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

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TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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501.03-02
509.03-00
4940.00-00
4941.04-00
4942.03-05
4943.00-00
4944.00-00
4945.04-06
6033.02-01

Identification Number:

Telephone Number:

T:EO:B2

Legend:
X =
Y =

Dear

This is in reply to your rulings request of December 31, 2001, on X's proposed transfer of all of its assets to Y and its merger into Y pursuant to section 507(b)(2) of the Internal Revenue Code.

X and Y are nonprofit corporations that 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. X and Y are effectively controlled by the same persons. X will transfer all of its asset to Y and merge into Y under state law. X will have no expenditure responsibility grants outstanding under section 4945(h) of the Code.

The following rulings are requested:

1. X's transfer of all of its assets to Y will be a transfer under section 507(b)(2) of the Code.

2. As a transfer described in section 507(b)(2), the proposed transaction will not result in a termination of the private foundation status of X under section 507(a) and will not cause the imposition of the termination tax described in section 507(c).

3. The proposed transfer from X to Y will not adversely affect the tax exempt status of either foundation.

4. The proposed transfer will not constitute a willful and flagrant act (or failure to act) giving rise to liability for tax under Chapter 42 of the Code.

5. Since X will have no assets at the time that notice of intent to terminate is given to the Service, no termination tax will be due from X under section 507(c) nor from Y as transferee.

6. Y will succeed to the tax benefits of X.

7. X's basis and holding periods in its assets will carry over to Y for purposes of section 4940 of the Code.

8. As the transferee of the net assets of X, Y will receive the benefit of any transitional rules or savings provisions applicable to X, as enumerated in sections 1.507-3(a)(8)(i) and (ii) of the Income Tax Regulations.

9. As a result of the proposed merger, Y will succeed to the excess qualifying distributions carryover of X as of the effective date of the merger.

10. After X transfers all of its assets to Y, X's excise tax liability under section 4940 of the Code for its final tax year may be subject to satisfaction by Y, and any refund to which X is entitled may be used by Y to offset Y's section 4940 excise tax. No taxes under Chapter 42 of the Code will be imposed on X or Y for Y's payment of any excise tax liability of X.

11. Because X and Y are effectively controlled by the same persons, for purposes of the Chapter 42 private foundation excise tax provisions and sections 507 through 509, Y will be treated as if Y is X, and Y will receive the tax attributes under Chapter 42 and sections 507 through 509 including the following:

(a) For purposes of section 4940, the net investment income of X for the taxable year of the transfer will be includible in the computation of the net investment income of Y in the taxable year of the transfer.

(b) The transfer will not be a realizable event giving rise to net investment income pursuant to section 53.4940-1(c)(1) of the Foundation and Similar Excise Tax Regulations. Therefore, such transfer will not give rise to tax under section 4940.

(c) Y can meet X's distributions under section 4942 of the Code for X's tax year in which X's transfer is made and for X's immediately preceding tax year if Y makes X's distributions under section 4942 of the Code on behalf of X in the same timely manner that would have otherwise been done by X itself. After X's tax year of its transfer has ended, X's remaining undistributed income, if any, which would have been the subject of X's next annual required distribution under section 4942 of the Code for X's next tax year after the tax year of the transfer, and which would have been distributed by X itself but for X's transfer to Y, can be allocated to Y, and can be distributed by Y on behalf of X on or before the end of X's tax year when X's undistributed income would have otherwise been distributed by X itself.

12. The transfer of assets will not result in any liability for tax under section 4940 since the transfer will not constitute a "sale or other disposition of property or other realizable event" within the meaning of section 4940 of the Code.

13. X will not be required to comply with the recordkeeping requirements of section 4942(g)(3)(B) with respect to the transfer of assets to Y pursuant to the merger after the transfer by operation of law of all of X's assets.

14. X will not be required to file the annual return described in section 6033 of the Code for any taxable years subsequent to the year of the merger.

15. The transfer of assets will not constitute self-dealing under section 4941 of the Code because, for purposes of section 4941, the term "disqualified person" does not include an organization described in section 501(c)(3) of the Code. Such transfer will not subject either foundation to tax under section 4941 of the Code.

16. The proposed transfer does not involve the application of section 4943 of the Code concerning excess business holdings because none of the assets transferred would place Y in the position of having excess business holdings.

17. The transfer of assets will not constitute a jeopardizing investment within the meaning of section 4944 of the Code.

18. The transfer of assets will not constitute taxable expenditures within the meaning of section 4945 of the Code, and X will not be required to exercise expenditure responsibility as the term is defined in section 4945(h) with respect to the transferred assets.

