SIN 513.00-00
4941.04-00

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

199943053

Date: AUG 5 - 1999

Contact Person:

ID Number:

Telephone Number:

OP:E:EO:T:2

Dear Sir or Madam:

This responds to your request for ruling dated November 24, 1998, as supplemented by information submitted in your letters of March 12, 1999 and June 30, 1999. You ask us to consider whether the providing of services and facilities as described below will be functionally related to your exempt purposes, and whether tax under Section 4941 of the Internal Revenue Code will arise as the result of providing of such services and facilities.

You filed articles of incorporation as a domestic nonprofit corporation on December 17, 1996 which provide you are organized exclusively for charitable purposes, and limit your activities to meet the organization test provided in Section 501(c)(3) of the Internal Revenue Code of 1986 (Code). In March 1998, you filed an application for recognition of exemption from income tax as an organization described in Section 501(c)(3) of the Code. In your application, you stated your intent to provide and operate a home for the developmentally disabled, and your expectation that between eight and ten developmentally disabled individuals would reside in the home. You stated you would be supported by a combination of contributions from your founder, investment income, foundation grants, and resident fees. You stated you owned property and were planning to build a facility for the above purposes on that land. You were determined to be exempt from income tax as an organization described in Section 501(c)(3) of the Code, and you were also determined to be a private foundation.

In your ruling request you iterate you are in the process of establishing an adult foster care home ("facility") for developmentally disabled individuals who are "severely, and severely and mentally handicapped" as those terms are used by the County Community Mental Health Services ("County") where you are located. Typically, such individuals are placed in institutions, but group homes provide an alternative to institutionalization. Information provided by County confirms there is shortage of facilities of the type you propose, and there is a waiting list of approximately one year for male individuals, and six months for females, before County is able to place such individuals in care. You further indicate your facility will serve six individuals, rather than the eight to ten individuals contemplated in your original application for recognition of exemption. This reduced number is a consequence of zoning restrictions. Information you submitted from the Zoning Administrator in the township where you are located confirms that you would be required to seek a zoning variance from the township if your facility were to attempt to serve more than six persons. The zoning administrator of the township confirms that the citizens of the township would be unlikely to approve of a variance for your facility, but state law supersedes all zoning laws applicable facilities housing six or fewer individuals.

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Your ruling request also provides detailed information about the proposed operation of your facility. Residents of your facility would be those requiring 24 hour supervision. State regulations permit you to charge such individuals a specified monthly fee payable from their social security benefits. In addition, the state reimburses you for the additional cost of necessities. You indicate, however, that this provides only the barest essentials and does not permit residents to attain a quality of life non-handicapped persons would find acceptable. You therefore expect to supply an environment and services above that provided by government allowances. Examples you cite of these services include recreational facilities, transportation to work (where a resident is able), entertainment and shopping, and individually designed separate living areas for each resident. You will bear the cost of these upgraded standards using donations you expect to receive. You indicate that you are committed to admitting only persons whose needs are equivalent, and that any differences in care offered residents will be the result of changes in a resident's condition after admission.

Finally, you represent that you will operate your facility at its capacity of six individuals, excepting brief vacancies occurring when a resident leaves the facility and is replaced by another. You indicate one of the six residents in your facility will be a disqualified person. This individual has been tested by the county and found to meet the criteria for residence. The remaining five individuals will also be tested by county and will be eligible as severely and multiply handicapped. You have stipulated that all gifts, grants and contributions you receive will be commingled and used to provide equal care for all residents.

Section 4941(a)(1) of the Code imposes a tax on each act of self-dealing between a disqualified person and a private foundation.

Section 4941(d)(1)(C) of the Code defines self-dealing as any direct or indirect furnishing of goods, services or facilities between a private foundation and a disqualified person.

Section 4941(d)(2)(D) of the Code provides that the furnishing of good, services, or facilities by a private foundation to a disqualified person shall not be an act of self-dealing if such furnishing is made on a basis no more favorable than that on which goods, services or facilities are made available to the general public.

Section 53.4941(d)-3(b)(1) of the Foundation and Similar Excise Tax Regulations provides the furnishing of goods, services or facilities by a private foundation to a disqualified person is not considered an act of self-dealing if such goods, services or facilities are made available to the general public on at least as favorable a basis as they are made available to the disqualified person. This exception does not apply, however, unless such goods, service or facilities are related, within the meaning of Section 4942(j)(5) of the Code, to the exercise or performance by a private foundation of its charitable purpose.

Section 4942(j)(5) of the Code includes certain elderly care facilities in the definition of "operating foundation" only if such facility meets the requirements of Section 4942(j)(3)(B)(ii) of the Code.

