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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

200238050

Date: JUN 25 2002

Contact Person:

Uniform Issue List: 507.00-00
501.03-02
509.03-00
4940.00-00
4941.04-00
4942.03-05
4945.04-06

Identification Number:

Telephone Number:

T:EO:B2

Legend:
P =
X =
Y =

Dear Sir or Madam:

This is in reply to your rulings request dated December 13, 2001, on P's proposed transfer of approximately one-half of its assets to R and S 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, are private foundations under section 509(a) of the Code, and are effectively controlled by the same persons, consisting of children of the founding substantial contributor to P. P will transfer all of its assets and its charitable pledges and its liabilities to X and Y. After the transfer, P will give notice to the Internal Revenue Service of termination of its private foundation status pursuant to section 507(a)(1) of the Code. P has no expenditure responsibility grants outstanding under section 4945(h) of the Code.

The following rulings are requested:

1. P's transfer of all of its assets to X and Y will not adversely affect the tax-exempt status of P, X, or Y under section 501(c)(3) of the Code.

2. P's transfer of assets to X and Y will not be treated as a transfer to newly created organizations but, instead, will qualify as an adjustment or reorganization under section 507(b)(2) of the Code.

3. P's transfer of assets to X and Y will not terminate P's status as a private foundation under section 507(a) of the Code prior to the time that P files notice of its intent to terminate, and, as a consequence, P's transfer of assets to X and Y will not result in the imposition of tax under section 507(c) of the Code.

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

5. P's transfer of assets to X and Y will not be an act of self-dealing under section 4941 of the Code.

6. P's assignment to X and Y of its obligations with respect to certain outstanding charitable pledges and the assumption of those obligations by X and Y will not constitute an act of self-dealing under section 4941 of the Code.

7. P's transfer of assets to X and Y will be a transfer to foundations effectively controlled by the same person or persons who effectively control P within the meaning of section 1.507-3(a)(9)(i) of the Income Tax Regulations.

8. The recordkeeping requirements of section 4942(g)(3)(B) of the Code will not apply to P during any period in which P has no assets.

9. P's transfer of assets to X and Y will not constitute a taxable expenditure under section 4945 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 the charitable and/or 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 Income Tax Regulations provide that a private foundation may voluntarily terminate its private foundation status by submitting to the Internal Revenue Service a statement of its intention to voluntarily terminate its private foundation status pursuant to section 507(a)(1) of the Code and by paying any termination tax under section 507(c) of the Code.

Section 507(c) of the Code imposes excise tax on a private foundation which voluntarily terminates its private foundation status under section 507(a)(1) of the Code, and provides that this section 507(c) tax is equal to the lower of: (1) the aggregate tax benefits that have resulted from the private foundation's exempt status under section 501(c)(3) of the Code, or (2) the value of the net assets of the 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 or liquidation, including a significant disposition of 25% or more of the transferor foundation's assets computed as of the beginning of its tax year.

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

Section 1.507-3(a)(5) of the regulations provides that a transferor private foundation is required to meet its charitable distribution requirements under section 4942 of the Code, even for any tax 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)(7) of the regulations provides that, where a private foundation has transferred all of its assets to another private foundation in a transfer under section 507(b)(2) of the Code, it is not required to exercise expenditure responsibility under section 4945(h) of the Code with respect to such transfer.

Section 1.507-3(a)(9)(i) of the regulations provides that, if a private foundation transfers assets to one or more private foundations which are effectively controlled directly or indirectly within the meaning of section 1.482-1(i)(4) of the regulations by the same persons who effectively control the transferor foundation, each 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. Each transferee is treated as its transferor in the proportion which the fair market value of the transferor's assets transferred to the transferee bears to the fair market value of all of the transferor's assets immediately before the transfer.

Section 1.507-3(a)(9)(ii) of the regulations provides that a transfer of assets under section 507(b)(2) of the Code does not relieve the transferor private foundation from filing its own final tax year return as required by section 6043(b) 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 under 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 private foundation's transfer of assets under section 507(b)(2) of the Code will not constitute any termination of the transferor foundation's private foundation status under section 509(a) of the Code.

