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

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Contact Person:
T:EO:B2
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Uniform Issue List:
507.00-00
501.03-02
509.03-00
0511.00-00
4940.00-00
4941.04-00
4944.00-00
4945.04-06
6033.02-01
6043.01-00

Legend:
P =
X =
Y =

Dear Sir or Madam:

This is in reply to your rulings request of October 20, 1999, on P's proposed transfer of all of its assets to X and Y pursuant to section 507(b)(2) of the Internal Revenue Code.

P, X, and Y are exempt from federal income tax under section 501(c)(3) of the Code and are private foundations under section 509(a) of the Code. P is also an operating foundation under section 4942(j)(3) of the Code. P's principal asset is its art collection. As part of P's dissolution, P will contribute a substantial portion of its art collection to a museum that is a public charity, not a private foundation, under section 509 of the Code. P will liquidate the balance of its art collection and distribute the proceeds equally shares to X and Y. P has no expenditure responsibility grants outstanding under section 4945(h) of the Code. P will voluntarily terminate its private foundation status by giving the notice under section 507(a)(1) of the Code to the Internal Revenue Service.

The following rulings are requested:

1. P's transfer of all of its assets in equal shares to X and Y will qualify as section 507(b)(2) transfers. Pursuant to section 1:507-1(b)(6) of the Income Tax Regulations, P will not have terminated its private foundation status and, pursuant to section 1.507-4(b) of the regulations, P will not be subject to any tax under section 507(c) of the Code.

2. Under section 1.507-3(a)(9)(i) of the regulations, each of X and Y will be treated as if each were P, in the proportion that the fair market value of P's assets transferred to each of X and Y bears to the fair market value of P immediately before the transfer.

3. P will be terminated for purposes of section 507 of the Code when P complies with the notification requirements of sections 507(a)(1) and 6043(b) of the Code in the year in which P terminates.

4. There will be no tax imposed under section 507(c) of the Code upon P's termination in any taxable year following P's transfers to X and Y because P will have no assets.

5. Any gain realized by P as a result of the proposed sales will not constitute unrelated business taxable income pursuant to section 512 of the Code and therefore will not be subject to the tax on unrelated business taxable income pursuant to section 511 of the Code.

6. P's gain, if any, realized as a result of its transfer of assets will not constitute net investment income pursuant to section 4940 of the Code and will not be subject to the excise tax on net investment income pursuant to section 4940(a) of the Code.

7. P's transfer of assets to X and Y will not constitute a sale or other disposition of property under section 4940(c)(4)(A) of the Code.

8. P's transfer of assets to X and Y will not constitute acts of self-dealing under section 4941 of the Code between P, X, Y, or their directors.

9. P's transfer of assets to X and Y will not constitute jeopardizing investments under section 4944 of the Code.

10. P's transfer of assets to X and Y will not constitute taxable expenditures under section 4945(d) of the Code to P, and P will not be required to exercise expenditure responsibility under section 4945(h) of the Code.

Section 501(c)(3) of the Code provides for the exemption from federal income tax of nonprofit organizations organized and operated exclusively for charitable and/or the other exempt purposes stated in that section.

Section 509(a) of the Code describes organizations exempt from federal income tax under section 501(c)(3) of the Code that are private foundations subject to the provisions of Chapter 42 of the Code.

Section 507(a)(1) of the Code and section 1.507-1(b)(1) of the regulations provide that a private foundation may voluntarily terminate its private foundation status by submitting to the Commissioner a statement of its intention to terminate its private foundation status and by paying the termination tax imposed under section 507(c) of the Code.

Section 507(c) of the Code imposes an excise tax on a private foundation which voluntarily terminates its status as a private foundation under section 507(a)(1) of the Code. This section 507(c) tax is equal to the lower of: (1) the aggregate tax benefit that has resulted from the foundation's exemption from federal income tax under section 501(c)(3) of the Code, or (2) the value of the net assets of the foundation.

Section 507(e) of the Code provides that, for purposes of section 507(c)(2) of the Code, the value of the net assets of the private foundation shall be determined at whichever time the value is higher: (1) the first day on which action is taken by the organization which culminates in its ceasing to be a private foundation or (2) the date on which it ceases to be a private foundation.

Section 507(b)(2) of the Code concerns the transfer of assets by one private foundation to one or more other private foundations, and provides that each transferee private foundation shall not be treated as a newly created organization.

Section 1.507-3(c)(1) of the regulations indicates that a transfer under section 507(b)(2) of the Code includes a transfer of assets from one private foundation to one or more other private foundations pursuant to any reorganization, including a significant disposition of 25% or more of the transferor foundation's assets.

Section 507(d) of the Code provides, in general, that the aggregate tax benefits of an exempt private foundation refer to the value of its exemption from federal income tax and the deductions taken by its donors during its existence.

Section 1.507-1(b)(9) of the regulations provides that a private foundation which transfers all of its assets is not required to file annual information returns required by section 6033 of the Code for its tax years after the tax year of its transfer when it has no assets or activities.