19. Although X does not have any outstanding grants that require the exercise of expenditure responsibility within the meaning of section 4945(h) of the Code and X does not have any plans to make any future grants that would require expenditure responsibility, if, notwithstanding the foregoing, X makes any grants that require expenditure responsibility prior to the transfer of all of its assets to Y, Y will exercise expenditure responsibility for all such grants. Such expenditure responsibility by Y would begin after X's transfer of all of its assets to Y. Any expenditure responsibility requirements imposed on X with respect to grants made to organizations other than Y will not subject X or Y to the imposition of any tax under section 4945 of the Code, provided that Y exercises such expenditure responsibility on behalf of X.

20. The legal, accounting and other expenses incurred by either foundation in connection with this ruling request and in effectuating the proposed transfer will not constitute taxable expenditures pursuant to section 4945 and will be considered qualifying distributions under section 4942.

Section 501(c)(3) of the Code provides for the exemption from federal income tax of nonprofit organizations organized and operated exclusively for the 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 are private foundations subject to the provisions of Chapter 42 of the Code.

Section 507(a)(1) of the Code and section 1.507-1(b)(1) of the Income Tax Regulations provide that a private foundation may voluntarily terminate its private foundation status by submitting to the Internal Revenue Service a statement of its intention to voluntarily terminate its private foundation status pursuant to section 507(a)(1) of the Code and by paying any termination tax under section 507(c) of the Code.

Section 507(c) of the Code impose excise tax on a private foundation which voluntarily terminates its private foundation status under section 507(a)(1) of the Code, and provides that this section 507(c) tax is equal to the lower of: (1) the aggregate tax benefits that have resulted from the private foundation's exempt status under section 501(c)(3) of the Code, or (2) the value of the net assets of the private foundation.

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 regulations indicates that a transfer under section 507(b)(2) of the Code includes a transfer of assets from one private foundation to one or more other private foundations pursuant to any reorganization, including a significant disposition of 25% or more of the transferor foundation's assets.

Section 1.507-3(a)(1) of the regulations provides that, in a transfer of assets from one private foundation to one or more private foundations pursuant to a reorganization, each transferee private foundation shall not be treated as a newly created organization, but shall succeed to the transferor's aggregate tax benefits under section 507(d) of the Code.

Section 507(d) of the Code indicates that the aggregate tax benefits of a private foundation refer to the value of its exemption from federal income tax and of the deductions taken by its donors during its existence.

Section 1.507-1(b)(9) of the regulations provides that a private foundation which transfers all of its net assets is not required to file annual information returns required by section 6033 of the Code for subsequent tax years after its tax year of such transfer when it has no assets or activities.

Section 1.507-3(a)(5) of the regulations provides that a transferor private foundation is required to meet its charitable distribution requirements under section 4942 of the Code, even for any tax year in which it makes a transfer of its assets to another private foundation pursuant to section 507(b)(2) of the Code. Also, where a private foundation transfers all of its assets, any recordkeeping requirements under section 4942(g)(3)(B) of the Code do not apply when the foundation has no assets.

Section 1.507-3(a)(7) of the regulations provides that, where a private foundation has transferred all of its assets to another private foundation in a transfer under section 507(b)(2) of the Code, it is not required to exercise expenditure responsibility under section 4945(h) of the Code with respect to such transfer.

Section 1.507-3(a)(9)(i) of the regulations provides that, if a private foundation transfers assets to one or more private foundations which are effectively controlled directly or indirectly within the meaning of section 1.482-1(i)(4) of the regulations by the same persons who effectively control the transferor foundation, each 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. Each transferee is treated as its transferor in the proportion which the fair market value of the transferor's assets transferred to the transferee bears to the fair market value of all of the transferor's assets immediately before the transfer.

Section 1.507-3(a)(9)(ii) of the regulations provides that a transfer of assets under section 507(b)(2) of the Code does not relieve the transferor private foundation from filing its own final tax year return as required by section 6043(b) of the Code.

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

Sections 1.507-1(b)(7) and 1.507-3(d) of the regulations provide that a private foundation's transfer of assets under section 507(b)(2) of the Code will not constitute any termination of the transferor foundation's private foundation status under section 509(a) 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 Foundation and Similar Excise Tax 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 4943 of the Code imposes excise tax on a foundation's excess business holdings.

Section 4944 of the Code imposes tax on any jeopardizing investments by a private foundation.

Section 4945 of the Code imposes excise tax on any private foundation's making of a 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 the grantor private foundation requiring pre-grant inquiry and post-grant reports as to the grantee private foundation on its uses of the grant.