Section 4941 of the Code imposes excise tax on any 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 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 with respect to the private foundation.

Section 4942 of the Code provides that a private foundation must expend annual qualifying distributions under section 4942(g) of the Code for the direct active conduct of exempt purposes.

Section 4942(g)(1)(A) of the Code and section 53.4942(a)-3(a)(2)(i) of the regulations provide that a "qualifying distribution" is any amount, including that portion of reasonable and necessary administrative expenses, paid to accomplish one or more purposes described in section 170(c)(2)(B) of the Code, other than any contribution to: (i) an organization controlled directly or indirectly by the transferor foundation or one or more disqualified persons with respect to the private foundation, except as provided in section 4942(g)(3) of the Code, or (ii) any private foundation that is not an operating foundation under section 4942(j)(3) of the Code, except as provided in section 4942(g)(3) of the Code. Under section 53.4942-3(a)(2)(i) of the regulations, such qualifying distributions include the reasonable administrative expenses that are incurred in the conduct of exempt purposes under section 170(c)(2)(B) of the Code.

Sections 4942(g)(3)(A) and 4942(g)(3)(B) of the Code require that a transferor private foundation, in order to have a qualifying distribution for its grant to another private foundation, must have adequate records, as required by section 4942(g)(3)(B), to show that the transferee private foundation in fact subsequently made a qualifying distribution that is equal to the amount of the transfer received and that is paid out of the transferee's own corpus within the meaning of section 4942(h) of the Code. That transferee private foundation's qualifying distributions must be expended before the close of the transferee's first tax year after the transferee's tax year in which the transferee received the transfer.

Section 1.507-3(a)(5) of the regulations provides that the recordkeeping requirements of section 4942(b)(3)(B) of the Code will not apply to a transferor private foundation, which has transferred all of its assets pursuant to section 507(b)(2) of the Code, during any period in which such transferor has no assets.

Revenue Ruling 78-387, 1978-2 C. B. 270, describes the carryover of a transferor private foundation's excess qualifying distributions under section 4942(i) of the Code where the transferor and the transferee foundations are controlled by the same persons under section 1.507-3(a)(9)(i) of the regulations. The transferee is treated as the transferor so that the transferee can reduce its own distributable amount under section 4942 of the Code by its share of the transferor foundation's excess qualifying distributions under section 4942(i) of the Code.

Section 4945 of the Code imposes excise tax on any private foundation's making of a taxable expenditure under section 4945(d) of the Code. Section 4945(d)(4)(B) 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(h) of the Code provides that, in order to exercise expenditure responsibility under section 4945(h), the grantor private foundation must: under section 4945(h)(1) see that its grant is spent solely for the grant's purpose; under section 4945(h)(2) obtain complete reports from the grantee foundation on how the funds are spent; and, under section 4945(h)(3) make reports to the Internal Revenue Service with respect to such grants.

Sections 53.4945-6(c)(3) allows a private foundation to transfer its assets to exempt organizations under section 501(c)(3) of the Code pursuant to section 507(b)(2) of the Code, without the transfers being taxable expenditures under section 4945(d) of the Code, provided that any applicable expenditure responsibility under section 4945(h) of the Code is met.

Analysis

1.

P's transfer of all of its assets to X and Y will be for exempt purposes under section 501(c)(3) of the Code. P's transfers will not adversely affect the exemptions of P, X, or Y from federal income tax under section 501(c)(3) of the Code.

2.

Under section 507(b)(2) of the Code and 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 one or more other private foundations pursuant to any reorganization, which includes any significant disposition of 25% or more of the transferor's assets. Because P will be in such a reorganization by its transfers of all of its assets, P's transfers of assets to X and Y will be transfers under section 507(b)(2) of the Code.

3.

Under section 1.507-4(b) of the regulations, P's transfers of assets pursuant to section 507(b)(2) of the Code will not terminate P's private foundation status under section 509(a) of the Code, and will not result in termination tax under section 507(c) of the Code.

4.

