U.I.L. 501.03-

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

199943045

Date: JUL 27 1999

Contact Person:

ID Number: OP:E:EO:T:1

Telephone Number:

Employer Identification Number:
Key District Office:

Legend:

A =
B =
C =

Dear Sir or Madam:

This is in response to a letter from your authorized representative requesting a series of rulings on your behalf regarding the tax consequences associated with the transactions described below.

A is exempt from federal income tax under section 501(c)(3) of the Code and is classified as a nonprivate foundation under section 509(a)(2) of the Internal Revenue Code. A operates a blood bank which collects, stores and distributes blood products. In addition, A owns or leases improved real estate and maintains an endowment fund.

You have stated that A has proposed a reorganization in which it will transfer its endowment fund to B and its improved real property to C. A will continue to collect, store and distribute blood products.

B and C are being recognized as exempt from federal income tax under section 501(c)(3) of the Code with a nonprivate foundation status under section 509(a)(3) by letter of even date.

You have stated that this reorganization will further your exempt purposes by providing flexible and efficient management, while adding needed expertise in property management and fund raising. The formation of a fund raising/endowment entity is intended to facilitate the attraction of funds and other property from a wider variety of sources to support the charitable programs of A. In addition, you believe separating the different functions into separate corporate entities will make it easier for each entity to account for income, expenses and assets as well to protect the assets of one entity from creditor claims against a different entity.

You have stated that, initially, the boards of directors of A, B and C will be composed of the same individuals and in the future A will retain control over the selection of the boards of directors of B and C.

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You have requested the following rulings in connection with the integration:

1. The proposed reorganization will not adversely affect the tax exempt status of A under section 501(c)(3) of the Code or the nonprivate foundation status of A under section 509(a)(2).

2. The proposed transfer, contribution, or sharing of assets, personnel, facilities, services and the allocation of costs, including the execution of contracts for such sharing of assets and services, in connection with the reorganization between and among A, B and C will not jeopardize the tax exempt status of these entities under section 501(c)(3) of the Code.

3. Subsequent ongoing transfers, contributions, or sharing of assets, personnel, facilities, services and the allocation of costs, including the execution of contracts for such sharing of assets and services, in connection with the reorganization between and among A, B and C shall, to the extent related to the exempt purposes of these entities, not jeopardize the tax exempt status of these entities under section 501(c)(3) of the Code.

4. The proposed transfer, contribution, or sharing of assets, personnel, facilities, services and the allocation of costs, including the execution of contracts for such sharing of assets and services, in connection with the reorganization between and among A, B and C will not, to the extent related to the exempt purposes of these entities, give rise to any unrelated business income tax under sections 511 through 514 of the Code.

5. Subsequent ongoing transfers, contributions, or sharing of assets, personnel, facilities, services and the allocation of costs, including the execution of contracts for such sharing of assets and services, in connection with the reorganization between and among A, B and C will not, to the extent related to the exempt purposes of these entities, give rise to any unrelated business income tax under sections 511 through 514 of the Code.

Section 501(a) of the Code provides an exemption from federal income tax for organizations described in section 501(c)(3), including organizations that are organized and operated exclusively for charitable, educational or scientific purposes.

Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations provides that the term "charitable" is used in section 501(c)(3) of the Code in its generally accepted legal sense.

Revenue Ruling 69-545, 1969-2 C.B. 117, provides that the promotion of health is a charitable purpose within the meaning of section 501(c)(3) of the Code.

Revenue Ruling 67-149, 1967-1 C.B. 133, provides that an organization providing only financial assistance to organizations exempt under section 501(c)(3) of the Code may qualify for exemption under section 501(c)(3).

Revenue Ruling 78-41, 1978-1 C.B. 148, provides that a trust created by an exempt hospital for the sole purpose of accumulating and holding funds to be used to satisfy malpractice claims against the hospital is operated exclusively for charitable purposes and is exempt under section 501(c)(3) of the Code.

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Section 501(c)(3) organizations do not jeopardize their tax exempt status by transferring their assets to other organizations exempt under section 501(c)(3) where the assets transferred are used to further exempt charitable purposes.

Section 1.509(a)-4(f)(1) of the Income Tax Regulations provides that section 509(a)(3)(B) of the Code sets forth three different types of relationships, one of which must be met in order to meet the requirements of that subsection. One of those requirements is "operated, supervised or controlled in connection with." Section 1.509(a)-4(f)(4) of the regulations provides that in the case of supporting organizations which are "supervised or controlled in connection with" one or more publicly supported organizations, the distinguishing feature is the presence of common supervision or control among the governing bodies of all organizations involved, such as the presence of common directors.

Section 511(a) of the Code imposes a tax on the unrelated business income of organizations described in section 501(c).

Section 512(a)(1) of the Code defines unrelated business taxable income as the gross income derived by an organization from any unrelated trade or business regularly carried on by it, less the allowable deductions which are directly connected with the carrying on of the trade or business, with certain modifications.

Section 512(b)(1) of the Code provides, in part, that interest and dividends are excluded from the computation of an exempt organization's unrelated business taxable income.

