 507(b)(2) to one or more private foundations, in any case where transferee liability applies, each transferee foundation shall be treated as receiving the transferred assets subject to such liability to the extent that the transferor foundation does not satisfy such liability.

Section 1.507-3(a)(8)(ii) of the regulations provides that the provisions enumerated in subparagraphs (a) through (g) of paragraph (8) apply to a transferee foundation to the same extent and in the same manner as they would have applied to the transferor foundation had the transfer described in section 507(b)(2) not been effected

Section 1.507-3(c)(1) of the regulations provides, in part, that a transfer of assets is described in section 507(b)(2) if it is made by a private foundation to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization, or reorganization. The terms "other adjustment, organization, or reorganization" include any partial liquidation or any other significant disposition of assets to one or more private foundations, other than transfers for full and adequate consideration or distributions out of current income.

Section 1.507-3(c)(2) of the regulations provides, in part, that the term "significant disposition of assets to one or more private foundations" includes any disposition for the taxable year of 25% or more of the fair market value of the net assets of the foundation at the beginning of the taxable year.

Section 1.507-3(d) of the regulations provides that unless a private foundation voluntarily gives notice pursuant to section 507(a)(1), a transfer of assets described in section 507(b)(2) will not constitute a termination of the transferor's private foundation status under section 507(a)(1). Such transfer must, nevertheless, satisfy the requirements of any pertinent provisions of Chapter 42.

Section 1.507-4(b) of the regulations provides that private foundations which make transfers described in section 507(b)(2)

are not subject to the tax imposed under section 507(c) with respect to such transfers unless the provisions of section 507(a) become applicable.

Section 4940(a) of the Code imposes on a private foundation with respect to the carrying on of its activities, a tax equal to 2% of its net investment income for the taxable year.

Section 4941(a) of the Code provides for the imposition of a tax on each act of self-dealing between a disqualified person and a private foundation.

Section 53.4946-1(a)(8) of the Foundation and Similar Excise Tax Regulations (also the "regulations") provides that, for purposes of section 4941 only, the term "disqualified person" shall not include any organization which is described in section 501(c)(3) (other than an organization described in section 509(a)(4)).

Section 4942(a) of the Code provides, in part, for the imposition of a tax on the undistributed income of a private foundation.

Section 4942(c) of the Code provides, in part, that the term "undistributed income" means, with respect to any private foundation for any taxable year, the amount by which the distributable amount for such taxable year exceeds the qualifying distributions made before such time out of such distributable amount.

Section 1.507-3(a)(5) of the regulations provides that, except as provided in subparagraph (9) of this paragraph, a private foundation is required to meet the distribution requirements of section 4942 for any taxable year in which it makes a section 507(b)(2) transfer of all or part of its net assets to another private foundation. Such transfer shall itself be counted toward satisfaction of such requirements to the extent the amount transferred meets the requirements of section 4942(g).

Section 4944(a) of the Code provides generally for the imposition of a tax on a private foundation and a foundation manager if investments are made in such a manner as to jeopardize the carrying out of the foundation's exempt purposes.

Section 4945(a) of the Code imposes a tax on each taxable expenditure (as defined in section 4945(d)) of the private foundation.

Section 4945(d)(5) of the Code provides that the term

"taxable expenditure" means an amount paid or incurred by a private foundation for any purpose other than one specified in section 170(c)(2)(B).

Section 53.4945-6(c)(3) of the regulations provides that if a private foundation makes a transfer of assets pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization, or reorganization to any person, the transferred assets will not be considered used exclusively for purposes described in section 170(c)(2)(B) unless the assets are transferred to a fund or organization described in section 501(c)(3) (other than an organization described in section 509(a)(4)).

Section 53.4945-5(b)(7) of the regulations provides that for rules relating to the extent to which the expenditure responsibility rules contained in section 4945(d)(4) and (h) and this section apply to transfers of assets described in section 507(b)(2), see sections 1.507-3(a)(7), 1.507(a)(8)(ii)(f) and 1.507-3(a)(9).

Section 1.507-3(a)(7) of the regulations provides that except as provided in subparagraph (9) of this paragraph, where the transferor has disposed of all of its assets, during any period in which the transferor has no assets, section 4945(d)(4) and (h) shall not apply to the transferee or the transferor with respect to any "expenditure responsibility" grants made by the transferor.

Section 1.507-3(a)(9)(i) of the regulations provides that if a private foundation transfers all of its net assets to one or more private foundations which are effectively controlled, directly or indirectly, by the same person or persons which effectively controlled the transferor private foundation, for purposes of chapter 42 (section 4940 et seq.) and part II of subchapter F of chapter 1 of the Code (sections 507 through 509) such a transferee private foundation shall be treated as if it were the transferor. However, where proportionality is appropriate, such a transferee private foundation shall be treated as if it were the transferor in the proportion which the fair market value of the assets (less encumbrances) transferred to such transferee bears to the fair market value of the assets (less encumbrances) of the transferor immediately before the transfer.

