



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
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Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Legend

<u>B</u>	=
<u>C</u>	=
<u>M</u>	=
<u>Fund</u>	=
<u>S</u>	=
<u>T</u>	=
<u>State</u>	=
<u>Date 1</u>	=
<u>Date 2</u>	=
<u>Date 3</u>	=
<u>x</u>	=

Dear :

This responds to your letter in which you request rulings on the application of Part II of Subchapter F of Chapter 1, Subtitle A (IRC §§ 507-509) and Subchapter A of Chapter 42, Subtitle D (§§ 4940-4948) to the transaction described below

Facts

You and the Fund are two philanthropic entities maintained by the family of B. B was involved in many philanthropic projects during his lifetime, a legacy which B's lineal descendants and their families (the "B Family") have adopted and continue. You are a State nonprofit corporation that has been determined by the Internal Revenue Service (the "Service") to be exempt from

federal income tax as an organization described in § 501(c)(3) and to be classified as a private foundation under § 509(a). You have 19 members, all of whom are lineal descendants of B. You have ten Trustees, each of whom is either a lineal descendant of B or a spouse of such lineal descendant.

The Fund was created under, and is governed by, State law. The Fund is a charitable trust that is not exempt from taxation under § 501(a), but that, pursuant to § 4947(a)(1), is treated as an organization described in § 501(c)(3) for purposes of §§ 507 through 509 and for purposes of Chapter 42 (§ 4940 *et seq.*). Currently, the two Trustees of the Fund are C (a member of the B Family and a member of your Board of Trustees) and M. The Fund's Trust Agreement provides, in part, that the income and principal of the Fund are to be used solely and exclusively for certain enumerated charitable purposes, and that those purposes are to be carried on, in whole or in substantial part, within the state of State.

The Trust Agreement provides that the Trustees of the Fund shall use the trust assets, and the income therefrom, or make available to others for the specified charitable purposes, such amounts of income from or principal of the Fund as they shall be directed by a Distribution Committee of four persons to be appointed annually, two by you and two by the trustee(s) of the Fund. All of the members of the Distribution Committee are lineal descendants of B.

As of Date 1, the Fund had an excess qualifying distribution carryover (within the meaning of § 4942(i) and § 53.4942(a)-3(e)) of approximately \$x.

You and the Fund have determined that the charitable objectives of both would be better served by combining the two entities, and that the Fund should transfer its assets to you in the transaction described below (the "Transaction"). The business objectives of the Transaction are:

- i. To establish for current and future B Family members a uniform governance structure to coordinate oversight and decision making over charitable grant making activities of the Fund and you;
- ii. To define the portion of the assets of the Fund to be permanently restricted for charitable purposes that are carried on within State as permitted by State law;
- iii. To improve access to investment opportunities, achieve greater diversification, and coordinate the investment policy and process to monitor investment results for the combined assets of the Fund and you; and
- iv. To achieve operational efficiencies for tax reporting, accounting, grant applications and grant making, and coordination of staff activities.

To implement the Transaction, you and the Fund have entered into an Agreement of Transfer dated Date 2 to provide for the transfer of all of the assets of the Fund to you. Pursuant to this Agreement, the transfer of the Fund's assets to you is conditioned upon the satisfaction of the following three Transfer Conditions:

- i. That you shall have amended your Articles of Incorporation to clarify that you are legally permitted to use the assets that the Fund intends to transfer to you for the charitable purposes set out in the Trust Agreement;

- ii. That you shall have amended your Code of Regulations to provide for two separate distribution committees to advise your Board of Trustees concerning the use of the assets to be transferred by the Fund to you; and
- iii. That you shall have received a ruling from the Service with respect to the Transaction to the effect that you will be treated under § 507(b)(2) and § 1.507-3(a)(9)(i) as the continuation of the Fund for purposes of Chapter 42 of the Code and §§ 507-509.

Under the Agreement of Transfer, you are obligated to provide written notice to the Fund of the completion of the Transfer Conditions (the "Notice of Completion").

The Agreement of Transfer provides that, upon the later of Date 3 or your delivery to the Fund of the Notice of Completion (the "Effective Time of Transfer"), the Fund will transfer all of its assets (the "Transferred Assets") to you, and you shall assume all of the obligations (the "Continuing Obligations") of the Fund, which shall include, but not be limited to, any outstanding pledge, commitment, or other obligation arising as the result of an authorized act of the Fund, including, but not limited to, fees payable to the Trustees of the Fund.

Pursuant to the Agreement of Transfer, you agree to indemnify, defend, and hold harmless each of C and M, in their respective capacity as a Trustee of the Fund, to the greatest extent permitted by applicable law (including, but not limited to, Chapter 42 of the Code and the Treasury Regulations promulgated thereunder), from and against all expenses, including reasonable attorney's fees, judgments, and amounts paid in settlement that are actually and reasonably incurred by the indemnified party that arise out of, or are attributable to, the execution or the performance of the Agreement (the "Indemnification Obligations").

Your obligation to satisfy the Continuing Obligations and the Indemnification Obligations shall not exceed, in the aggregate, the sum of the value of the Transferred Assets at the Effective Time of Transfer, less the value of any Transferred Assets that are transferred to the Fund after the Effective Time of Transfer, and less any costs, fees (including reasonable attorneys' fees), and expenses incurred by you which are directly attributable to the Continuing Obligations or the Indemnification Obligations, provided that your obligation to satisfy an Indemnification Obligation at any time, and from time to time, shall be subordinate to your obligations to satisfy the Continuing Obligations that are known or may be reasonably estimated at such time.

The Agreement of Transfer further provides that, subject to any Continuing Obligation, you shall account for the Transferred Assets as two separate funds, initially equal in value, to be known as S and T. The charitable purposes of the Fund, and the amendments to your Articles of Incorporation and Code of Regulations shall constitute permanent restrictions on the use and governance of S and T. In addition, S will be permanently restricted to charitable purposes that are carried on within State. However, these permanent restrictions shall not require you to maintain the Transferred Assets as an endowment fund under State law, and you shall be free to use as much or all of the income and principal of S or T, subject to the restrictions stated in the Agreement of Transfer, as you shall determine.