Section 1.507-3(a)(5) of the regulations indicates that a transferor private foundation is required to meet its charitable distribution requirements under section 4942 of the Code, even for any taxable year in which it makes a transfer of its assets to another private foundation pursuant to section 507(b)(2) of the Code.

Section 1.507-3(a)(9)(i) of the regulations indicates that, if a transferor private foundation transfers assets to a private foundation effectively controlled, directly or indirectly, by the same person or persons who effectively control the transferor private foundation, the transferee foundation will be treated as if it were the transferor foundation, for purposes of sections 4940 through 4948 and sections 507 through 509 of the Code. The transferee is treated as the transferor in the proportion which the fair market value of the transferor's assets that were transferred bears to the fair market value of all of the assets of the transferor immediately before the transfer.

Revenue Ruling 78-387, 1978-2 C. B. 270, concerns a private foundation that transferred all of its assets to another private foundation that was effectively controlled by the same persons. In accordance with section 1.507-3(a)(9)(i) of the regulations, the transferee foundation is treated as the transferor foundation and, thus, the transferee can use its transferor's excess qualifying distributions carryover, if any, under section 4942(i) of the Code to reduce the transferee's distributable amount under section 4942 of the Code by the amount, if any, of its transferor's excess qualifying distributions carryover under section 4942(i) of the Code.

Section 1.507-4(b) of the regulations provides that the tax on termination of private foundation status under section 507(c) of the Code does not apply to a transfer of assets pursuant to section 507(b)(2) of the Code.

Sections 1.507-1(b)(7) and 1.507-3(d) of the regulations provide that a transferor foundation's transfer of assets under section 507(b)(2) of the Code will not constitute any termination of the transferor foundation's status as a private foundation.

Sections 511, 512, 513, and 514 of the Code describe the income tax on unrelated business taxable income that applies to income from an unrelated business conducted by an organization that is otherwise exempt from federal income tax pursuant to section 501(c)(3) of the Code.

Section 512(b)(5) of the Code and section 1.512(b)-1(d) of the regulations provide for the exclusion from unrelated business income taxable income of gains or losses from the sale, exchange, or disposition of property or assets that are not held by the exempt organization as stock in trade or inventory or for sale to customers in the ordinary course of business.

Section 513 of the Code defines an unrelated business as a business that is not directly and substantially related to the performance of the organization's exempt purposes.

Section 4940 of the Code imposes excise tax on certain investment income of a private foundation.

Section 4941 of the Code imposes excise tax on an act of self-dealing between a private foundation and any of its disqualified persons under section 4946 of the Code.

Section 53.4946-1(a)(8) of the Foundation and Similar Excise Taxes Regulations provides that, for purposes of self-dealing under section 4941 of the Code, an exempt organization under section 501(c)(3) of the Code is not a disqualified person.

Section 4945 of the Code imposes tax upon a private foundation's making of any taxable expenditure under section 4945(d) of the Code.

Section 4945(d)(4) of the Code requires that, in order to avoid making a taxable expenditure, a transferor private foundation must exercise "expenditure responsibility" under section 4945(h) of the Code on its grants to another private foundation.

Section 4945(d)(5) of the Code provides that a taxable expenditure includes any amount expended by a private foundation for purposes other than the charitable or other purposes under section 170(c)(2)(B) of the Code.

Section 4945(h) of the Code defines expenditure responsibility in terms of a grantor private foundation requiring proper reports from a grantee private foundation on the grantee's uses of a grant.

Sections 53.4945-6(c)(3) and 1.507-3(b) of the regulations allow a private foundation to make transfers of its assets pursuant to section 507(b)(2) of the Code to organizations exempt from federal income tax under section 501(c)(3) of the Code, including private foundations, without the transfers being taxable expenditures under section 4945 of the Code.

Section 1.507-3(a)(7) of the regulations provides that, where a private foundation transfers all of its assets pursuant to section 507(b)(2) of the Code to one or more private foundations exempt from federal income tax under section 501(c)(3) of the Code, the transferor private foundation will have no expenditure responsibility requirement under section 4945(h) of the Code.

Section 6043(b) of the Code and section 1.6043-3(a)(1) of the regulations provides that a private foundation must file its return with respect to its dissolution.

Analysis

P will transfer all of its assets to X and Y. Your requested rulings are discussed below:

1.

Under section 1.507-3(c)(1) of the regulations, a transfer under section 507(b)(2) of the Code includes a transfer of assets from one private foundation to another private foundation pursuant to any reorganization or liquidation, including a significant disposition of 25% or more of the transferor foundation's assets. Because P will transfer all of its assets, P's transfer will be a significant disposition of its assets under section 1.507-3(c)(1) of the regulations and, thus, will be a transfer under section 507(b)(2) of the Code.

Under section 1.507-3(d) of the regulations, P's transfer of assets to X and Y pursuant to section 507(b)(2) of the Code will not terminate P's private foundation status under section 509(a) of the Code.

Under section 1.507-4(b) of the regulations, P's transfer of assets to X and Y pursuant to section 507(b)(2) of the Code will not result in termination tax under section 507(c) of the Code.

2.

