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

Date: MAY 6 1999

Contact Person:

ID Number:

Telephone Number

OP:E:EO:T:2

Employer Identification Number:

LEGEND: A =
B =
C =
D =
E =
F =

Dear Sir or Madam:

This is in reply to the letter of August 19, 1998, submitted on your behalf, regarding the possible tax consequences of a disqualified person as defined in section 4946 of the Internal Revenue Code exercising an option to purchase property from the estate of A.

B has been recognized as exempt under section 501(c)(3) of the Code and is a private foundation within the meaning of section 509(a).

A is the founder of B and he is now deceased. His will is being probated and B is the sole remaining beneficiary of his estate. Assets remaining in the estate include an undivided one-half interest in certain timber properties he jointly owned with C as tenants-in-common.

C was once the wife of A, but they divorced many years ago. C has the right, so long as she lives, to either sit on B's board of directors or to appoint another to serve in her place. D, her daughter, is currently appointed by her to sit on B's board. The submitted information states that C is a substantial contributor to B.

E is a holding company which conducts its business through a number of wholly-owned subsidiaries. It has two classes of authorized stock, voting and nonvoting. F holds all the shares of the voting common stock. F is the son of A and C and is one of B's directors. E and its predecessor companies have also been represented as being substantial contributors to B.

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The above mentioned undivided one-half interest in certain timber properties was subject to a long standing option agreement which is currently held by E as successor to an earlier corporation that was also owned by A. E has notified the Estate of A that it wishes to exercise its option to purchase the property interest and will pay the sales price in cash. The property is to be sold at fair market value as determined by an appraisal done by independent third parties. Once the appraisal is completed, the personal representatives of A's estate will seek approval of the sale from the court having jurisdiction over the estate.

Once E has acquired A's interest in the property it expects to enter into an arrangement with C to exchange pieces of their undivided one-half interests so that each will become the sole owner of an identifiable portion of the acreage. Thereafter C and E shall use the property as they desire.

It has been represented that this transaction will satisfy all of the requirements set forth in section 53.4941(d)-l(b)(3) of the Foundation and Similar Excise Tax Regulations.-

Accordingly, a ruling has been requested that pursuant to section 53.4941(d)-l(b)(3) of the regulations the sale by the Estate and purchase by E pursuant to the terms and provisions of the option agreement will not be an act of self-dealing under section 4941 of the Code.

Section 501(c)(3) of the Code exempts from Federal income tax organization organized and operated exclusively for charitable or educational purposes.
Section 509(a) of the Code provides that, unless specifically excepted, a domestic or foreign organization described in section 501(c)(3) is a private foundation and subject to the excise taxes of Chapter 42.

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

Section 4941(d)(l) of the Code defines self-dealing as including a sale or exchange of property or the extension of credit between a foundation and a disqualified person whether done directly or indirectly.

Section 53.4941(d)-l(a) of the regulations provides that for the purposes of section 4941, the term "self-dealing" means any direct or indirect transaction described in section 53.4941(d)-2 of the regulations.

Section 53.4941(d)-l(b)(l) of the regulations states that indirect self-dealing includes any transaction between a disqualified person and an organization controlled by a private foundation.

Section 53.4941(d)-l(b)(3) of the regulations provides that the term indirect self-dealing shall not include a transaction with respect to a private foundation's interest or expectancy in property (whether or not encumbered) held by an estate (or revocable trust, including a trust which has become irrevocable on a grantor's death), regardless of when title to the property vests under local law, if -

(i) The administrator or executor of an estate or trustee of a revocable trust either -

(a) Possess a power of sale with respect to the property,

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(b) Has the power to reallocate the property to another beneficiary, or

(c) Is required to sell the property under the terms of any option subject to which the property was acquired by the estate (or revocable trust);

(ii) Such transaction is approved by the probate court having jurisdiction over the estate (or by another court having jurisdiction over the estate (or trust) or over the private foundation);

(iii) Such transaction occurs before the estate is considered terminated for Federal income tax purposes pursuant to paragraph (a) of section I.641(b)-3 of this chapter (or in the case of a revocable trust, before it is considered subject to section 4947);

(iv) The estate (or trust) receives an amount which equals or exceeds the fair market value of the foundation's interest or expectancy in such property at the time of the transaction taking into account the terms of any option subject to which the property was acquired by the estate (or trust); and

(v) With respect to transaction occurring after April 16, 1973, the transaction either -

(a) results in the foundation receiving an interest or expectancy at least as liquid as the one it gave up,

(b) results in the foundation receiving an asset related to the active carrying out of its exempt purposes, or

(c) is required under the terms of any option which is binding on the estate (or trust).