Pursuant to the Agreement of Transfer, within ten days after the Effective Time of Transfer, you and the Fund shall provide written notice to the State Attorney General that the Fund has transferred the Transferred Assets to you. The Agreement of Transfer provides that you will not

distribute funds from I for charitable purposes that are carried on outside of State until the earlier of (i) receipt by the Fund and you of a written approval of the terms of the Agreement of Transfer from the State Attorney General, or (ii) in the absence of such approval, then the latter of (A) the expiration of such two-year (or extended) period provided above, or (B) if a proceeding is filed by the State Attorney General with respect to the Transaction prior to the expiration of such period, then the date of the final resolution of such proceeding by written agreement of you and the Fund and the State Attorney General or a non-appealable order of a State court pursuant to a proceeding initiated by the State Attorney General (the "Review Period").

The Agreement of Transfer also provides that the Fund shall provide the Service with written notice of intent to terminate its status as a private foundation promptly after the expiration of the Review Period unless otherwise provided by the written agreement of the Fund, you, and the State Attorney General or an order of court pursuant to an action initiated by the State Attorney General during the Review Period.

In the Agreement of Transfer, the Fund has represented to you that there is no grant made by the Fund for which you will be required to exercise expenditure responsibility under § 4945.

Finally, you represent that, as of the date of the Agreement of Transfer, and at the Effective Time of Transfer:

- a. All of your members and all of the members of your Board of Trustees are, and will be, members of the B Family; one of the Trustees of the Fund is, and will be, a member of the B Family and a member of your Board of Trustees; and all of the members of the Fund's Distribution Committee are, and will be, members of the B Family, members of yours, and members of your Board of Trustees.
- b. The Fund and you are, and will be, effectively controlled (within the meaning of §§ 1.507-3(a)(9)(i) and 1.482-1A(a)(3)), directly or indirectly by the same persons.

#### Rulings Requested

You have requested the following rulings:

1. The transfer of the assets of the Fund to you in the Transaction will constitute a significant disposition of assets to a private foundation as described in § 1.507-3(c), and will constitute a transfer of assets by a private foundation to another private foundation described in § 507(b)(2).
2. The transfer of the assets of the Fund to you in the Transaction will not result in the termination of the Fund's treatment as a private foundation and will not result in the Fund being subject to the tax imposed by § 507(c).
3. Pursuant to § 507(b)(2), you will not be treated as a newly-created organization.
4. You will succeed to all of the tax attributes and characteristics of the Fund described in §

1.507-3(a)(2), (3), and (4).

5. Assuming that the Fund and you are effectively controlled (within the meaning of § 1.482-1A(a)(3)), directly or indirectly, by the same persons, you will be treated as if you were the Fund for purposes of Chapter 42 and §§ 507 through 509.
6. Pursuant to § 1.507-3(a)(9)(i) and Rev. Rul. 78-387, you may reduce the amount of your required distributions under § 4942 by the amount of the Fund's excess qualifying distribution carryover.
7. The transfer of the assets of the Fund to you in the Transaction will not give rise to any net investment income under § 4940.
8. The transfer of the assets of the Fund to you in the Transaction will not constitute an act of self-dealing under § 4941 by the Fund, you, or any foundation managers (as defined in § 4946(b)) of you or the Fund.
9. The transfer of the assets of the Fund to you in the Transaction will not constitute a jeopardizing investment within the meaning of § 4944.
10. The transfer of the assets of the Fund to you in the Transaction will not constitute a taxable expenditure under § 4945, and the Fund will not be required to exercise any expenditure responsibility under § 4945(h) with respect to any assets transferred by the Fund to you.
11. Any transfer of your assets to a Trustee of the Fund in satisfaction of the Indemnification Obligations will not constitute an act of self-dealing under § 4941 or a taxable expenditure under § 4945.

#### Law

I.R.C. § 501(a) exempts from taxation under subtitle A an organization described in subsection (c).

I.R.C. § 501(c)(3) describes organizations that are organized and operated exclusively for charitable and other specified exempt purposes.

I.R.C. § 507(a) provides that, except as provided in subsection (b), the status of any organization as a private foundation shall be terminated only if: (1) it notifies the Secretary of its intent to accomplish such termination, or (2) with respect to such organization, there have been either willful repeated acts (or failures to act), or a willful and flagrant act (or failure to act), giving rise to liability for tax under Chapter 42, and the Secretary notifies such organization that it is liable for the tax imposed by subsection (c), and either such organization pays the tax (or any portion not abated under subsection (g)) or the entire amount of such tax is abated under subsection (g).

I.R.C. § 507(b)(2) provides that in the case of a transfer of assets of any private foundation to

another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization or reorganization, the transferee foundation shall not be treated as a newly created organization.

I.R.C. § 507(c) imposes a tax on each terminating private foundation equal to the lesser of the aggregate tax benefit resulting from the § 501(c)(3) status of such foundation and the value of the net assets of such foundation.

I.R.C. § 509(a) provides that the term "private foundation" means a domestic or foreign organization described in § 501(c)(3) other than an organization described in paragraphs (1) through (4).

I.R.C. § 4940(a) imposes on each private foundation which is exempt from taxation under § 501(a) for the taxable year, with respect to the carrying on of its activities, a tax equal to two percent of the net investment income of the foundation for the taxable year.

I.R.C. § 4940(b) imposes on each private foundation which is not exempt from taxation under § 501(a) for the taxable year, with respect to the carrying on of its activities, a tax equal to—  
 (1) the amount (if any) by which the sum of (A) the tax imposed under subsection (a) (computed as if such subsection applied to such private foundation for the taxable year), plus (B) the amount of the tax which would have been imposed under section 511 for the taxable year if such private foundation had been exempt from taxation under § 501(a), exceeds  
 (2) the tax imposed under subtitle A on such private foundation for the taxable year.

I.R.C. § 4941(a)(1) imposes a tax on each act of self-dealing between a disqualified person and a private foundation.