Sections 53.4945-6(c)(3) allows a private foundation to transfer its assets to exempt organizations under section 501(c)(3) of the Code, including private foundations, pursuant to section 507(b)(2) of the Code, without the transfers being taxable expenditures under section 4945 of the Code, provided that any applicable expenditure responsibility requirement under section 4945(h) of the Code is met by the transferor private foundation.

Analysis

1.

Under section 507(b)(2) of the Code and section 1.507-3(c)(1) of the regulations, a transfer under section 507(b)(2) of the Code includes a transfer of assets from one private foundation to one or more other private foundations pursuant to any reorganization or liquidation or merger, which includes any significant disposition of 25% or more of the transferor foundation's assets, computed as of the beginning of the transferor's tax year. Because X will be in such a reorganization by its transfer and merger of all of its assets to Y, X's transfer of all of its assets will be a transfer under section 507(b)(2) of the Code.

2.

Under section 1.507-4(b) of the regulations, X's transfer of its assets pursuant to section 507(b)(2) of the Code will not terminate X's private foundation status under section 509(a) of the Code.

3.

X's transfer of all of its assets and merger under state law into Y is for exempt purposes under section 501(c)(3) of the Code and will not adversely affect the exemption of X or Y under section 501(c)(3) of the Code or the private foundation status of X or Y under section 509(a) of the Code.

4.

Under section 507(a)(2) of the Code, X's transfer of assets for exempt purposes under section 501(c)(3) of the Code will not be a willful and flagrant act (or failure to act) giving rise to liability for tax under the private foundation provisions of Chapter 42 of the Code.

5.

Section 507(c) of the Code imposes excise tax on a private foundation which voluntarily terminates its status as a private foundation pursuant to section 507(a)(1) of the Code. This section 507(c) tax is equal to the lower of: (a) the aggregate tax benefits that have resulted from the foundation's exempt status under section 501(c)(3) of the Code, or (b) the value of the net assets of the transferor private foundation. After X has transferred all of its assets to Y, the value of X's net assets will be zero. Thus, at that time, X's voluntary notice to the Internal Revenue Service of its termination of its private foundation status pursuant to section 507(a)(1) of the Code will not result in any termination tax under section 507(c) of the Code.

6.

Under section 507(b)(2) of the Code and section 1.507-3(a)(1) of the regulations, in this transfer of assets under section 507(b)(2) of the Code, X's aggregate tax benefits under section 507(d) of the Code will be transferred to Y.

7.

Under section 1.507-3(a)(8)(ii)(a) of the regulations, the tax bases and holding periods of X's assets transferred to Y will carry over to Y for purposes of section 4940 of the Code. Thus, the bases of X's assets transferred to Y will be the same in the hands of Y as the bases of such assets were in the hands of X.

8.

Under section 1.507-3(a)(8) of the regulations, X's transferee Y will receive the benefits, if any, of the transitional rules and savings provisions of that regulation that were applicable to X.

9.

As in Revenue Ruling 78-387, cited above, after X transfers all of its assets to Y, X's excess qualifying distributions, if any, under section 4942(i) of the Code, may be used by Y to reduce Y's distributable amount 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.

10.

Under section 1.507-3(a)(9)(i) of the regulations, transferee Y will be treated as its transferor X after X's transfer of all of its assets to Y pursuant to section 507(b)(2) of the Code. Thus, after X transfers all of its assets to Y, X's excise tax liability under section 4940 of the Code for its final tax year may be satisfied by Y, and any refund to which X is entitled may be used by Y to offset Y's excise tax under section 4940 of the Code. No taxes under Chapter 42 of the Code will be imposed on X or Y for Y's payment of any such excise tax liability of X.

11.

Under section 1.507-3(a)(9)(i) of the regulations, after X's transfer of all of its assets to Y pursuant to section 507(b)(2) of the Code, transferee Y will be treated as its transferor X for purposes of the private foundation provisions of Chapter 42 of the Code and sections 507 through 509 of the Code.

11.a.

Under section 1.507-3(a)(9)(i) of the regulations, after X's transfer of all of its assets to Y pursuant to section 507(b)(2) of the Code, Y will be treated as X for purposes of Chapter 42 of the Code. Thus, under section 4940 of the Code, X's net investment income for its tax year of its transfer can be included in Y's net investment income in the tax year of the transfer.

11.b.

X's transfer of assets to Y will not result in tax under section 4940 of the Code.

11.c.