Section 53.4941(d)-I(b)(8) of the regulations, Example (4), describes a situation where a substantial contributor to a private foundation bequeaths one-half of his estate to his spouse and one-half to the private foundation. The estate includes a one-third interest in a partnership, the remaining two-thirds of the partnership are owned by a disqualified person to the private foundation. The one-third interest was subject to an option agreement when it was acquired by the estate. The sale of the one-third interest in the partnership to the disqualified person did not constitute an act of self-dealing because the transaction satisfied the requirements set forth in section 53.4941(d)-I(b)(3).

Section 53.4941(d)-2 of the regulations discusses specific acts of self-dealing.

Section 53.4941(d)-2(a)(I) of the regulations provides that in general the sale or exchange of property between a private foundation and a disqualified person shall constitute an act of self-dealing.

Section 4946(a)(I) defines the term "disqualified persons" with respect to a private foundation as including a substantial contributor to the foundation, a foundation manager, and an owner of more than 20 percent of the total combined voting power of a corporation which is a substantial contributor to the foundation. It also includes a member of the family of any individual described above. In addition it includes a trust or estate in which persons described in above hold more than 35 percent of the beneficial interest.

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Section 4946(b) defines the term foundation manager as including 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.

Section 4946(d) states that the term "a member" of the family of a disqualified person includes the spouse, children of and grandchildren of a disqualified person.

Section 507(d)(2)(A) of the Code defines a substantial contributor as any person who contributed or bequeathed an aggregated amount of more than $5,000 to a private foundation, if such amount is more than 2 percent of the total contributions and bequests received by the foundation before the close of the taxable year of the foundation in which the contribution or bequest is received by the foundation from such person. In the case of a trust, the term substantial contributor also means the creator of the trust.

Section 4947(a) of the Code provides that certain trusts which are not exempt under section 501(a) of the Code are treated as private foundations and subject to the excise taxes imposed by Chapter 42.

Section 53.4947-1(b)(2)(ii)(A) of the regulations provides that when an estate from which the executor or administrator is required to distribute all of the net assets in trust for charitable beneficiaries, or free of trust to such beneficiaries, is considered terminated for Federal income tax purposes under section 1.641(b)-3(a) the estate will be treated as a charitable trust under section 4947(a)(1) between the date on which the estate is considered terminated under section 1.641(b)-3(a) and the date final distribution of all of the net assets is made to or for the benefit of the charitable beneficiaries.

B is a private foundation within the meaning of section 509(a) of the Code. The Estate of A is subject to the provisions of Chapter 42 by reason of section 4947(a). You have represented that C, D, E and F are all considered disqualified persons within the meaning of section 4946.

The regulations provide an exception from the self-dealing rules for matters involving the administration of an Estate. The transfer of the involved property is subject to an option agreement held by E which has been represented as being legally binding. In addition, the various requirements set forth in section 53.4941(d)-1(b)(3) of the regulations have been or will be satisfied.

Accordingly, based on the submitted information and representations submitted we have concluded that the sale by the Estate and purchase of the interest by E pursuant to the terms and provisions of the option agreement will not be an act of self-dealing under section 4941 of the Code.

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

In this ruling we have not determined whether the methodology to be used to determine fair market value of the assets is proper. We merely have accepted the given representation that the appraisal will reflect fair market value.

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We are informing the key District Director of this ruling. Because this letter could help resolve any question about B's exempt status, it should be kept in B's permanent records.

If there are any question about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter. For other matters, including questions concerning reporting requirements, please contact the key District Director.

Sincerely yours,

(signed) Garland A. Carter

Garland A. Carter
Chief, Exempt Organizations
Technical Branch 2