I.R.C. § 4941(d)(1)(A) provides that the term "self-dealing" means any direct or indirect sale or exchange, or leasing, of property between a private foundation and a disqualified person.

I.R.C. § 4941(d)(1)(E) provides that the term "self-dealing" means any direct or indirect transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a private foundation.

I.R.C. § 4941(d)(2)(A) provides that the transfer of real or personal property by a disqualified person to a private foundation shall be treated as a sale or exchange if the property is subject to a mortgage or similar lien which the foundation assumes or if it is subject to a mortgage or similar lien which a disqualified person placed on the property within the 10-year period ending on the date of the transfer.

I.R.C. § 4942(a) imposes a tax on the "undistributed income" of a private foundation for any taxable year which has not been distributed before the first day of the second (or any succeeding) taxable year following such taxable year.

I.R.C. § 4942(c) provides that the term "undistributed income" means, with respect to any private foundation for any taxable year as of any time, the amount by which the distributable

amount for such taxable year exceeds the qualifying distributions made before such time out of such distributable amount.

I.R.C. § 4942(g)(1)(A) provides that the term "qualifying distribution" means any amount (including that portion of reasonable and necessary administrative expenses) paid to accomplish one or more purposes described in § 170(c)(2)(B), other than any contribution to: (i) an organization controlled (directly or indirectly) by the foundation or disqualified persons with respect to the foundation, except as provided in paragraph (3), or (ii) a private foundation which is not an operating foundation (as described in subsection (j)(3)), except as provided in paragraph (3).

I.R.C. § 4942(g)(3) provides that the term "qualifying distribution" includes a contribution to a § 501(c)(3) organization described in paragraph (1)(A)(i) or (ii) if—

- (A) not later than the close of the first taxable year after its taxable year in which such contribution is received, such organization makes a distribution equal to the amount of such contribution and such distribution is a qualifying distribution (within the meaning of paragraph (1) or (2), without regard to this paragraph) which is treated under subsection (h) as a distribution out of corpus (or would be so treated if such § 501(c)(3) organization were a private foundation which is not an operating foundation), and
- (B) the private foundation making the contribution obtains adequate records or other sufficient evidence from such organization showing that the qualifying distribution described in subparagraph (A) has been made by such organization.

I.R.C. § 4942(i)(1) provides that if, for the taxable years in the adjustment period for which an organization is a private foundation—

- (A) the aggregate qualifying distributions treated (under subsection (h)) as made out of the undistributed income for such taxable year or as made out of corpus (except to the extent subsection (g)(3) with respect to the recipient private foundation or § 170(b)(1)(D)(ii) applies) during such taxable years, exceed
- (B) the distributable amounts for such taxable years (determined without regard to this subsection),

then, for purposes of this section (other than subsection (h)), the distributable amount for the taxable year shall be reduced by an amount equal to such excess.

I.R.C. § 4942(i)(2) provides that, for purposes of paragraph (1), with respect to any taxable year of a private foundation, the taxable years in the adjustment period are the taxable years (not exceeding five) preceding the taxable year.

I.R.C. § 4944(a)(1) imposes a tax on any amount invested by a private foundation in a manner that jeopardizes the carrying out of any of the foundation's charitable purposes.

I.R.C. § 4945(a) imposes a tax on each taxable expenditure of a private foundation (as defined in subsection (d)).

I.R.C. § 4945(d)(4) provides that the term "taxable expenditure" includes any amount paid or incurred by a private foundation as a grant to a private non-operating foundation unless the grantor foundation exercises expenditure responsibility with respect to such grant in accordance

with subsection (h).

I.R.C. § 4945(d)(5) provides that the term “taxable expenditure” includes any amount paid or incurred by a private foundation for any purpose other than one specified in § 170(c)(2)(B).

I.R.C. § 4945(h) provides that the expenditure responsibility referred to in subsection (d)(4) means that the private foundation is responsible to exert all reasonable efforts to establish adequate procedures: (1) to see that the grant is spent solely for the purpose for which made, (2) to obtain full and complete reports from the grantee on how the funds are spent, and (3) to make full and detailed reports with respect to such expenditures to the Secretary.

I.R.C. § 4946(a)(1)(B) provides that for purposes of subchapter A of Chapter 42 (§§ 4940 through 4948), the term “disqualified person” means, with respect to a private foundation, a person who is a foundation manager within the meaning of subsection (b)(1).

I.R.C. § 4946(b)(1) provides that the term “foundation manager” means, with respect to any private foundation, an officer, director, or trustee of a foundation (or an individual having powers or responsibilities similar to those of officers, directors, or trustees of the foundation).

I.R.C. § 4947(a)(1) provides that for purposes of part II of subchapter F of chapter 1 (other than § 508(a), (b), and (c)) and for purposes of Chapter 42, a trust which is not exempt from taxation under § 501(a), all of the unexpired interests in which are devoted to one or more of the purposes described in § 170(c)(2)(B), and for which a deduction was allowed under § 170, 545(b)(2), 642(c), 2055, 2106(a)(2), or 2522 (or the corresponding provisions of prior law) shall be treated as an organization described in § 501(c)(3).

Treas. Reg. § 1.482-1A(a)(3) provides that the term “controlled” includes any kind of control, direct or indirect, whether legally enforceable, and however exercisable or exercised. It is the reality of the control which is decisive, not its form or the mode of its exercise.

Treas. Reg. § 1.507-1(b)(1) provides that in order to terminate its private foundation status under § 507(a)(1), an organization must submit a statement to the Service of its intent to terminate its private foundation status under § 507(a)(1). Such statement must set forth in detail the computation and amount of tax imposed under § 507(c). Unless the organization requests abatement of such tax pursuant to § 507(g), full payment of such tax must be made at the time the statement is filed under § 507(a)(1).

Treas. Reg. § 1.507-1(b)(6) provides that if a private foundation transfers all or part of its assets to one or more other private foundations pursuant to a transfer described in § 507(b)(2) and § 1.507-3(c), such transferor foundation will not have terminated its private foundation status under § 507(a)(1).

