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200020058

Internal Revenue Service

Department of the Treasury

Washington, DC 20224

OP:E:EO:T4

Contact Person:

Telephone Number:

In Reference to:

Date: FEB 22 2000

Legend:

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Dear Sir or Madam:

This is in response to your letter dated November 15, 1999, in which you requested certain rulings with respect to a proposed transfer of assets from B to C, D, E, and F.

B, C, D, E and F are exempt under section 501(c)(3) of the Internal Revenue Code and are classified as private foundations under section 509(a).

At the present time, approximately one-half of B's annual gifts are gifts matching other contributions made by its four trustees individually or through their individual foundations (C, D, E and F). The four trustees are the children of the founders of B. B is planning to distribute one-half of its assets equally to C, D, E and F.

The primary reason for the transfer of assets is that three of the four trustees have established domicile or significant ties with communities in different areas of the United States. These ties include commitments to charitable organizations in those areas. They would, therefore, rather satisfy those obligations and commitments directly with gifts from their own foundations, rather than through matching gifts made by B.

Following the transfer of assets, B will retain its focus on charitable activities in the G area. The four siblings will

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remain trustees of B. After the transfer, B's matching gifts to C, D, E and F will be eliminated.

B represents that it does not have any outstanding grants with respect to which it is required to exercise expenditure responsibility under section 4945 of the Code. When B makes the proposed distributions, no flagrant repeated act (or failure to act) or willful and flagrant act (or failure to act) that could give rise to liability for excise taxes under Chapter 42 of the Code will have occurred.

Section 507(a) of the Code provides for the voluntary and involuntary termination of private foundation status. It states, in part, that except for transfers described in section 507(b), an organization's private foundation status will be terminated only if (1) the organization notifies the Service of its intent to terminate or (2) there has 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.

Section 507(b)(2) of the Code provides that when a private foundation transfers assets 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 new organization.

Section 1.507-1(b)(7) of the Income Tax Regulations provides that neither a transfer of all of the assets of a private foundation, nor a significant disposition of assets (as defined in section 1.507-3(c)(2)) by a private foundation (whether or not any portion of such significant disposition of assets is made to another private foundation) shall be deemed to result in a termination of the transferor private foundation under section 507(a) of the Code unless the transferor private foundation elects to terminate, pursuant to section 507(a)(1) or section 507(a)(2), is applicable.

Section 1.507-3(a)(2) of the regulations provides that a transferee organization, in the case of a transfer described in section 507(b)(2) of the Code, shall succeed to the aggregate tax benefit of the transferor organization in an amount equal to the amount of such aggregate tax benefit of the transferor organization, multiplied by a fraction the numerator of which is the fair market 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 is determined at the time of transfer.

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Section 1.507-3(a)(5) of the regulations provides that, except as provided in section 1.507-3(a)(9) (which only relates to 507(b)(2) transfers where all net assets are transferred to one or more controlled private foundations), a private foundation is required to meet the distribution requirements of section 4942 of the Code for any taxable year in which it makes a section 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 the requirements to the extent the amount transferred meets the requirements of section 4942(g).

Section 1.507-3(b) of the regulations provides that in order for a transfer of assets, pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization or reorganization, not to be a taxable expenditure, it must be to an organization described in section 501(c)(3) (other than an organization described in section 509(a)(4)) or treated as described in section 501(c)(3) under section 4947.

Section 4941(a) of the Code imposes a tax on each act of self-dealing between a disqualified person and a private foundation.

Section 4945(a) of the Code imposes a tax on the foundation on each "taxable expenditure" as defined in section 4945(d). Section 4945(d)(4) of the Code provides that for purposes of this section, the term "taxable expenditure" means any amount paid or incurred by a private foundation as a grant to an organization unless (A) such organization is described in paragraph (1),(2),or(3) of section 509(a) or is an exempt operating foundation (as defined in section 4940(d)(2)), or (B) the private foundation exercises expenditure responsibility with respect to such grant in accordance with subsection (h).

Section 4945(h) of the Code provides that expenditure responsibility referred to in subsection (d)(4) means that the private foundation is responsible to exert all reasonable efforts and to establish adequate procedures (1) to see that the grant is spent solely for the purpose for which made, (2) to obtain full and detailed reports with respect to such expenditures, and (3) to make full and detailed reports to the Secretary.