Section 507(c) of the Code imposes excise tax on a private foundation which voluntarily terminates its private foundation status pursuant to section 507(a)(1) of the Code. This tax under section 507(c) of the Code is equal to the lower of: (a) the aggregate tax benefits that have resulted from the foundation's exemption from federal income tax under section 501(c)(3) of the Code, or (b) the value of the net assets of the foundation. After P transfers all of its assets to X and Y, the value of P's assets will be zero when P notifies the Internal Revenue Service of its voluntary termination of private foundation status pursuant to section 507(a)(1) of the Code and, thus, such termination of P's private foundation status under section 509(a) of the Code pursuant to a notice under section 507(a)(1) of the Code will result in zero termination tax under section 507(c) of the Code.

5.

P's transfers of assets will be made for exempt purposes to R and to S, which are organizations exempt from federal income tax under section 501(c)(3) of the Code. Under section 53.4946-1(a)(8) of the regulations, because P is exempt from federal income tax under section 501(c)(3) of the Code, P is not a disqualified person as to R or S under section 4946 of the Code for purposes of section 4941 of the Code. Because P's transfers of assets will not be transfers between a disqualified person and a private foundation, P's transfers will not be acts of self-dealing under section 4941 of the Code.

6.

P's assignment to X and Y of its obligations with respect to certain outstanding charitable pledges and the assumption of those obligations by X and Y will not constitute any acts of self-dealing under section 4941 of the Code.

7.

P's transfer of its assets to X and Y will be a transfer to private foundations effectively controlled by the same persons who effectively control P within the meaning of section 1.507-3(a)(9)(i) of the Income Tax Regulations.

8.

Under section 1.507-3(a)(5) of the regulations, after P transfers all its assets, any recordkeeping requirements of section 4942(g)(3)(B) of the Code will not apply to P during any period in which P has no assets.

9.

Section 53.4945-6(c)(3) of the regulations indicates that a private foundation can transfer 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, provided that any expenditure responsibility under section 4945(h) of the Code is met. P's transfer is a transfer of all of its assets that is not subject to the expenditure responsibility requirement under section 4945(h) of the Code, will be made to exempt transferee Y for exempt purposes under section 501(c)(3) of the Code and, thus, will not be a taxable expenditure or result in tax under section 4945 of the Code.

Section 1.507-3(a)(7) of the regulations provides that, if a private foundation transfers all of its assets to one or more transferee private foundations pursuant to section 507(b)(2) of the Code, such transferor foundation does not incur any expenditure responsibility requirement under section 4945(h) of the Code with respect to such transfer of all of its assets pursuant to section 507(b)(2) of the Code. Thus, when P transfers all of its assets to X and Y, pursuant to section 507(b)(2) of the Code, P will not be required to exercise any expenditure responsibility under section 4945(h) of the Code with respect to its transfer of all of its assets to Y pursuant to section 507(b)(2) of the Code.

Accordingly, we rule that:

1. P's transfer of all of its assets to X and Y will not adversely affect the tax-exempt status of P, X, or Y under section 501(c)(3) of the Code.

2. P's transfer of assets to X and Y will not be treated as a transfer to newly created organizations but, instead, will qualify as an "adjustment or reorganization" under section 507(b)(2) of the Code.

3. P's transfer of assets to X and Y will not terminate P's status as a private foundation under section 507(a) of the Code prior to the time that P files notice of its intent to terminate, and as a consequence, P's transfer of assets to X and Y will not result in the imposition of tax under section 507(c) of the Code.

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

5. P's transfer of assets to X and Y will not be an act of self-dealing under section 4941 of the Code.

6. P's assignment to X and Y of its obligations with respect to certain outstanding charitable pledges and the assumption of those obligations by X and Y will not constitute an act of self-dealing under section 4941 of the Code.

7. P's transfer of assets to X and Y will be a transfer to foundations effectively controlled by the same persons who effectively control P within the meaning of section 1.507-3(a)(9)(i) of the Income Tax Regulations.

8. The recordkeeping requirements of section 4942(g)(3)(B) of the Code will not apply to P during any period in which P has no assets.

9. P's transfer of assets to X and Y will not constitute a taxable expenditure under section 4945 of the Code.

Because this rulings letter could help to resolve any questions, please keep it in your permanent records.

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

Sincerely,

/S/

Joseph Chasin
Acting Manager, Exempt Organizations
Technical Group 2