Treas. Reg. § 1.507-1(b)(7) provides that neither a transfer of all the assets of a private foundation nor a significant disposition of assets (as defined in § 1.507-3(c)(2) by a private foundation shall be deemed to result in a termination of the transferor private foundation under § 507(a) unless the transferor private foundation elects to terminate pursuant to § 507(a)(1) or § 507(a)(2) is applicable.



Treas. Reg. § 1.507-3(a)(1) provides that in the case of a transfer of assets of any private foundation to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization, or reorganization, including a significant disposition of assets to one or more private foundations within the meaning of paragraph (c), the transferee organization shall not be treated as a newly created organization. Rather, the transferee organization shall be treated as possessing those attributes and characteristics of the transferor organization which are described in subparagraphs (2), (3), and (4) of this paragraph.

Treas. Reg. § 1.507-3(a)(2)(i) provides that a transferee organization to which this paragraph (a) applies shall succeed to the aggregate tax benefit of the transferor organization in an amount equal to the amount of such aggregate tax benefit multiplied by a fraction the numerator of which is the fair market value of the assets (less encumbrances) transferred to such transferee and the denominator of which is the fair market value of the assets of the transferor (less encumbrances) immediately before the transfer. Fair market value shall be determined as of the time of the transfer.

Treas. Reg. § 1.507-3(a)(3) provides that, for purposes of § 507(d)(2), in the event of a transfer of assets described in § 507(b)(2), any person who is a "substantial contributor" (within the meaning of § 507(d)(2)) with respect to the transferor foundation shall be treated as a "substantial contributor" with respect to the transferee foundation, regardless of whether such person meets the \$5,000-two percent test with respect to the transferee organization at any time.

Treas. Reg. § 1.507-3(a)(4) provides that if a private foundation incurs liability for one or more of the taxes imposed under Chapter 42 (or any penalty resulting therefrom) prior to, or as a result of, making a transfer of assets described in § 507(b)(2) to one or more private foundations, in any case where transferee liability applies each transferee foundation shall be treated as receiving the transferred assets subject to such liability to the extent that the transferor foundation does not satisfy such liability.

Treas. Reg. § 1.507-3(a)(5) provides that, except as provided in subparagraph (9) of this paragraph, a private foundation is required to meet the distribution requirements of § 4942 for any taxable year in which it makes a § 507(b)(2) transfer of all or part of its net assets to another private foundation. Such transfer shall itself be counted toward satisfaction of such requirements to the extent the amount transferred meets the requirements of § 4942(g). However, where the transferor has disposed of all of its assets, the recordkeeping requirements of § 4942(g)(3)(B) shall not apply during any period in which it has no assets. Such requirements are applicable for any taxable year other than a taxable year during which the transferor has no assets.

Treas. Reg. § 1.507-3(a)(9)(i) provides that if a private foundation transfers all of its net assets to one or more private foundations that are effectively controlled (within the meaning of § 1.482-1A(a)(3)), directly or indirectly, by the same person or persons that effectively controlled the transferor private foundation, for purposes of Chapter 42 (§ 4940 *et seq.*) and part II of subchapter F of chapter 1 of the Code (§§ 507 through 509), such a transferee private foundation shall be treated as if it were the transferor.

Treas. Reg. § 1.507-3(c)(1) provides that a transfer of assets is described in § 507(b)(2) if it is made by a private foundation to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization, or reorganization. For purposes of § 507(b)(2), the terms "other adjustment, organization or reorganization" shall include any partial liquidation or any other significant disposition of assets to one or more private foundations, other than transfers for full and adequate consideration or distributions out of current income.

Treas. Reg. § 1.507-3(c)(2) provides that the term "significant disposition of assets to one or more private foundations" includes any disposition (or series of related dispositions) by a private foundation to one or more private foundations of 25 percent or more of the fair market value of the net assets of the transferor foundation at the beginning of the taxable year in which the transfers occur.

Treas. Reg. § 1.507-3(d) provides that unless a private foundation voluntarily gives notice pursuant to § 507(a)(1), a transfer of assets described in § 507(b)(2) will not constitute a termination of the transferor's private foundation status under § 507(a)(1).

Treas. Reg. § 1.507-4(b) provides that private foundations which make transfers described in § 507(b)(2) are not subject to the tax imposed under § 507(c) with respect to such transfers unless the provisions of § 507(a) become applicable.

Treas. Reg. § 53.4940-1(b)(1) provides that the excise tax imposed under § 4940 on private foundations which are not exempt from taxation under § 501(a) is equal to:

- (i) The amount (if any) by which the sum of
  - (A) The tax on net investment income imposed under § 4940(a), computed as if such private foundation were exempt from taxation under section 501(a) and described in § 501(c)(3) for the taxable year, plus
  - (B) The amount of the tax which would have been imposed under section 511 for such taxable year if such private foundation had been exempt from taxation under § 501(a), exceeds,
- (ii) The tax imposed under subtitle A on such private foundation for the taxable year.

Treas. Reg. § 53.4941(d)-2(a)(2) provides that a "mortgage or similar lien" shall include, but is not limited to, deeds of trust and vendor's liens, but shall not include any other lien if such lien is insignificant in relation to the fair market value of the property transferred.

Treas. Reg. § 53.4941(d)-2(f)(1) provides that the transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a private foundation shall constitute an act of self-dealing. If a private foundation makes a grant or other payment which satisfies the legal obligation of a disqualified person, such grant or payment shall ordinarily constitute an act of self-dealing.

Treas. Reg. § 53.4941(d)-3(c)(1) provides, generally, that, under § 4941(d)(2)(E), the payment of compensation (and the payment or reimbursement of expenses, including reasonable advances for expenses anticipated in the immediate future) by a private foundation to a

disqualified person for the performance of personal services which are reasonable and necessary to carry out the exempt purpose of the private foundation shall not be an act of self-dealing if such compensation (or payment or reimbursement) is not excessive. For the determination of whether compensation is excessive, see § 1.162-7.

