Internal Revenue Service
Index No.: 2522.00-00

Department of the Treasury

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Washington, DC 20044

199911050

Person to Contact:

Telephone Number:

Refer Reply To:
CC:DOM:P&SI:4 - PLR-111894-98
Date: December 17, 1998

Re:

LEGEND:

We received your letter, dated May 28, 1998, requesting rulings concerning the tax consequences of a proposed transfer to Foundation, located in Country. This letter responds to your request regarding the gift tax charitable deduction under § 2522 of the Internal Revenue Code. The other ruling requests will be addressed in a separate letter from the Internal Revenue Service.

The facts and representations submitted are summarized as follows: Donor is a United States citizen. Under the will of Donor's Father, Donor and her three siblings each received a one-fourth portion of Father's estate that included a large collection of b and c century Country paintings. Father had hoped to establish a museum in City, Country for the placement of his art collection. This goal was never achieved during Father's life.

Donor proposes to donate to Foundation a number of paintings that Donor inherited from Father. In addition, Donor proposes to donate to Foundation a sum of cash.

Foundation was formed by Donor's three siblings in Country, in December, 1997. The Foundation intends to exhibit the works of art to a museum that is being constructed by and in City, Country. City is building the museum for the purpose of receiving the works of art to be lent by Foundation to City for the museum's purposes. Under the terms of the agreement entered into by Foundation and City, City will allow the Foundation to participate in decisions with respect to the construction of the museum and the installation and first exhibition of paintings by the museum. The paintings will be contributed in the form of a perpetual loan. The Foundation will have no interest in the museum real estate. The Foundation will contribute to the financial support of the museum.

According to the Articles of Foundation, the purpose of the Foundation is to preserve and to administer a stock of paintings and drawings of the art collection of Father, to treat and to conserve the stock scientifically and educationally and to make the stock accessible to the public through exhibitions and otherwise. Under Section 3, subparagraph (1) of the Articles of the Foundation, the "Foundation is organized and is to be operated exclusively and directly for charitable purposes in accordance with the chapter 'tax-privileged purposes' of the Country Code (of Tax Procedure)." The tax authorities in City have issued a preliminary confirmation of exemption statement to Foundation which states, " the legal entity Foundation, serves exclusively and directly tax exempt charitable purposes in the sense of the applicable Country statutes." The certificate further provides that a final statement on tax exemption can be granted only if the Foundation serves its charitable purpose not only pursuant to the Articles of Foundation but also pursuant to its actual operations. Therefore, upon examination of the Foundation's books with respect to income and expenses at the conclusion of the applicable tax assessment period the Foundation must demonstrate that its actual operations are directed to the exclusive and direct performance of tax exempt purposes. The preliminary statement of exemption has a maximum duration of 18 months from the date of issue.

The following provisions are included in the Articles of the Foundation. Under the Articles of Foundation, Section 5, subparagraph (1), Foundation is required to distribute its income for each taxable year at such time and in such manner as not to become subject to the tax on undistributed income imposed by § 4942. Under subparagraph (2), of Section 5, Foundation is prohibited from engaging in any act of self-dealing as defined in § 4941(d). Under subparagraph (3), Foundation is prohibited from retaining any excess business holdings as defined in § 4943(c). Under subparagraph (4), Foundation may not make any investments in such manner

as to jeopardize the carrying out of the Foundation's charitable purposes, so as to incur tax liability under § 4944. Subparagraph (5) provides that Foundation shall not make any expenditures as defined in § 4945 , including, but not limited to amounts paid or incurred (a) to carry on propaganda or otherwise attempting to influence legislation, or (b) to influence the outcome of any specific public election, or to carry on, directly, or indirectly, any voter registration drive. Under subparagraph (6), no substantial part of the activities of the Foundation shall be the carrying on of propaganda, or otherwise attempting to influence legislation, and the Foundation shall not participate in, or intervene in (including the publishing or distribution of statements) any political campaign on behalf of (or in opposition to) any candidate for public office.

In the case of the termination or liquidation of Foundation, the property of Foundation will be transferred to State, with the requirement that it be used exclusively for charitable purposes in accordance with the Code and the laws of Country and as much as possible in accordance with the Articles of Foundation.

You request a ruling that the Donor's contribution of paintings to Foundation qualifies for the gift tax charitable deduction under § 2522.

Section 2501 provides that a tax is imposed for each calendar year on the transfer of property by gift during such calendar year by any individual, resident or nonresident.