Section 4942(j)(3)(B)(ii) of the Code defines operating foundation to include an organization which normally makes qualifying distributions directly for the active conduct of the activities constituting the purpose or function for which it is organized and operated.

Section 53.4941(d)-3(b)(2) of the regulations defines "general public" to include those persons who, because of the particular nature of the activities of the private foundation, would be reasonably expected to utilize such goods, services or facilities of the private foundation. This provision does not apply unless there are a substantial number of persons other than disqualified persons who are actually utilizing such goods, services or facilities. This regulation cites, as examples, a private foundation which makes recreational or park facilities to the general public and disqualified persons on the same basis, and the

sale of a book or magazine to disqualified persons on the same terms as members of the general public.

Revenue Ruling 76-10, 1976-1 C.B. 355 considered whether the use by a government official, a disqualified person by definition, of a private foundation's library meeting room would be an act of self-dealing. The ruling held that, generally, the government official's use of foundation's facility would be an act of self-dealing. In this circumstance, however, the room was made available on the same basis to both the disqualified person and other community and civic groups. In addition, use of the room for communications between the government official and members of the public was functionally related to the foundation's exempt purpose of making the room available for civic and community purposes. Accordingly, it was held that use by the government official did not constitute an act of self-dealing.

Revenue Ruling 76-459, 1976-2 C.B. 369 considered whether a disqualified person's use of a private road, owned by a private foundation, constituted an act of self-dealing. The foundation's museum property was adjacent to a manufacturing plant owned by a corporation which was the disqualified person. The road in question separated the foundation's museum from the manufacturing plant, and connects two public streets intersecting at either end. The road is open at all times the museum is open, and is used by museum visitors, the corporation's employees, and as a thoroughfare by the general public. There is no other convenient substitute for traveling between the two public streets, and the road functions as integral part of the municipal street system. The ruling holds that, generally, permitting a disqualified person to use the road would be an act of self-dealing. However, the road is made available to the disqualified person on the same basis as members of the general public, and a substantial number of persons, other than disqualified persons actually use the road. Further, use of the road as an entrance to the foundation's museum if functionally related to the operation of the museum.

In contrast to the above two revenue rulings, Revenue Ruling 79-374, 1979-2 C.B. 387 considered whether office space rented to disqualified persons by a private foundation was an act of self-dealing. In this situation, the foundation owned a small office building and use approximately half the available space. The foundation conducted agricultural economics research and experimentation. The remaining space was rented to disqualified persons engaged in agricultural activities not used by the foundation in its research. It was held that, although the disqualified person was engaged in business in the same general subject area as the foundation's research, the activities of the disqualified persons did not contribute importantly to the foundation's research and experimentation. Because there was a lack of functional relationship, the exception rules provided in Section 4941(d)(2)(D) did not apply.

Section 4942(j)(4) of the Code defines "functionally related business" as a trade or business which is not an unrelated trade or business as defined in Section 513 of the Code.

Section 513 of the Code defines an "unrelated trade or business" as any trade or business the conduct of which is not substantially related, aside from the need of such organization for income or funds, to the exercise of performance by such organization of its charitable purpose or function constituting the basis for its exemption under Section 501(a).

Generally, providing goods, services or facilities to a disqualified person would be an act of self-dealing. You were organized and will be operated care and shelter for severely and multiply handicapped individuals and you were recognized as an organization described in Section 501(c)(3) of the Code as a result. Clearly the conduct of this activity and any income derived from this activity would not be considered as sums derived from an unrelated trade or business. Your intent to utilize your facility for the benefit of persons meeting the criteria for severe and multiply handicapped in county, and to conduct this activity for the benefit of the maximum number of persons permitted by law indicates members of the general public will benefit to the maximum degree consistent with your capacity. Your commitment to provide goods, services and facilities to a disqualified person brings you within the exception to self-

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dealing contained in Section 4941(d)(2)(D) of the Code.

Based on the above, it is held:

1. The facilities and services provided by you are available to the general public and are functionally related to your exempt purposes, and;

2. Your provision of facilities and services to a disqualified person on the same basis as members of the general public will not be treated as an act of self-dealing.

Because this letter could help resolve any questions about your tax status, you should keep it with your permanent records.

This ruling is based on the understanding that there will be no material changes in the facts upon which it is based. Any changes that may have a bearing upon your tax status should be reported to your key District Director.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Internal Revenue Code provides that it may not be used or cited by others as precedent.

Sincerely,

(signed) Garland A. Carter

Garland A. Carter
Chief, Exempt Organizations
Technical Branch 2

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