Treas. Reg. § 53.4942(a)-3(e)(1) provides that if in any taxable year for which an organization is subject to the initial excise tax imposed by § 4942(a) there is created an excess of qualifying distributions (as determined under subparagraph (2) of this paragraph), such excess may be used to reduce distributable amounts in any taxable year of the adjustment period (as defined in subparagraph (3) of this paragraph).

Treas. Reg. § 53.4942(a)-3(e)(2) provides, generally, that an excess of qualifying distributions is created if (i) the total qualifying distributions treated as made out of the undistributed income for such taxable year or as made out of corpus with respect to such taxable year exceeds (ii) the distributable amount for such taxable year.

Treas. Reg. § 53.4942(a)-3(e)(3) provides that the taxable years of the adjustment period are the five taxable years immediately following the taxable year in which the excess of qualifying distributions is created.

Treas. Reg. § 53.4945-6(b) provides that reasonable expenses to carry out charitable purposes ordinarily will not be treated as taxable expenditures.

Treas. Reg. § 53.4946-1(a)(8) provides that, for purposes of § 4941 only, the term "disqualified person" shall not include any organization which is described in § 501(c)(3) (other than an organization described in § 509(a)(4)).

Treas. Reg. § 53.4947-1(a) provides that § 4947 subjects trusts which are not exempt from taxation under § 501(a), all or part of the unexpired interests in which are devoted to one or more of the purposes described in § 170(c)(2)(B), and which have amounts in trust for which a deduction was allowed under § 170, 545(b)(2), 556(b)(2), 642(c), 2055, 2106(a)(2), or 2522 to the same requirements and restrictions as are imposed on private foundations. The basic purpose of § 4947 is to prevent these trusts from being used to avoid the requirements and restrictions applicable to private foundations.

Treas. Reg. § 53.4947-1(b)(1) provides that a "charitable trust", within the meaning of § 4947(a)(1), is a trust which is not exempt from taxation under § 501(a), all of the unexpired interests in which are devoted to one or more of the purposes described in § 170(c)(2)(B), and for which a deduction was allowed under § 170, 545(b)(2), 556(b)(2), 642(c), 2055, 2106(a)(2), or 2522. A charitable trust (as defined in this paragraph) shall be treated as an organization described in § 501(c)(3) and, if it is determined under § 509 that the trust is a private foundation, then Part II of Subchapter F of Chapter 1 of the Code (other than § 508(a), (b), and (c)) and Chapter 42 shall apply to the trust. However, the charitable trust is not treated as an organization described in § 501(c)(3) for purposes of exemption from taxation under § 501(a). Thus, the trust is subject to the excise tax on its investment income under § 4940(b) rather than the tax imposed by § 4940(a).

Rev. Rul. 78-387, 1978-2 C.B. 270, concerns a private foundation, M, that has a carryover of excess qualifying distributions as described in § 4942(i) and § 53.4942(a)-3(e). M transfers all of its net assets to private foundation N in a transfer qualifying under § 507(b)(2). M is controlled (within the meaning of § 1.482-1A(a)(3)) by the same persons who control N. Because M and N are controlled by the same persons, N is treated as if it were M pursuant to § 1.507-3(a)(9)(i). Accordingly, for purposes of determining N's distribution requirements under § 4942, it is held that N may reduce its distributable amount by the excess qualifying distributions carryover of M.

Rev. Rul. 2002-28, 2002-1 C.B. 941, holds:

- When a private foundation transfers all of its assets to one or more private foundations in a transfer described in § 507(b)(2), the transfers do not give rise to net investment income and are not subject to tax under § 4940(a). The transferee foundations may use their proportionate share of any excess § 4940 tax paid by the transferor to offset the transferees' § 4940 tax liability.
- When a private foundation transfers all of its assets to one or more private foundations in a transfer described in § 507(b)(2), the transfers do not constitute qualifying distributions of the transferor foundation under § 4942. The transferee foundations assume their proportionate share of the transferor foundation's undistributed income under § 4942 and reduce their own distributable amount for purposes of § 4942 by their proportionate share of the transferor's excess qualifying distributions under § 4942(i).
- When a private foundation transfers all of its assets to one or more private foundations in a transfer described in § 507(b)(2), the transfers do not constitute investments for purposes of § 4944 and, consequently, do not constitute investments jeopardizing the transferor foundation's exempt purposes and are not subject to tax under § 4944(a)(1).
- When a private foundation transfers all of its assets to one or more private foundations effectively controlled by the same persons that effectively control the transferor, the transferee foundation is treated as the transferor foundation rather than as a recipient of an expenditure responsibility grant. Therefore, there are no expenditure responsibility requirements that must be exercised under § 4945(d)(4) or (h) with respect to the transfers to the transferee foundation. The transferor foundation is required to exercise expenditure responsibility over the transferor's outstanding grants until it disposes of all of its assets. Thereafter, during any period in which the transferor foundation has no assets, the transferor foundation is not required to exercise expenditure responsibility over any outstanding grants. However, the transferor foundation must still meet the § 4945(h) reporting requirements for the outstanding grants for the year in which the transfer was made.

### Analysis

#### Issue 1

*Whether the transfer of assets of the Fund to you in the Transaction will constitute a significant disposition of assets to a private foundation as described in § 1.507-3(c), and will constitute a transfer of assets by a private foundation to another private foundation described in § 507(b)(2).*

By reason of § 4947(a)(1) and § 53.4947-1(b)(1), the Fund is treated as an organization described in § 501(c)(3) for purposes of §§ 507 and 509. As determined under § 509, the Fund is a private foundation. Consequently, Part II of Subchapter F of Chapter 1 of the Code (other than § 508(a), (b), and (c)), and Chapter 42 shall apply to the Fund, including the provisions of § 507.

I.R.C. § 507(b)(2) applies to the transfer of the assets of any private foundation to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization, or reorganization. Treas. Reg. § 1.507-3(c)(1) provides that the terms "other adjustment, organization, or reorganization" shall include any partial liquidation or any other significant disposition of assets to one or more private foundations, other than transfers for full and adequate consideration or distributions out of current income. The term "significant disposition of assets to one or more private foundations" is defined by § 1.507-3(c)(2) as any disposition or series of dispositions where the aggregate value transferred is 25 percent or more of the fair market value of the net assets of the foundation at the beginning of the taxable year.

