



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

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Date: November 21, 2005

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

UIL No.:

507.00-00
4940.00-00
4941.00-00
4942.00-00
4945.00-00

Legend:

M =
R =
S =
T =
State =
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Date =
Date 2 =
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Dear :

We have considered your ruling request dated July 17, 2003, as revised, supplemented and amended by subsequent correspondence. Your original ruling request was amended by you in a letter dated July 12, 2005. In that letter, you requested certain rulings under sections 507, 4940, 4941, 4942, 4944, and 4945 of the Internal Revenue Code, related to a proposed transfer of assets, in the manner and for the purposes described below.

FACTS

The original entity, R was formed as a non-stock corporation for the exclusively charitable purpose of operating a not-for-profit home to care for dependent women in S and surrounding areas. In Date, R applied for and received recognition of its exempt status as a private foundation. R filed annual reports as required under State law until Year. R failed to file reports as required and the corporate status was administratively terminated by T effective Date 2. R continued to operate from Year to present and continued to timely file the required information returns reporting its revenues, expenses and activities to the Internal Revenue Service. Your board of directors became aware of the administrative termination in Date 3. However because more than five years has passed since the date of the administrative termination of the legal corporate status of the Home, under Code, R cannot apply to the state corporation commission for reinstatement.

M was formed on Date 4 and has the same officers and directors as R. The Articles of Incorporation and Bylaws of M are the same in all material respects to the articles of incorporation and bylaws of R. M and R have the same articles of incorporation and bylaws updated for the language required by section 501(c)(3) of the Code. You will then transfer all of your assets to the successor corporation. Afterwards, you will notify the Service of your intent to terminate and will file all returns and reports required under sections 6033, 6043, and 6104 of the Code.

You filed your original request for a private letter ruling with the Internal Revenue Service with respect to the administrative dissolution of the corporate status. You requested that the Service approve the proposed transfer by R of its assets to M. In a letter dated July 24, 2003, the Service requested that you file a Form 1023 and obtain a new employer identification number for M. Thereafter you filed an amended and restated request for a letter ruling on July 11, 2005.

LAW

Section 501(c)(3) of the Internal Revenue Code provides for the exemption from federal income tax of any nonprofit organization that is organized and operated exclusively for charitable and/or other exempt purposes stated in that section.

Section 507 of the Code provides that a section 501(c)(3) exempt organization's classification as a private foundation may be terminated in the ways described respectively in sections 507(a)(1), 507(a)(2), 507(b)(1)(A), and 507(b)(1)(B). Section 507 also concerns, under section 507(b)(2), the transfer of assets by one private foundation to another private foundation(s).

Section 507(b)(2) of the Code provides that, in the transfer of assets by one private foundation to one or more other private foundations as part of a reorganization, the transferee private foundations shall not be treated as newly created organizations.

Section 507(c) of the Code imposes on each organization, the private foundation status of which is terminated under section 507(a), a tax equal to the lower of: (1) the amount which such organization substantiates by adequate records (or other corroborating evidence which may be required by the Commissioner) as the aggregate tax benefit (as defined in section 5079d)

resulting from the section 501(c)(3) status of such organization or (2) the value of the net assets of such organization.

Section 6043(b) of the Code provides, in part, that any exempt organization that for any of the last five taxable years preceding its liquidation, dissolution, termination or substantial contraction was exempt under section 501(a) shall file such return and other information with respect to such liquidation, dissolution, termination or substantial contraction as the Secretary, shall by forms or regulations prescribe.

Section 1.507-3(a) of the Income Tax Regulations indicates that, in a transfer of assets from one private foundation to another private foundation pursuant to a reorganization or liquidation, the transferee private foundation shall not be treated as a newly created organization, but shall succeed to the transferor's aggregate tax benefit under Code section 507(d).

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

Section 1.507-1(b)(6) of the regulations 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 section 507(b)(2) of the Code and section 1.507-3(c), such transferor foundation will not have terminated its private foundation status under section 507(a)(1).

Section 1.507-1(b)(9) of the regulations provides that a private foundation which transfers all of its net assets is required to file the annual information return required by section 6033, and the foundation managers are required to file the annual report of a private foundation required by section 6056, for the taxable year in which such transfer occurs. However, neither such foundation nor its foundation managers will be required to file such returns for any taxable year following the taxable year in which the last of any such transfers occurred, if at no time during the subsequent taxable years in question the foundation has either legal or equitable title to any assets or engages in any activity.

Section 1.507-3(a)(5) of the regulations provides that except as provided in subparagraph (9) of this paragraph, a private foundation is required to meet the distribution requirements of section 4942 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 such requirements to the extent the amount transferred meets the requirements of section 4942(g). However, where the transferor has disposed of all of its assets, the recordkeeping requirements of section 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.

