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

200106040

Date: NOV 14 2000

Contact Person:

Uniform Issue List: 507.00-00
509.03-00
4940.00-00
4941.04-00
4942.03-05

Contact Number:

T:EO:B2

Legend:
X =
Y =

Dear Sir or Madam:

This is in reply to your rulings request of October 22, 1999, concerning X's proposed transfer of approximately one-half of its assets to Y pursuant to section 507(b)(2) of the Internal Revenue Code.

X and Y are exempt from federal income tax under section 501(c)(3) of the Code and are private foundations under section 509(a) of the Code which are effectively controlled by the same persons. X will transfer approximately one-half of its assets to Y. X will exercise the capital endowment grant expenditure responsibility required by section 4945(h) of the Code and section 53.4945-5(c)(2) of the Foundation and Similar Excise Taxes Regulations with respect to its transfer of part of its assets to Y.

The following rulings are requested:

1. Under section 4941 of the Code, X's transfer of part of its assets to Y will not be an act of self-dealing by X or Y or any disqualified person with respect to X or Y.

2. Under section 4940 of the Code, X's basis and holding period in the assets transferred will carry over to Y.

3. Under section 4940 of the Code, X's transfer of assets to Y will not be considered a sale of assets and will not result in capital gain net income.

4. Under section 4942 of the Code, X's transfer will carry over to Y the proportionate amount of X's excess qualifying distributions carryover under section 4942(i) of the Code from X's prior years.

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

Section 509(a) of the Code describes organizations exempt from federal income tax under section 501(c)(3) of the Code that are private foundations subject to the private foundation provisions of Chapter 42 of the Code.

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

Section 1.507-3(c)(1) of the Income Tax Regulations indicates that a transfer under section 507(b)(2) of the Code includes a transfer of assets from one private foundation to another private foundation pursuant to any reorganization, including a significant disposition of 25% or more of the transferor foundation's assets.

217

Section 1.507-3(a)(7) of the regulations provides that a private foundation that has transferred all of its assets to another private foundation in a transfer pursuant to section 507(b)(2) of the Code is not subject to the expenditure responsibility requirement of section 4945(h) of the Code.

Section 1.507-3(a)(9)(i) of the regulations indicates that, if a transferor private foundation transfers assets to another private foundation which is effectively controlled directly or indirectly by the same person or persons who effectively control the transferor private foundation, then the transferee foundation will be treated as if it were the transferor foundation, for purposes of sections 4940 through 4948 and sections 507 through 509 of the Code. The transferee is treated as the transferor in the proportion which the fair market value of the transferor's assets that were transferred bears to the fair market value of all of the assets of the transferor immediately before the transfer.

Sections 1.507-1(b)(7) and 1.507-3(d) of the regulations provide that a transferor foundation's transfer of assets under section 507(b)(2) of the Code will not constitute any termination of the transferor foundation's status as a private foundation.

Section 1.507-4(b) of the regulations provides that the tax under section 507(c) of the Code on termination of private foundation status does not apply to a transfer of assets pursuant to section 507(b)(2) of the Code.

Section 4940 of the Code imposes excise tax on certain investment income of a private foundation.

Section 4941 of the Code imposes excise tax on any act of self-dealing between a private foundation and any of its disqualified persons under section 4946 of the Code.

Section 53.4946-1(a)(8) of the regulations provides that, for purposes of self-dealing under section 4941 of the Code, an exempt organization under section 501(c)(3) of the Code is not a disqualified person.

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

Revenue Ruling 78-387, 1978-2 C.B. 270, describes the carryover of a transferor private foundation's excess qualifying distributions under section 4942(i) of the Code where the transferor and the transferee foundations are controlled by the same persons under section 1.507-3(a)(9)(i) of the regulations. The transferee is treated as the transferor so that the transferee can reduce its own distributable amount under section 4942 of the Code by its share of the transferor foundation's excess qualifying distributions under section 4942(i) of the Code.

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

Section 4945 of the Code imposes excise tax on a private foundation's making of any taxable expenditure under section 4945(d) of the Code.

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) of the Code on its grants to another private foundation.

Section 4945(h) of the Code defines expenditure responsibility in terms of a grantor private foundation requiring proper pre-grant inquiry and post-grant reports from a grantee private foundation on the grantee's uses of the grant.

Section 53.4945-5(c)(2) of the regulations provides that, if a private foundation makes a grant to another private foundation for endowment or other capital purposes, the grantor foundation must obtain reports from the grantee foundation on the uses of the principal and the income, if any, from the grant funds. The grantee must make such reports annually for its tax year in which the grant is made and for its immediately succeeding two tax years. Only if it is reasonably apparent to the grantor, before the end of such grantee's second succeeding tax year, that neither the principal nor the income from the grant funds has been used for any purpose which would result in liability for tax under section 4945 of the Code, may the grantor then allow the grantee's reports to be discontinued.

Analysis

X will transfer approximately one-half of its assets to Y pursuant to section 507(b)(2) of the Code. Your requested rulings are discussed below:

1.

Under section 4941 of the Code, X's transfer of assets to Y will not be an act of self-dealing because the transfer will be for exempt purposes to an organization Y exempt from federal income tax under section 501(c)(3) of the Code, which is not a disqualified person, for purposes of section 4941of the Code, pursuant to section 53.4946-1(a)(8) of the regulations.

2.

Under section 1.507-3(a)(8)(ii)(a) of the regulations, in this transfer of assets from X to Y pursuant to section 507(b)(2)of the Code, X's tax bases and holding periods for its assets transferred to Y will carry over to Y for purposes of section 4940 of the Code.

3.

X's transfer of assets to Y pursuant to this reorganization transfer under section 507(b)(2) of the Code will not result in any income or tax to X or Y under section 4940 of the Code.

4.

As in Revenue Ruling 78-387, described above, Y may reduce its required distributions under section 4942 of the Code by the amount, if any, of X's excess qualifying distributions carryover under section 4942(i) of the Code as of the time of the transfer because, under section 1.507-3(a)(9)(i) of the regulations, X's transfer will result in Y being treated as if Y were X for purposes of that section 4942 of the Code.

Accordingly, we rule that:

1. Under section 4941 of the Code, X's transfer of part of its assets to Y will not be an act of self-dealing by X or Y or any disqualified persons under section 4946 of the Code with respect to X or Y.

2. Under section 4940 of the Code, X's bases and holding periods in its assets transferred to Y will carry over to Y.

3. Under section 4940 of the Code, X's transfer of assets to Y will not be considered a sale of assets and will not result in capital gain net income or tax under that section 4940 of the Code.

4. Under section 4942 of the Code, X's transfer of a portion of its assets to Y will carry over to Y that proportionate amount of X's excess qualifying distributions carryover under section 4942(i) of the Code, if any, from X's prior years.

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Because this ruling letter could help to resolve any questions, please keep it in your permanent records, and include a copy in your next annual return.

This ruling letter 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,

Joseph Chasin

Joseph Chasin
Acting Manager, Exempt Organizations
Technical Group 2

220