The Transaction will result in the Fund transferring 100 percent of its assets to you, a private foundation, for no consideration. Hence, the Transfer is a significant disposition of assets that qualifies as a transfer described in § 507(b)(2).

## Issue 2

*Whether the transfer of the assets of the Fund to you in the Transaction would result in the termination of the Fund's treatment as a private foundation or would result in the Fund being subject to the tax imposed by § 507(c).*

Treas. Reg. § 1.507-1(b)(1) provides that in order for a private foundation to terminate its private foundation status under § 507(a)(1), it must submit a statement to the Service of its intent to terminate its private foundation status under § 507(a)(1). Treas. Reg. § 1.507-1(b)(6) provides that when a private foundation transfers all or part of its assets to one or more other private foundations pursuant to a transfer described in § 507(b)(2), such transferor foundation will not have terminated its private foundation status under § 507(a)(1). In addition, § 1.507-1(b)(7) provides that neither a transfer of all the assets of a private foundation nor a significant disposition of assets by a private foundation shall be deemed to result in a termination of the transferor private foundation under § 507(a) unless the transferor private foundation elects to terminate pursuant to § 507(a)(1). Furthermore, § 1.507-3(d) provides that unless a private foundation voluntarily gives notice pursuant to § 507(a)(1), a transfer of assets described in § 507(b)(2) will not constitute termination of the transferor's private foundation status under § 507(a)(1). Finally, § 1.507-4(b) provides that a private foundation that makes a transfer described in § 507(b)(2) is not subject to the tax imposed under § 507(c) with respect to such transfer unless the provisions of § 507(a) become applicable.

As explained under Issue 1, above, the Transfer will constitute a significant disposition of assets described in § 507(b)(2). The Fund will not provide the Service with written notice of intent to terminate its status as a private foundation until the expiration of the Review Period described in the Agreement of Transfer which is after the Effective Time of Transfer. Therefore, the Transfer would not terminate the Fund's private foundation status under § 507(a) or subject the Fund to

the tax imposed under § 507(c).

#### Issues 3 and 4

*Whether, pursuant to § 507(b)(2), you will not be treated as a newly-created organization.*

*Whether you will succeed to the all of the tax attributes and characteristics of the Fund described in § 1.507-3(a)(2), (3), and (4).*

When a private foundation makes a transfer described in § 507(b)(2), the transferee foundation is not treated as a newly created organization under § 1.507-3(a)(1). Since the Transfer is a transfer described in § 507(b)(2), you will not be treated as a newly created organization.

In the case of a significant disposition of assets from one or more private foundations within the meaning of § 507(b)(2), the transferee organization shall be treated as possessing those attributes and characteristics of the transferor organization which are described in subparagraphs (2), (3), and (4) of § 1.507-3(a). Accordingly, you will be treated as possessing those attributes and characteristics of the Fund that are described in § 1.507-3(a)(2), (3), and (4).

#### Issue 5

*Assuming the Fund and you are effectively controlled (within the meaning of § 1.482-1A(a)(3)), directly or indirectly, by the same persons, whether you will be treated as if you were the Fund for purposes of Chapter 42 and §§ 507-509.*

Treas. Reg. § 1.507-3(a)(9)(i) provides that if a private foundation transfers all of its net assets to one or more private foundations which are effectively controlled (within the meaning of § 1.482-1A(a)(3)), directly or indirectly, by the same person or persons which effectively controlled the transferor private foundation, for purposes of Chapter 42 (§ 4940 *et seq.*) and §§ 507 through 509, such a transferee private foundation shall be treated as if it were the transferor. You represent that at the Effective Time of Transfer the Fund and you will be effectively controlled (within the meaning of § 1.482-1A(a)(3)), directly or indirectly, by the same persons. Therefore, after the Transfer, you will be treated as if you were the Fund for purposes of Chapter 42 and §§ 507 through 509.

#### Issue 6

*Whether, pursuant to § 1.507-3(a)(9)(i), you may reduce the amount of your required distributions under § 4942 by the amount of the Fund's excess qualifying distribution carryover.*

I.R.C. § 4942(a) generally imposes a tax on the undistributed income of a private foundation for any taxable year which has not been distributed before the first day of the second (or any succeeding) taxable year following such taxable year. I.R.C. § 4942(c) defines "undistributed income" for any taxable year as the amount by which the distributable amount for such taxable year exceeds the qualifying distributions made out of such distributable amount for such taxable year. I.R.C. § 4942(g)(1)(A) defines "qualifying distribution" generally as any amount (including

that portion of reasonable and necessary administrative expenses) paid to accomplish one or more purposes described in § 170(c)(2)(B), but a qualifying distribution does not include a contribution to an organization controlled directly or indirectly by the foundation or by one or more disqualified persons with respect to the foundation.

Treas. Reg. § 1.507-3(a)(5) provides that, except as provided in § 1.507-3(a)(9), a private foundation making a transfer described in § 507(b)(2) must satisfy its distribution requirements under § 4942 for the taxable year in which the transfer is made. It further provides that the transfer will count as a distribution in satisfaction of the transferor foundation's distribution requirement under § 4942 subject to the provisions of § 4942(g). I.R.C. § 4942(g) provides that a distribution from one private foundation to another private foundation, where both foundations are effectively controlled by the same persons, will not be treated as a qualifying distribution of the transferor foundation for purposes of § 4942 except to the extent that the transferee foundation makes one or more distributions that would be qualifying distributions under § 4942(g) prior to the close of the transferee's first tax year following the tax year in which it received the transfer and the distributions are treated as being made out of corpus.