Section 1.507-3(a)(7) of the regulations provides that, except as provided in section 1.507-

3(a)(9), where the transferor private foundation has disposed of all of its assets, sections 4945(d)(4) and 4945(h) of the Code shall not apply to the transferor or transferee foundations with respect to any "expenditure responsibility" grants made by the transferor foundation, except for any information reporting requirements imposed by section 4945 for any year in which any such transfer is made.

Section 1.507(a)-3(a)(8) of the regulations provides that certain tax provisions, listed therein, will carry over to a transferee private foundation that is given a Code section 507(b)(2) transfer of assets from a transferor private foundation.

Section 1.507-3(a)(9)(i) of the regulations 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 Sec. 1.482-1(a)(3)), directly or indirectly, by the same person or persons which effectively controlled the transferor private foundation, for purposes of chapter 42 (section 4940 et seq.) and part II of subchapter F of chapter 1 of the Code (sections 507 through 509) such a transferee private foundation shall be treated as if it were the transferor. However, where proportionality is appropriate, such a transferee private foundation shall be treated as if it were the transferor in the proportion which the fair market value of the assets (less encumbrances) transferred to such transferee bears to the fair market value of the assets (less encumbrances) of the transferor immediately before the transfer.

Section 1.507-3(a)(9)(ii) of the regulations provides that Subdivision (i) of this subparagraph shall not apply to the requirements under sections 6033, 6056, and 6104 which must be complied with by the transferor private foundation, nor to the requirement under section 6043 that the transferor file a return with respect to its liquidation, dissolution, or termination.

Section 1.507-3(a)(9)(iii) of the regulations, Example (2), describes a situation where a private foundation P, controlled by trustees A and B, made a grant to another private foundation W for which P was therefore required to exercise expenditure responsibility under sections 4945(d)(4) and 4945(h) of the Code. The same trustees A and B then transferred all of P's assets to private foundations R, S, and T, all also controlled by A and B. The Example concludes that R, S, and T are each required to assume P's expenditure responsibility for P's grant to W, unless one or two of them is assigned that task by agreement with P as part of the transfer. The Example also concludes that R, S, and T have no expenditure responsibility for the transfer grants received by them from P, because in this regard R, S, and T are treated as P rather than as recipients of expenditure responsibility grants from P.

Section 1.507-3(b) of the regulations provides that since a transfer of assets pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization or reorganization to an organization not described in section 501(c)(3) (other than an organization described in section 509(a)(4)) or 4947 is a taxable expenditure under section 4945(d)(5), in order for such a transfer of assets 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. See § 53.4945- 6(c)(3) of this chapter. Consequently, unless such a transferee is an organization described in section 509(a)(1), (2), or (3), the transferee is a private foundation and the rules of section 507(b)(2) and paragraph (a) of this section apply. On the other hand, if such a transfer of assets is made

to a transferee organization which is not described in either section 501(c)(3) (other than an organization described in section 509(a)(4)) or 4947, and in order to correct the making of a taxable expenditure, such assets are transferred to a private foundation, section 507(b)(2) and paragraph (a) of this section shall apply as if the transfer of assets had been made directly to such private foundation.

Section 1.507-3(c) of the regulations provides a transfer of assets is described in section 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. This shall include any organization or reorganization described in subchapter C of chapter 1. For purposes of section 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. For purposes of this paragraph, a distribution out of current income shall include any distribution described in section 4942(h)(1)(A) and (B).

The term significant disposition of assets to one or more private foundations shall include any disposition for a taxable year where the aggregate of:

- i. The dispositions to one or more private foundations for the taxable year, and
- ii. Where any disposition to one or more private foundations for the taxable year is part of a series of related dispositions made during prior taxable years, the total of the related dispositions made during such prior taxable years,

is 25 percent or more of the fair market value of the net assets of the foundation at the beginning of the taxable year (in the case of subdivision (i) of this subparagraph) or at the beginning of the first taxable year in which any of the series of related dispositions was made (in the case of subdivision (ii) of this subparagraph). A significant disposition of assets may occur in a single taxable year (as in subdivision (i) of this subparagraph) or over the course of two or more taxable years (as in subdivision (ii) of this subparagraph). The determination whether a significant disposition has occurred through a series of related distributions (within the meaning of subdivision (ii) of this subparagraph) will be made on the basis of all the facts and circumstances of the particular case. However, if one or more persons who are disqualified persons (within the meaning of section 4946) with respect to the transferor private foundation are also disqualified persons with respect to any of the transferee private foundations, such fact shall be evidence that the transfer is part of a series of related dispositions (within the meaning of subdivision (ii) of this subparagraph). In the case of a series of related dispositions described in subdivision (ii) of this subparagraph, each transferee private foundation shall (on any date) be subject to the provisions of section 507(b)(2) (with respect to all such dispositions made to it on or before such date) to the extent described in paragraphs (a) and (b) of this section.