Section 2522(a)(2) provides that in computing taxable gifts for the calendar year, in the case of a citizen or resident, a deduction is allowed in the amount of all gifts made during such year to or for the use of a "foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, including the encouragement of art."

Section 25.2522(a)-1(a)(4) of the Gift Tax Regulations provides that the deduction is not limited to gifts for use within the United States or to gifts to or for the use of domestic corporations, trusts, community chests, funds, foundations, or fraternal societies, orders, or associations operating under the lodge system.

Section 25.2522(a)-1(b) provides that the deduction under § 2522 is not allowed for a transfer to a corporation, trust, community chest, fund, or foundation unless the organization or trust meets the following four tests: (1) it must be organized and operated exclusively for one or more of the specified purposes; (2) it must not be disqualified for tax exemption under § 501(c)(3) by reason of attempting to influence legislation; (3) in the case of gifts made after December 31, 1969, it must not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office; (4) its net earnings must not inure in whole or part to the benefit of private shareholders or individuals other than as legitimate objects of the exempt purposes.

Section 2522(c)(1) provides that no deduction is allowed under § 2522 for a gift to or for the use of an organization or trust described in § 508(d) or § 4948(c)(4) subject to the conditions specified in those sections.

Section 508 provides special rules and requirements with respect to § 501(c)(3) organizations. Section 508(d) provides that no gift made to an organization is allowed as a deduction under § 2522 if the gift is made to a private foundation or trust described in § 4947 in a taxable year for which it fails to meet the requirements of § 508(e) (determined without regard to § 508(e)(2).)

Section 508(e)(1) provides that a private foundation is not exempt from taxation under § 501(a) unless its governing instrument includes provisions the effects of which are:

> (A) to require its income for each taxable year to be distributed at such time and in such manner as not to subject the foundation to tax under § 4942, and (B) to prohibit the foundation from engaging in any act of self-dealing (as defined in § 4941(d)), from retaining any excess business holdings (as defined in § 4943(c), from making any investments in such manner as to subject the foundation to tax under § 4944, and from making any taxable expenditures (as defined in § 4945(d)).

Section 4948(b) provides, however, that § 508 will not apply to any foreign organization which has received substantially all of its support (other than gross investment income) from sources outside the United States.

Section 53.4948-1(b) of the Private Foundation Regulations provides, in part, that § 508 (relating to special rules with respect to § 501(c)(3) organizations) and chapter 42 (other than § 4948) will not apply to any foreign organization which from the date of its creation has received at least 85 percent of its support as defined in § 509(d), other than gross investment income under § 509(d)(4), from sources outside the United States. Section 509(d) provides in part that "support" includes, but is not limited to gifts, grants, contributions, or membership fees.

Section 4948(c)(1) provides that a foreign organization described in § 4948(b) shall not be exempt from taxation under § 501(a) if it has engaged in a prohibited transaction after December 31, 1969.

Section 4948(c)(4) provides that no gift shall be allowed as a deduction under § 2522 if made, (A) to a foreign organization described in § 4948(b) after the date on which the Secretary publishes notice under § 4948(c)(3)(A) that he has notified such organization that it has engaged in a prohibited transaction, and (B) in a taxable year of such organization for which it is not exempt from taxation under § 501(a) by reason of §4948(c)(1).

Based on the information submitted and the representations made, and presuming that Foundation has not been notified by the Secretary that it has engaged in a prohibited transaction within the meaning of § 4948(c)(1), we conclude that the inter vivos gifts by Donor to

Foundation will qualify for the gift tax charitable deduction within the meaning of § 2522(a)(2), provided that Foundation maintains its status in Country as an exempt foundation. Specifically, the gifts to Foundation must neither inure to the benefit of an individual or be used for a noncharitable purposes.

We are specifically not ruling on whether the Foundation's total support, as provided in § 509(d), from sources outside the United States is at least 85%.

Except as ruled above, we express or imply no opinion concerning the federal tax consequences of this transaction under the cited provisions of the Code or any other provision of the Code.

This ruling is directed only to the taxpayer who requested it. Section 6110(j)(3) provides that it may not be used or cited as precedent.

A copy of this letter should be attached to Donor's federal gift tax returns when they are filed. A copy is included for that purpose.

Sincerely yours,

(signed) George L. Masnik

George Masnik
Branch Chief,
Branch 4
Office of the Assistant Chief Counsel
(Passthroughs and Special Industries)

Enclosures:
Copy of this letter
Copy for section 6110 purposes