Rev. Rul. 78-387 and Rev. Rul. 2002-28 hold that where, by reason of § 1.507-3(a)(9)(i), a transferee private foundation is treated as though it were the transferor for purposes of § 4942, a transfer to the transferee foundation is not treated as a qualifying distribution of the transferor foundation. Rather, the transferee foundation assumes all obligations with respect to the transferor's "undistributed income" within the meaning of § 4942(c), if any, and reduces its own distributable amount under § 4942(d) by the transferor foundation's excess qualifying distributions under § 4942(i).

As explained under Issue 5, above, by reason of § 1.507-3(a)(9)(i) you would be treated as if you were the Fund for purposes of Chapter 42, including § 4942. Accordingly, the Transfer would not be treated as a qualifying distribution of the Fund. Rather, you would assume the Fund's obligations with respect to its undistributed income within the meaning of § 4942(c), if any, and you would reduce your own distributable amount under § 4942 by the Fund's excess qualifying distribution carryover under § 4942(i).

#### Issue 7

*Whether the transfer of the assets of the Fund to you in the Transaction would give rise to any net investment income under § 4940.*

By reason of § 4947(a)(1) and § 53.4947-1(b)(1), the Fund is treated as an organization described in § 501(c)(3) for purposes of §§ 507 and 509. As determined under § 509, the Fund is a private foundation and, thus, subject to the provisions of Chapter 42, including § 4940.

I.R.C. § 4940(a) imposes a tax on a private foundation's net investment income for the taxable year. Treas. Reg. § 53.4947-1(b)(1) provides that a charitable trust defined in § 4947(a)(1) is not treated as an organization described in § 501(c)(3) for purposes of exemption from taxation under § 501(a) and, thus, is subject to the excise tax on its investment income under § 4940(b) rather than the tax imposed by § 4940(a).

I.R.C. § 4940(b) imposes a tax on private foundations which are not exempt from taxation under § 501(a), including charitable trusts described in § 4947(a)(1). The amount of tax is equal to the amount, if any, by which the sum of (1) the tax imposed under § 4940(a) (computed as if the foundation were exempt) plus (2) the amount of tax which would have been imposed under § 511 if the foundation were exempt exceeds (3) the tax imposed on the organization under subtitle A. The foundation must therefore compute the amount of tax for which it would have been liable had it been an exempt foundation.

Rev. Rul. 2002-28 holds that when a private foundation transfers all of its assets to one or more private foundations in a transfer described in § 507(b)(2), the transfers do not constitute investments of the transferor and, therefore, do not give rise to net investment income subject to tax under § 4940(a).

As explained under Issue 1, above, the Transfer of all of the Fund's net assets to you is a transfer described in § 507(b)(2). Therefore, such Transfer would not constitute an investment of the Fund, and would not give rise to net investment income subject to tax under § 4940(a) or (b).

#### Issue 8

*Whether the transfer of the assets of the Fund to you in the Transaction would constitute an act of self-dealing under § 4941 of the Code by the Fund, you, or any foundations managers (as defined in § 4946) of you or the Fund.*

By reason of § 4947(a)(1) and § 53.4947-1(b)(1), the Fund is treated as an organization described in § 501(c)(3) for purposes of §§ 507 and 509. As determined under § 509, the Fund is a private foundation and, thus, subject to the provisions of Chapter 42, including § 4941.

I.R.C. § 4941(a) imposes an excise tax on each act of self-dealing between a disqualified person and a private foundation. I.R.C. § 4941 and Treas. Reg. § 1.507-3(a) determine whether the Transfer will constitute an act of self-dealing between a private foundation and its disqualified persons, as defined in § 4946. Under § 53.4946-1(a)(8), a "disqualified person," for purposes of § 4941, does not include organizations that are exempt under § 501(c)(3). Since the assets of the Fund will be transferred to you, an organization exempt under § 501(c)(3), by reason of § 53.4946-1(a)(8) the Transfer would not be a transfer to a disqualified person for purposes of § 4941. Hence, the Transfer will not constitute an act of self-dealing under § 4941.

#### Issue 9

*Whether the transfer of the assets of the Fund to you in the Transaction would constitute a jeopardizing investment within the meaning of § 4944.*

By reason of § 4947(a)(1) and § 53.4947-1(b)(1), the Fund is treated as an organization described in § 501(c)(3) for purposes of §§ 507 and 509. As determined under § 509, the Fund is a private foundation and, thus, subject to the provisions of Chapter 42, including § 4944.

I.R.C. § 4944 imposes an excise tax on any amount invested by a private foundation in a



manner that jeopardizes the carrying out of the foundation's exempt purposes. Rev. Rul. 2002-28 holds that where a private foundation transfers all of its assets and liabilities to another private foundation, the transfer does not constitute an investment for purposes of § 4944,

Since the Fund, an organization treated as a private foundation for purposes of § 4944, will transfer all of its assets and liabilities to you, a private foundation, the Transfer will not constitute an investment for purposes of § 4944 and, thus, will not be subject to tax under § 4944(a)(1). Therefore, the Transfer would not constitute a jeopardizing investment within the meaning of § 4944.

#### Issue 10

*Whether the transfer of the assets of the Fund to you in the Transaction would constitute a taxable expenditure under § 4945, and whether the Fund would be required to exercise any expenditure responsibility under § 4945(h) with respect to any assets transfer by the Fund to you.*

By reason of § 4947(a)(1) and § 53.4947-1(b)(1), the Fund is treated as an organization described in § 501(c)(3) for purposes of §§ 507 and 509. As determined under § 509, the Fund is a private foundation and, thus, subject to the provisions of Chapter 42, including § 4945.

I.R.C. § 4945(a) imposes a tax on any "taxable expenditure." I.R.C. § 4945(d)(4) provides that the term "taxable expenditure" includes any amount paid or incurred as a grant to a private non-operating foundation unless the grantor foundation exercises expenditure responsibility with respect to such grant in accordance with § 4945(h).

Rev. Rul. 2002-28 holds that where, by reason of § 1.507-3(a)(9)(i), a transferee foundation is treated as though it were the transferor foundation for purposes of § 4945, the transferee foundation is not treated as the recipient of an expenditure responsibility grant, and no expenditure responsibility requirements must be exercised under § 4945(d)(4) or (h) with respect to the transfer to the transferee foundation.