Section 1.507-4(b) of the regulations provides that, with exceptions not involved here, the tax on termination of private foundation status imposed by section 507(c) of the Code does not apply to a section 507(b)(2) transfer of assets.

Section 1.507-3(d) of the regulations provides that a transfer of assets under section 507(b)(2) of the Code will not constitute a termination of the transferor's private foundation status.

Section 1.507-9(a) of the regulations provides that the Commissioner may at his discretion abate the unpaid portion of the assessment of any tax imposed by section 507(c), or any liability in respect thereof, if: (1) The private foundation distributes all of its net assets to one or more organizations described in section 170(b)(1)(A) (other than in clauses (vii) or (viii)) each of which has been in existence and so described for a continuous period of at least 60 calendar months, or (2) Effective assurance is given to the Commissioner in accordance with paragraphs (b) and (c) of this section that the assets of the organization which are dedicated to charitable purposes will, in fact, be used for charitable purposes.

Section 1.507-9(b) of the regulations, the Commissioner may at his discretion abate the unpaid portion of the assessment of any tax imposed by section 507(c), or any liability in respect thereof, under sections 1.507-9(b)(2) and (3) if the Commissioner determines that corrective action has been taken.

Section 1.507-9(c) of the regulations provides that the term corrective action referred to in section 1.507-9(b) means vigorous enforcement of State laws sufficient to assure implementation of the provisions of chapter 42 and insure that the assets of such private foundation are preserved for such charitable or other purposes specified in section 501(c)(3). Except where assets of the terminated private foundation are transferred to an organization described in section 509(a)(1) through (4) the State is required to take such action to assure that the provisions of section 508(e)(1)(A) and (B) are applicable to the terminated foundation (or any transferee) with respect to such assets as if such organization were a private foundation. Thus, the governing instrument of such organization must include provisions with respect to such assets:

- 1) Requiring its income therefrom for each taxable year to be distributed at such time and in such manner as not to subject such organization to tax under section 4942 (as if the organization were a private foundation),
- 2) Prohibiting such organization from engaging in any act of self-dealing (as defined in section 4941(d) as if the organization were a private foundation),
- 3) Prohibiting such organization from retaining any excess business holdings (as defined in section 4943(c) as if the organization were a private foundation),
- 4) Prohibiting such organization from making any investments in such manner as to subject such organization to tax under section 4944 (as if the organization were a private foundation), and
- 5) Prohibiting such organization from making any taxable expenditures (as defined in section 4945(d) as if the organization were a private foundation).

Consequently, in cases where the preceding sentence applies, although the private foundation status of an organization is terminated for tax purposes, it is contemplated that its status under State law would remain unchanged, because the tax under section 507(c) has been abated solely because the Commissioner has been given effective assurance that there is vigorous enforcement of State laws sufficient to assure implementation of the provisions of chapter 42. Therefore, in such a case while chapter 42 will not apply to acts occurring subsequent to termination which previously would have resulted in the imposition of tax under chapter 42, it is contemplated that there will be vigorous enforcement of State laws (including laws made applicable by the provisions in the governing instrument) with respect to such acts.

Notwithstanding the preceding three sentences, no amendment to the organization's governing instrument is necessary where there are provisions of State law which have the effect of requiring a terminated private foundation to which the rules of subparagraphs (1) through (5) of this paragraph apply to be subject to such rules whether or not there are such provisions in such terminated private foundation's governing instrument.

Section 4941 of the Code imposes a tax upon any act of self-dealing between a private foundation and any of its disqualified persons as defined in section 4946.

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

Section 4942(g)(1)(A) of the Code indicates, in pertinent part, that a private foundation does not make any qualifying distribution under section 4942(g) where the contribution is either: (i) to another organization that is controlled by the transferor or by one or more of the transferor's disqualified persons, or (ii) to any private foundation that is not an operating foundation under section 4942(j)(3), unless section 4942(g)(3) is met.

Section 4942(g)(3) of the Code requires that the transferor private foundation, in order to have a qualifying distribution for its grant to another private foundation, must have adequate records to show that the transferee private foundation in fact makes a qualifying distribution that is equal to the amount of the transfer received and that is paid out of the transferee's own corpus within the meaning of section 4942(h). That transferee's qualifying distribution must be expended before the close of the transferee's first taxable year after the transferee's taxable year in which the section 507(b)(2) transfer was received.