Under section 1.507-3(a)(9)(i) of the regulations, after X's transfer of all of its assets to Y pursuant to section 507(b)(2) of the Code, Y will be treated as X for purposes of Chapter 42 of the Code. Thus, Y can meet X's distributions under section 4942 of the Code for X's tax year in which X's transfer is made and for X's immediately preceding tax year if Y makes X's distributions under section 4942 of the Code, on behalf of X, in the same timely manner that would have otherwise been done by X itself. Similarly, after X's tax year of its transfer has ended, X's remaining undistributed income, if any, which would have been the subject of X's next annual required distribution under section 4942 of the Code for X's next tax year after the tax year of the transfer, and which would have been distributed by X itself but for X's transfer to Y, can be allocated to Y, and can be distributed by Y, on behalf of X, on or before the end of X's tax year when X's undistributed income would have otherwise been distributed by X itself.

12.

X's transfer of assets to Y will not result in tax under section 4940 of the Code.

13.

Under section 1.507-3(a)(5) of the regulations, any recordkeeping requirement under section 4942(g)(3)(B) of the Code as to transferor X will not apply after X has transferred all of its assets to Y.

14.

Under section 1.507-1(b)(9) of the regulations, X will not be required to file any returns under section 6033 of the Code for any tax year subsequent to the tax year in which X transfers all of its assets to Y.

15.

X's transfer of its assets will be for exempt purposes to Y, which is an organization exempt from federal income tax under section 501(c)(3) of the Code. Under section 53.4946-1(a)(8) of the regulations, because Y is exempt from federal income tax under section 501(c)(3) of the Code, Y is not a disqualified person as to X under section 4946 of the Code for purposes of section 4941 of the Code. Because X's transfer of its assets will not be a transfer between a disqualified person and a private foundation, X's transfer of assets will not be acts of self-dealing under section 4941 of the Code.

16.

Based on your representation that X's assets are not excess business holdings of X or Y under section 4943 of the Code, X's transfer of its assets will not result in tax under section 4943 of the Code.

17.

X's transfer of its assets to Y for exempt purposes under section 501(c)(3) of the Code will not be a jeopardizing investment or result in tax under section 4944 of the Code.

18.

Under section 53.4945-6(c)(3) of the regulations, a private foundation can transfer assets pursuant to section 507(b)(2) of the Code to organizations exempt from federal income tax under section 501(c)(3) of the Code without the transfer being a taxable expenditure under section 4945 of the Code, provided that any expenditure responsibility requirement under section 4945(h) of the Code is met by the transferor.

Section 1.507-3(a)(7) of the regulations provides that, where a private foundation transfers all of its assets to one or more exempt organizations under section 501(c)(3) of the Code pursuant to section 507(b)(2) of the Code, such transferor foundation will not have to exercise any expenditure responsibility under section 4945(h) of the Code.

Thus, X's transfer of its assets to Y will not be a taxable expenditure under section 4945 of the Code, and X will not have to exercise expenditure responsibility under section 4945(h) of the Code with respect to its transfer of all of its assets to Y.

19.

If X makes any grants that require expenditure responsibility prior to X's transfer of all of its assets to Y, Y will exercise X's expenditure responsibility for all such grants by X. Y's expenditure responsibility for any grants made by X before the transfer of assets will begin after the transfer by X. X's expenditure responsibility requirements with respect to grants made by X to organizations other than its transferee Y will not subject X or Y to tax under section 4945 of the Code, provided that X's transferee Y will exercises X's expenditure responsibility on behalf of X.

20.

Under section 53.4942(a)-3(a)(2)(i) of the regulations, a private foundation's payment of administrative expenses as part of its charitable grantmaking may constitute a qualifying distribution under section 4942(g)(1)(A) of the Code. Thus, the legal, accounting, and other necessary expenses, incurred to implement X's transfer of assets to Y, if reasonable in amount, will be paid to accomplish exempt purposes and thus will not be taxable expenditures under section 4945 of the Code, but will be qualifying distributions under section 4942(g)(1)(A) of the Code.

Accordingly, we rule that:

1. X's transfer of all of its assets and merger into Y will be a transfer under section 507(b)(2) of the Code.

2. As a transfer described in section 507(b)(2) of the Code, the proposed transaction will not result in a termination of the private foundation status of X under section 507(a) of the Code and will not cause the imposition of the termination tax described in section 507(c) of the Code.

3. The proposed transfer from X to Y will not adversely affect the tax exempt status of either foundation X or Y under sections 501(c)(3) of the Code and 509 of the Code.

4. The proposed transfer will not constitute a willful and flagrant act (or failure to act) giving rise to liability for tax under Chapter 42 of the Code.

5. Since X will have no assets at the time that its notice of intent to terminate is given to the Internal Revenue Service, no termination tax will be due from X under section 507(c) of the Code nor from Y as transferee.