As explained under Issue 5, above, by reason of § 1.507-3(a)(9)(i), you would be treated as if you were the Fund for purposes of Chapter 42, including § 4945. Consequently, the Transfer would not be considered a taxable expenditure under § 4945 and there would be no expenditure responsibility requirements to be exercised by the Fund under § 4945(d)(4) or (h) with respect to the Transfer.

#### Issue 11

*Whether any transfer of your assets to a Trustee of the Fund in satisfaction of the Indemnification Obligations would constitute an act of self-dealing under § 4941 or a taxable expenditure under § 4945.*

Pursuant to the Agreement of Transfer, you have agreed to the Indemnification Obligations, which consist of obligations to indemnify, defend, and hold harmless each of the Trustees of the Fund, i.e., C and M, to the greatest extent permitted by applicable law, including the provisions

of Chapter 42 of the Code and the Treasury Regulations promulgated thereunder, from and against all expenses (including reasonable attorney's fees), judgments, and amounts paid in settlement that are actually and reasonably incurred by the Trustees that arise out of, or are attributable to, the execution or the performance of the Agreement of Transfer.

While M is a Trustee of the Fund, it is not a Trustee of yours, and is not, otherwise, a foundation manager or disqualified person with respect to you. Consequently, the transfer of your assets to M in satisfaction of the Indemnification Obligations would not be an act of self-dealing between a private foundation and a disqualified person within the meaning of § 4941. On the other hand, C, as one of your Trustees and, hence, a "foundation manager" within the meaning of § 4946(b)(1), is a disqualified person with respect to you. Thus, unless an exception applies, a transfer of your assets to C would constitute self-dealing under § 4941(d)(1)(E) and § 53.4941(d)-2(f)(1).

You represent that, under both State statutes and case law, the Trustees of the Fund are entitled to repayment out of Fund property for expenses (including reasonable attorney's fees), judgments, and amounts paid in settlement that are actually and reasonably incurred in the execution or performance of the Agreement of Transfer. Further, you represent that, under State law, the Trustees of the Fund would have an equitable lien on Fund property as against the Fund's beneficiaries for expenses (including reasonable attorney's fees, judgments, and amounts paid in settlement) that are actually and reasonably incurred in the execution or performance of the Agreement of Transfer. By entering into the Agreement of Transfer, you have notice of, and have agreed to, as a matter of contract law, an equitable lien on the Transferred Assets. You have also represented that any indemnification by you of a Trustee of the Fund in satisfaction of the Indemnification Obligations will be made only in compliance with applicable law, including the provisions of Chapter 42.

Since the Agreement of Transfer merely restates and clarifies the terms of the Trustees' equitable lien, any payment made in satisfaction of the Indemnification Obligations will not involve a "transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a private foundation" within the meaning of § 4941(d)(1)(E) and § 53.4941(d)-2(f)(1). Moreover, the Indemnification Obligations do not constitute a "mortgage or similar lien" on the Transferred Assets within the meaning of § 4941(d)(2)(A). Although the Indemnification Obligations constitute a "lien" on the Transferred Assets in the ordinary sense of the term, the term "mortgage or similar lien" generally involves a volitional act by a disqualified person in placing the lien on the property, whereas the equitable lien arises by operation of law. In addition, § 53.4941(d)-2(a)(2) provides that the term "similar lien" shall not include a lien that is insignificant in relation to the fair market value of the property transferred. In this case, the lien has no monetary value associated with it other than a speculative or negligible actuarial value.

Similarly, any payments made in satisfaction of the Indemnification Obligations will not constitute expenditures of charitable purposes within the meaning of § 4945(d)(5). They will instead be considered necessary administrative expenses to carry out charitable purposes within the meaning of § 53.4945-6(b).

## Conclusion

In light of the foregoing, we rule as follows:

1. The transfer of the assets of the Fund to you in the Transaction will constitute a significant disposition of assets to one or more private foundations within the meaning of § 1.507-3(c), and will constitute a transfer of assets by a private foundation to another private foundation described in § 507(b)(2).
2. The transfer of the assets of the Fund to you in the Transaction will not result in the termination of the Fund's treatment as a private foundation and will not result in the Fund being subject to the tax imposed by § 507(c).
3. Pursuant to § 507(b)(2), you will not be treated as a newly-created organization.
4. You will succeed to all of the tax attributes and characteristics of the Fund described in § 1.507-3(a)(2), (3), and (4).
5. Assuming that the Fund and you are effectively controlled (within the meaning of § 1.482-1A(a)(3)) by the same persons at the Effective Time of Transfer, you will be treated as if you were the Fund for purposes of Chapter 42 and §§ 507 through 509.
6. Pursuant to § 1.507-3(a)(9)(i) and Revenue Ruling 78-387, you may reduce the amount of your required distributions under § 4942 by the amount of the Fund's excess qualifying distribution carryover.
7. The transfer of the assets of the Fund to you in the Transaction will not give rise to any net investment income under § 4940.
8. The transfer of the assets of the Fund to you in the Transaction will not constitute an act of self-dealing under § 4941 by the Fund, you, or any foundation managers (as defined in § 4946(b)) of you or the Fund.
9. The transfer of the assets of the Fund to you in the Transaction will not constitute a jeopardizing investment within the meaning of § 4944.
10. The transfer of the assets of the Fund to you in the Transaction will not constitute a taxable expenditure under § 4945 and the Fund will not be required to exercise any expenditure responsibility under § 4945(h) with respect to any assets transferred by the Fund to you.
11. Any transfer of your assets to a Trustee of the Fund in satisfaction of the Indemnification Obligations will not constitute an act of self-dealing under § 4941 or a taxable expenditure under § 4945.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

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

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes in these facts. This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept in your permanent records.

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

In accordance with the Power of Attorney currently on file with the Internal Revenue Service, we are sending a copy of this letter to your authorized representative.

Sincerely,

Steven B. Grodnitzky  
Manager, Exempt Organizations  
Technical Group 1

Enclosure  
Notice 437