Section 4944(a)(1) of the Code imposes a tax upon the making by any private foundation of any investment that jeopardizes the conduct of its exempt purposes.

Section 4944(c) of the Code indicates that there is no tax upon any investment whose purpose is to further exempt purposes.

Section 4945 of the Code imposes tax upon a private foundation's making of any taxable expenditure as defined in section 4945(d).

Section 4945(d)(4) of the Code requires that, in order to avoid making a taxable expenditure, a transferor private foundation must exercise "expenditure responsibility" under section 4945(h) on its grants to another private foundation.

Section 4945(h) of the Code defines expenditure responsibility in terms of the grantor private foundation requiring proper reports from the grantee private foundation on the grantee's uses of the grant. In pertinent part, section 53.4945-5(b)(7) of the regulations refers to the rules of section 1.507-3(a)(7) of the regulations, cited above.

Section 4945(d)(5) of the Code provides that a taxable expenditure includes any amount expended by a private foundation for purposes other than exempt purposes under section 170(c)(2)(B).

Section 53.4946-1(a)(8) of the Foundation and Similar Excise Tax Regulations provide that, for purposes of self-dealing under section 4941 of the Code, an exempt organization under section 501(c)(3) is not a disqualified person.

Sections 53.4945-6(c)(3) and 1.507-3(b) of the regulations allow a private foundation to make section 507(b)(2) transfers of its assets to organizations exempt under section 501(c)(3) of the Code, not excluding private foundations, without the transfers being taxable expenditures.

Section 7701(a)(3) of the Code provides that the term 'corporation' includes associations.

Section 301-7701-3(a) of the regulations defines certain business entities (including associations under section 301.7701-2(b)(2)), as eligible entities.

Section 301-7701-3(b)(3)(i) of the regulations provides that (except for certain partnerships), unless the entity elects otherwise, an eligible entity in existence prior to the effective date of this section of the Code and regulations will have the same classification that the entity claimed under section 301.7701-1 through 301.7701-3 as in effect on the date prior to the effective date of this section.

Section 301.7701-3(c)(1)(v) of the regulations provides that an eligible entity that has been determined to be, or claims to be, exempt from taxation under section 501(a) of the Code is treated as having made an election under this section to be classified as an association. Such election will be effective as of the first day for which exemption is claimed or determined to apply, regardless of when the claim or determination is made, and will remain in effect unless an election is made under section 301.7701-3(c)(1)(i) after the date the claim for exempt status is withdrawn or rejected or the date the determination of exempt status is revoked.

ANALYSIS

R formed M as the successor according to articles of incorporation and bylaws that are the same in all material respects to the articles of incorporation and bylaws of R, updated to add language required under section 501(c)(3) of the Code and application regulations and by appointing officers and directors of M that are identical to the current officers and directors of R,

Under section 507(b)(2) of the Code, the transfer of all of the assets by R to M will result in M not being treated as a newly created organization, provided that R is first formed and recognized as an exempt private foundation. Under section 1.507-3(a)(1) of the regulations, M shall be treated as possessing those attributes and characteristics of R described in section 1.507-3(a)(2), (3) and (4).

As required under section 6043(b) of the Code, R shall file such returns and other information with respect to the transfer of its assets to M and termination as the Secretary may by forms or regulations require.

Since R is transferring all of its net assets to M, which is effectively controlled by R, for purposes of Chapter 42 (section 4940, et. seq.) and sections 507 through 509 of the Code, M

shall be treated as if it were R. Section 1.507-3(a)(9)(i). However, M shall not be treated as R with respect to the requirements of sections 6033 and 6104, as well as the requirement under section 6043 that R file a return with respect to its liquidation, dissolution, or termination. Sections 1.507-1(b)(9) and 1.507-3(a)(9)(ii). R will comply with its reporting and filing obligations under sections 6033, 6104 and 6043.

Because R will dispose of all of its assets, the recordkeeping requirements of section 4943(g)(3)(B) of the Code shall not apply to R during any period in which it has no assets. Since R will file a termination statement with the Service in accordance with section 507(a)(1) and terminate following its transfer of assets to M, such requirements will not apply to R for any taxable year following the taxable year of termination of R.

Under section 1.507-3(c) of the regulations, the transfer by R of its net assets to M shall constitute a "significant disposition of assets to one or more private foundations" because the transfer will constitute a disposition to one or more private foundations in a tax year of more than 25 percent of the fair market value of the net assets of R at the beginning of the taxable year. As such, under section 507(b)(2) of the Code and section 1.507-4(b), no tax imposed under section 507(c) shall apply to R's transfer of its net assets to M.