Section 512(b)(3) of the Code provides that rents from real property (and its incidental related personal property) are not treated as unrelated business income unless the real property is debt-financed under section 514. Debt-financed property does not include any property substantially related to the exercise or performance by such organization of its exempt purposes.

Section 512(b)(4) of the Code provides that notwithstanding paragraphs (1), (2), (3), or (5), in the case of debt-financed property (as defined in section 514), there shall be included, as an item of gross income derived from an unrelated trade or business, the amount ascertained under section 514(a)(1), and there shall be allowed, as a deduction, the amount ascertained under section 514(a)(2).

Section 512(b)(5) of the Code provides that all gains and losses from the sale of property other than inventory or property held for sale to customers are excluded from unrelated business taxable income.

Section 512(b)(13) of the Code provides, in part, that notwithstanding paragraphs (1), (2), or (3), amounts of interest, annuities, royalties, and rents derived from any organization (in this paragraph called the "controlled organization") of which the organization deriving such amounts (in this paragraph called the "controlling organization") has control (as defined in section 368(c)) shall be included as an item of gross income (whether or not the activity from which such amounts are derived represents a trade or business or is regularly carried on).

Section 513(a) of the Code defines unrelated trade or business as any trade or business the conduct of which is not substantially related (aside from the need of the organization for funds or

the use it makes of the profits derived) to the exercise of the organization's exempt purposes or functions.

Section 514(b) of the Code defines debt-financed property as any property which is held to produce income and with respect to which there is an acquisition indebtedness at any time during the taxable year.

Section 1.513-1(d)(2) of the regulations provides, in part, that a trade or business is related to exempt purposes only where the conduct of the business activities has a causal relationship to the achievement of exempt purposes; and it is substantially related for purposes of section 513 of the Code only if the causal relationship is a substantial one. Thus, for the conduct of trade or business from which a particular amount of gross income is derived to be substantially related to purposes for which exemption is granted, the production or distribution of the goods or the performance of the services from which the gross income is derived must contribute importantly to the accomplishment of exempt purposes.

Contributions to organizations exempt from federal income tax under section 501(c)(3) of the Code do not fall within the definition of unrelated business income under section 512, nor create taxable gain or loss to the transferor or transferee.

The proposed transaction will not adversely affect A's exemption under section 501(c)(3) of the Code because A will continue to promote the health of the community by operating a blood bank. A will continue to qualify as a nonprivate foundation because the sources of its financial support will not change. Therefore, it will continue to be an organization described in section 509(a)(2) of the Code.

The proposed transaction will not adversely affect the exempt status of B or C under section 501(c)(3) of the code because their exemption will continue to be based on the fact that, like the organization described in Rev. Rul. 78-41, supra, they are controlled by A and are performing activities that A itself could perform in furtherance of its exempt purpose.

The transfer and sharing of assets, personnel, facilities and services by and among A, B and C, and the allocation of costs connected with these activities, is substantially related to the attainment of the exempt purposes that will be furthered by the reorganization. Therefore, such transactions will not give rise to liability for unrelated business income tax under sections 511 through 514 of the Code.

Accordingly, based on all the facts and circumstances described above, we rule:

1. The proposed reorganization will not adversely affect the tax exempt status of A under section 501(c)(3) of the Code or the nonprivate foundation status of A under section 509(a)(2).

2. The proposed transfer, contribution, or sharing of assets, personnel, facilities, services and the allocation of costs, including the execution of contracts for such sharing of assets and services, in connection with the reorganization between and among A, B and C will not jeopardize the tax exempt status of these entities under section 501(c)(3) of the Code.

3. Subsequent ongoing transfers, contributions, or sharing of assets, personnel, facilities, services and the allocation of costs, including the execution of contracts for such sharing of assets and services, in connection with the reorganization between and among A, B and C shall, to the extent related to the exempt purposes of these entities, not jeopardize the tax exempt status of these entities under section 501(c)(3) of the Code.

4. The proposed transfer, contribution, or sharing of assets, personnel, facilities, services and the allocation of costs, including the execution of contracts for such sharing of assets and services, in connection with the reorganization between and among A, B and C will not, to the extent related to the exempt purposes of these entities, give rise to any unrelated business income tax under sections 511 through 514 of the Code.

5. Subsequent ongoing transfers, contributions, or sharing of assets, personnel, facilities, services and the allocation of costs, including the execution of contracts for such sharing of assets and services, in connection with the reorganization between and among A, B and C will not, to the extent related to the exempt purposes of these entities, give rise to any unrelated business income tax under sections 511 through 514 of the Code.

These rulings are based on the understanding that there will be no material changes in the facts upon which they are based.

These rulings are directed only to the organizations that requested them. Section 6110(j)(3) of the Code provides that they may not be used or cited by others as precedent.

These rulings do not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described.

We are informing your key District Director of this action. Please keep a copy of these rulings in your permanent records.

Sincerely,

Marvin Friedlander

Marvin Friedlander
Chief, Exempt Organizations
Technical Branch 1

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