6. Y will succeed to the tax benefits of X under section 507(d) of the Code .

7. X's basis and holding periods in its assets will carry over to Y for purposes of section 4940 of the Code.

8. As the transferee of X's net assets, Y will receive the benefit of any transitional rules or savings provisions applicable to X, as enumerated in sections 1.507-3(a)(8)(i) and (ii) of the Income Tax Regulations.

9. As a result of the proposed transfer and merger, Y will succeed to the excess qualifying distributions carryover, if any, of X under section 4942(i) of the Code as of the effective date of the merger.

10. After X transfers all of its assets to Y, X's excise tax liability under section 4940 of the Code for its final tax year may be satisfied by Y, and any refund to which X is entitled may be used by Y to offset Y's section 4940 excise tax. No taxes under Chapter 42 of the Code will be imposed on X or Y for Y's payment of any excise tax liability of X.

11. Because X and Y are effectively controlled by the same persons, for purposes of the Chapter 42 private foundation excise tax provisions and sections 507 through 509, Y will be treated as if Y is X and will receive X's tax attributes under Chapter 42 of the Code and sections 507 through 509 of the Code including the following:

a. For purposes of section 4940 of the Code, the net investment income of X for the taxable year of the transfer will be includible in the computation of the net investment income of Y in the taxable year of the transfer.

b. The transfer will not be a realizable event giving rise to net investment income pursuant to section 53.4940-1(c)(1) of the regulations. Therefore, such transfer will not give rise to tax under section 4940 of the Code.

c. Y can meet X's distributions under section 4942 of the Code for X's tax year in which X's transfer is made and for X's immediately preceding tax year if Y makes X's distributions under section 4942 of the Code on behalf of X in the same timely manner that would have otherwise been done by X itself. After X's tax year of its transfer has ended, X's remaining undistributed income, if any, which would have been the subject of X's next annual required distribution under section 4942 of the Code for X's next tax year after the tax year of the transfer, and which would have been distributed by X itself but for X's transfer to Y, can be allocated to Y, and can be distributed by Y, on behalf of X, on or before the end of X's tax year when X's undistributed income would have otherwise been distributed by X itself.

12. X's transfer and merger of its assets into Y will not result in any liability for tax under section 4940 of the Code.

13. X will not be required to comply with the recordkeeping requirements of section 4942(g)(3)(B) of the Code with respect to the transfer of assets to Y pursuant to the merger after X's transfer by operation of law of all of its assets to Y.

14. X will not be required to file the annual return described in section 6033 of the Code for any taxable years subsequent to the year of the merger.

15. X's transfer of assets to Y will not constitute any act of self-dealing under section 4941 of the Code between a private foundation and any of its disqualified persons under section 4946 of the Code because, for purposes of section 4941 of the Code, the term "disqualified person" does not include any organization described in section 501(c)(3) of the Code. X's transfer to Y will not subject either foundation to tax under section 4941 of the Code.

16. X's proposed transfer does not involve the application of section 4943 of the Code concerning excess business holdings because, as you represent, none of the assets transferred will place Y in the position of having excess business holdings under section 4943 of the Code.

17. X's transfer of assets will not constitute a jeopardizing investment within the meaning of section 4944 of the Code.

18. X's transfer of assets will not constitute taxable expenditures within the meaning of section 4945 of the Code, and X will not be required to exercise expenditure responsibility as the term is defined in section 4945(h) of the Code with respect to X's transfer of all of its assets to Y.

19. Although X does not have any outstanding grants that require the exercise of expenditure responsibility within the meaning of section 4945(h) of the Code and X does not have any plans to make any future grants that would require expenditure responsibility, if, notwithstanding the foregoing, X makes any grants that require expenditure responsibility prior to the transfer of all of its assets to Y, Y will exercise expenditure responsibility for all such grants. Such expenditure responsibility by Y would begin after X's transfer of all of its assets to Y. Any expenditure responsibility requirements imposed on X with respect to grants made to organizations other than Y will not subject X or Y to the imposition of any tax under section 4945 of the Code, provided that Y exercises X's expenditure responsibility on behalf of X.

20. The legal, accounting, and other expenses, incurred by either foundation in connection with this ruling request and in effectuating the proposed transfer, if reasonable in amount, will not constitute taxable expenditures pursuant to section 4945 of the Code, and will be considered qualifying distributions under section 4942(g)(1)(A) of the Code.

Because this rulings letter could help to resolve any questions, please keep it in your permanent records.

This rulings letter is directed only to the organizations that requested it. Section 6110(k)(3) of the Code provides that this rulings letter may not be used or cited as precedent.

Sincerely,

Joseph Chasin
Acting Manager, Exempt Organizations
Technical Group 2