Upon notification by R to the Service of its intent to terminate, after the transfer of R's net assets to M, the termination tax imposed under section 507(c) of the code shall be zero because the value of the net assets of R upon its notice of intent to terminate will be zero. To the extent that the Service determines any termination tax is application to R upon delivery to the Service of its notice of intent to terminate, the Commissioner should at his discretion abate any tax imposed under section 507(c), or any liability in respect thereof, under section 1.507-9(a)(2) of the regulations since the articles of incorporation and bylaws of R satisfy section 1.507-9(c) and provide effective assurance to the Commissioner that the assets of R are dedicated to charitable purposes and will, in fact, be used for charitable purposes.

Under section 301.7701-2(b)(2) and section 301.7701-3(c)(v), R is treated as having elected to be classified as an association as of Date, the first day for which exemption is claimed or determined to apply for R, and this election will remain in effect unless R makes an election under section 301.7701-3(c)(1)(i) after the date the claim for exempt status is withdrawn or rejected, or as of the date the determination of exempt status is revoked.

Accordingly, based on the information submitted in your ruling request, we rule as follows:

1. That there was and is no change in R's corporate or tax-exempt status resulting from the administrative dissolution of R's corporate charter and status by T.
2. That M qualifies as an organization exempt from tax pursuant to section 501(c)(3) of the Code and that it will be treated as a private foundation pursuant to section 509(a) as of the date it is first organized.
3. That the deemed transfer of all of the net assets of R to M will constitute an adjustment described in section 507(b)(2) of the Code and R will not be treated as a newly created organization.

4. That the deemed transfer of all of the net assets of R to M will not terminate the status of R as a private foundation under section 507(a) of the Code, and will not result in the imposition of the termination tax under section 507(c).
5. That the deemed transfer from R to M does not constitute a willful and flagrant act or failure to act giving rise to liability for tax under Chapter 42 of the Code.
6. That M is effectively controlled (within the meaning of Treas. Reg. section 1.482-1(a)(3)) by the same persons who effectively controlled R; thus for purposes of Chapter 42 and part II of subchapter 1 of the Code, M, as the transferee foundation, will be treated as if it were the transferor.
7. That the deemed transfer of assets from R to M will not constitute a taxable expenditure of R under section 4945 of the Code and R will not be required to exercise expenditure responsibility or to comply with the information reporting requirements of section 4945, in any year following the year of the deemed transfer to M.
8. That R will not be required, for any taxable year subsequent to termination of its private foundation status under section 507(a) of the Code to comply with the periodic reporting, return, notice, inspection and information provisions of section 6033 and 6104. R will be required, upon termination to file the return required under section 6043(b). Further, in order to terminate, R must file the statement, and tax computations under section 507(c), as required by Treas. Reg. section 1.507-1(b)(1).
9. That section 4942 of the Code applies to M in the year of the deemed transfer as if it were R and, therefore, M will succeed to R's distribution requirements for the taxable years of the deemed transfers. Each foundation's distributable amount for the taxable years in which the deemed transfers occurred will be increased by the transferee foundation's pro rata share of the transferor's distributable amount for the year of the deemed transfer and all qualifying distributions made by the transferor in the year of the deemed transfer will be treated on a pro rata basis as having been made by the foundations. Each foundation will be responsible for reporting its respective pro rata share of all undistributed income determined under section 4942 for the year of the deemed transfer.
10. That M may, for purposes of determining its respective distribution requirements under section 4942 of the Code, reduce its respective distributable amounts by its ratable shares of R's excess qualifying distribution carryover, if any, determined as of the end of the taxable year immediately preceding the taxable year of the deemed transfer.
11. That the deemed transfer of R's assets to M does not give rise to net investment income for R or M and, therefore, does not result in the imposition of additional tax under section 4940 of the Code on either R or M.
12. That the deemed transfer does not constitute an act of self-dealing with respect to R or M under section 4941 of the Code.

13. That the deemed transfer from R to M does not constitute jeopardizing investments within the meaning of section 4944(a) of the Code.
14. Should R properly notify the Service that it intends to terminate its private foundation status, then such notice will be effective to terminate the private foundation status of R under section 507(a) of the Code.
15. Should the value of the net assets of R equal zero at such time as R gives the above notice and terminates its private foundation status, then R will not be liable for any termination tax under section 507(c) of the Code since the tax imposed by section 507(c) on zero assets is zero.

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.

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.

Sincerely,

Mary Jo Salins
Acting Manager
Exempt Organizations
Technical Group 2

Enclosure
Notice 437