The proposed transaction involves a significant disposition of assets within the meaning of section 1.507-3(c)(1) of the regulations. Accordingly, the proposed transfer is described in section 507(b)(2) of the Code and not subject to tax under

section 507(c). Consistent with the provisions of section 507(b)(2) and the regulations promulgated thereunder, Y and Z will not be treated as newly created organizations. Also, Y and Z will be deemed to possess certain attributes and characteristics of X, including being entitled to a pro-rata portion of X's aggregate tax benefit not exceeding the fair market value of the transferred assets at the time of the proposed transfer. In addition, and as long as Y and Z are exempt under section 501(c)(3) of the Code, the transfer of X's assets to them will constitute a distribution for a charitable purpose and will not be treated as self-dealing, jeopardizing investments or taxable expenditures within the meaning of sections 4941, 4944 and 4945.

Based on the foregoing, we rule, as requested, as follows:

1. The transfer by X of all of its assets to Y and Z will be a significant disposition of assets to one or more private foundations as described in section 1.507-3(c) of the regulations made pursuant to an adjustment or reorganization, and will be a transfer of assets by a private foundation to another foundation described in section 507(k)(2) of the Code. Accordingly, Y and Z, as transferees of all of the total assets of X, will be treated as if they were X for purposes of sections 4946 through 4948 and sections 507 through 509 of the Code.

2. The transfer of assets will not affect the continued qualification of X as an organization described in section 501(c)(3) of the Code that is exempt from federal income tax under section 501(a) and will not result in the termination of X's private foundation status pursuant to section 507(b)(1) prior to the time that it files notice of its intent to terminate, and will not result in X being subject to the tax imposed by 507(c) in the year of the transfer.

3. X will not be subject to the termination tax imposed by section 507(c) of the Code if it has no assets as of the date notice of intent to accomplish termination under section 507(a)(1) is given.

4. Pursuant to section 1.507-3(a)(2) of the regulations, Y and Z will succeed to the aggregate tax benefits of X in proportion to the net fair market value of the assets transferred to them. Following the transfer, Y and Z may each proportionately reduce the amount of the required distribution under section 4942

of the Code, by the amount, if any of X's excess qualifying distributions carryover for prior years as defined under section 4942(i). Y and Z will be treated as having received the transferred assets subject to the proportionate amount of any liability that X may have incurred under Chapter 42 of the Code, to the extent not satisfied by X.

5 Following the transfer, X will be liable for the tax imposed by section 4940 of the Code on assets held until the date of the transfer. After the transfer has occurred, Y and Z will be liable for the tax imposed under section 4940 with respect to their respective share of assets as of the date of the transfer.

6. The provisions of 1.507-3(a)(8)(ii)(a) through (g) of the regulations will apply to Y and Z with respect to the assets transferred to them from X.

7. The transfer of X's assets to the newly created entities will not constitute an act of self-dealing under section 4941 of the Code by the transferor foundation, by the transferee foundations or by any disqualified person.

8. The transfer of X's assets to Y and Z will not constitute a jeopardizing investment within the meaning of section 4944(a) of the Code by the transferor foundation, by the transferee foundations or by any disqualified person.

9. The transfer of X's assets to the newly created entities will not constitute taxable expenditures within the meaning of section 4945 of the Code, nor will such transfer constitute a grant for which X, Y or Z will be required to exercise expenditure responsibility within the meaning of section 4945(d)(4).

10. X's transfer of all of its assets to the transferee foundations may in itself be counted toward satisfaction of its charitable requirements under section 4942, if, and to the extent that section 4942(g) is met by it in that specific regard.

11. X will not be required to comply with the record-keeping requirements of 4942(g)(3)(B) of the Code with respect to the transfer of its assets to Y and Z for any taxable year subsequent to the taxable

year in which the transfer of its assets occurs.

12. The proposed assignment by X of all of its outstanding pledges to Y and Z and the assumption by Y and Z of those pledges will not constitute an act of self-dealing under 4941 of the Code.

13. The proposed assignment and assumption will not violate any of the other Chapter 42 excise tax provisions, will not constitute a taxable expenditure within the meaning of section 4945 of the Code, nor will such transfer constitute a grant for which X, Y or Z will be required to exercise expenditure responsibility within the meaning of section 4945(d)(4) of the Code.

14. The proposed assignment and assumption will not obligate X to comply with the record-keeping requirements of section 4942(g)(3)(B) of the Code with respect to the assigned pledges.

We are informing your Key District of this ruling. Please keep a copy of it in your permanent records.

We express or imply no opinion as to the federal tax consequences of the transactions under any other provisions of the Code. This ruling is directed to the organization that requested it. Section 6110(j)(3) of the Code provides that it may not be used or cited by others as precedent.

Sincerely,

Kenneth J. Earnest
Kenneth J. Earnest
Acting Chief,
Exempt Organizations
Technical Branch 3

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