Under section 1.507-3(a)(9)(i) of the regulations, transferees X and Y will each be treated as if each were P, in the proportion that the fair market value of P's assets transferred to each of X and Y bears to the fair market value of P immediately before the transfer.

3.

Under section 507(a)(1) of the Code and section 1.507-1(b)(1) of the regulations, P's status as a private foundation under section 509(a) of the Code will be terminated under section 507(a)(1) of the Code when P complies with the notice and requirements of that section 507(a)(1) of the Code.

Under section 1.507(a)-1(b)(9) of the regulations, P must file its final annual information return on Form 990-PF pursuant to section 6043(b) of the Code for the tax year when P terminates.

4.

Under section 507(e) of the Code, after P has transferred all of its assets to X and Y, the value of P's assets will be zero. Thus, P's voluntary notice of termination of its private foundation status under section 509(a) of the Code pursuant to section 507(a)(1) of the Code will not result in tax under section 507(c) of the Code when P has no assets.

5.

P's transfer of a substantial portion of its art collection to a museum, which is exempt from federal income tax under section 501(c)(3) of the Code and is a public charity, not a private foundation, under section 509 of the Code, is a grant of assets to such museum for furtherance of exempt purposes under section 501(c)(3) of the Code and, thus, is not an unrelated sale or disposition of property that results in unrelated business taxable income or unrelated business income tax under sections 511, 512, 513, or 514 of the Code.

Under section 512(b)(5) of the Code, P's liquidation of the balance of its art collection will not be the sale of assets that are held in inventory or trade or business for sale to customers and, thus, P's liquidation of the balance of its art collection will not result in unrelated business taxable income or unrelated business income tax under sections 511, 512, 513, or 514 of the Code.

6. and 7.

P's transfer of its assets pursuant to section 507(b)(2) of the Code to X and Y will not result in income or tax under section 4940 of the Code.

8.

Under section 4941 of the Code, P's transfer of assets to X and Y will not be an act of self-dealing because P's transfer will be for exempt purposes to X and Y as organizations exempt from federal income tax under section 501(c)(3) of the Code, which are not disqualified persons under section 4946 of the Code, for purposes of section 4941 of the Code, pursuant to section 53.4946-1(a)(8) of the regulations.

9.

Under section 4944 of the Code, P's transfer of assets to X and Y is for exempt purposes and will not be a jeopardizing investment or result in tax under that section.

10.

Under section 53.4945-6(c)(3) of the regulations, a private foundation can transfer its assets pursuant to section 507(b)(2) of the Code to an organization exempt from federal income tax under section 501(c)(3) of the Code without the transfer being a taxable expenditure under section 4945 of the Code. Thus, P's transfer of its assets to X and Y will not be a taxable expenditure under section 4945 of the Code or subject P to tax under that section.

Under section 1.507-3(a)(7) of the regulations, where a private foundation transfers all of its assets pursuant to section 507(b)(2) of the Code to one or more private foundations exempt from federal income tax under section 501(c)(3) of the Code, the transferor private foundation will have no expenditure responsibility requirement under section 4945(h) of the Code. Thus, P will not be required to exercise expenditure responsibility under section 4945(h) of the Code with respect to its transfer of all of its assets to X and Y.

Accordingly, we rule:

1. P's transfer of all of its assets to X and Y will qualify as transfers under section 507(b)(2) of the Code. Pursuant to section 1.507-1(b)(6) of the Income Tax Regulations, P will not have terminated its private foundation status and, pursuant to section 1.507-4(b) of the regulations, P will not be subject to any termination tax under section 507(c) of the Code.

2. Under section 1.507-3(a)(9)(i) of the regulations, X and Y will be treated as if each were P in the proportion that the fair market value of P's assets transferred to each bears to the fair market value of P's transferred assets immediately before its transfer.

3. P will be terminated for purposes of section 507 of the Code when P complies with the notification requirements of sections 507(a)(1) and 6043(b) of the Code in the tax year in which P terminates.

4. No tax under section 507(c) of the Code will be imposed on P's termination under section 507(a)(1) of the Code in any tax year when P has transferred all of its assets to X and Y and has no assets.

5. P's transfer and sales of its art collection will not constitute unrelated business taxable income and will not result in unrelated business income tax under section 511 of the Code.

6. and 7. P's transfers of assets to X and Y will not constitute net investment income or a sale or other disposition of property resulting in tax under section 4940 of the Code.

8. P's transfer of assets to X and Y will not constitute acts of self-dealing under section 4941 of the Code between P, X, Y, or their directors or disqualified persons.

9. P's transfer of assets to X and Y will not constitute jeopardizing investments under section 4944 of the Code.

10. P's transfer of assets to X and Y will not constitute taxable expenditures under section 4945(d) of the Code to P, and P will not be required to exercise expenditure responsibility under section 4945(h) of the Code with respect to P's transfer of all of its assets to X and Y.

Because this ruling letter could help to resolve any questions, please keep it in your permanent records and include a copy in your annual return, Form 990-PF.

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

Sincerely,

Joseph Chasin

Joseph Chasin
Acting Manager, Exempt Organizations
Technical Group 2