Section 53.4945-5(b)(7)(i) of the Foundation and Similar Excise Taxes Regulations refers to the rules relating to the extent to which the expenditure responsibility rules contained in section 4945(d)(4) and (h), and this section apply to transfers of assets described in section 507(b)(2).

Section 53.4945-5(c)(2) of the regulations provides that if a private foundation makes a grant described in section 4945(d)(4) to a private foundation which is exempt from taxation under section 501(a) for endowment, for the purchase of capital equipment, or for other capital purposes, the grantor foundation shall require reports from the grantee on the use of the principal and income (if any) from the grant funds. The grantee shall make such reports annually for its taxable year in which the grant was made and the immediately succeeding two taxable years.

Section 53.4945-6(b)(2) of the regulations provides that any expenditures for unreasonable administrative expenses, including compensation, consultant fees, and other fees for services rendered, will ordinarily be taxable expenditures under section 4945(d)(5) unless the foundation can demonstrate that such expenses were paid or incurred in the good faith belief that they were reasonable and that the payment or incurrence of such expenses in such amounts was consistent with ordinary business care and prudence. The determination whether an expenditure is unreasonable shall depend upon the facts and circumstances of the particular case.

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

Based upon the above facts, following the transfer of one-half of B's assets to C, D, E and F, B will continue to conduct its charitable activities in the G area. The four trustees of C, D, E and F will remain the trustees of B.

Because B is not terminating its existence and because there has been no willful, repeated or flagrant act giving rise to liability under Chapter 42, no tax will be imposed on B under section 507(c) as a result of the transfer of assets from B to C, D, E and F.

Since a transfer of assets as described in section 507(b)(2) will not cause a termination of an organization's private foundation status, the transfer of B's assets to C, D, E and F will not terminate B's status as a private foundation.

Because B will continue to conduct its charitable activities in the G area following the transfer of assets to C, D, E, and F, the proposed transfer of assets will not adversely affect the exempt status of B.

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B's transfer of assets to C, D, E and F will not be a taxable expenditure under section 4945(d), provided B exercises expenditure responsibility over the capital endowment grants made to C, D, E and F pursuant to section 4945(d)(4).

Because B, as an organization described in section 501(c)(3) of the Code, is not a disqualified person with respect to either C, D, E or F, the transfers of assets to C, D, E and F will not constitute acts of self-dealing within the meaning of section 4941 of the Code.

Provided the expenses incurred by B in the transfer of assets to C, D, E and F meet the "good faith" standard of section 53.4945-6(b)(2), such expenses will not constitute taxable expenditures under section 4945.

Accordingly, based on the information furnished, we rule as follows:

1. The transfer of one-half of the assets of B to C, D, E and F will qualify as transfers pursuant to section 507(b)(2) of the Code and will not subject B to the tax imposed by section 507(c) of the Code.

2. The proposed transfer of assets by B to C, D, E and F will not constitute either a willful flagrant act (or failure to act or one of a series of willful repeated acts (or failures to act) giving rise to tax liability under Chapter 42 of the Code.

3. The proposed transfer of assets by B to C, D, E and F will not adversely affect the exempt status of B under section 501(c)(3) and 509(a) of the Code.

4. The proposed transfer of assets by B to C, D, E and F will not be a taxable expenditure by B under section 4945(d) but will require B to exercise expenditure responsibility over these capital endowment grants pursuant to section 4945(d)(4).

5. B and its disqualified persons will not be deemed to have engaged in an act of self-dealing under section 4941 as a result of the transfer by B of 50 percent of the fair market value of its assets to C, D, E and F.

6. The reasonable expenditures for expenses incurred by B in connection with this ruling request and in effectuating the proposed transfer of assets will not constitute taxable expenditures under section 4945(d)(5) of the Code.

7. B's proposed transfer of assets to C, D, E and F will not result in the imposition of any other taxes under Chapter 42 of the Code.

We are informing the office of this action. Please keep a copy of this ruling with your organization's permanent records.

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 as precedent.

Sincerely,

Gerald V. Sack

Gerald V. Sack
Manager, Exempt Organizations
Technical Group 4