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

200221069

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: MAR 01 2002

S/N: 507.00-00

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Employer Identification Number:

Legend:
B=
C=
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Dear Sir or Madam:

This is in response to your letter dated December 11, 2001, in which you requested certain rulings with respect to a proposed transfer of all of the assets of B to C.

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

B and C were originally organized and funded by E and F. Both B and C have always operated as grant-making organizations for the purpose of supporting other organizations organized and operated for charitable and educational purposes. E is the sole voting member of both B and C.

The Board of Directors for B and C intend to approve a plan of merger under which B would merge with C. Under the plan C would be the surviving entity. The directors have concluded that the proposed merger would eliminate duplicative expenses associated with the operation of two foundations and would result in greater efficiency with respect to planning and making distributions to qualifying charitable organizations. After the merger, all of B's assets and liabilities would be transferred to C.

B has not notified the Service that it intends to terminate its private foundation status, nor has B ever received notification that its status as a private foundation has been terminated.

Furthermore, B has stated that it has not committed 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(a) of the Code 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 have 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 507(c) of the Code imposes a tax on an organization that terminates its private foundation status under section 507(a) of the Code.

Section 1.507-3(a)(5) of the Income Tax Regulations provides that a transferor private foundation is required to meet its charitable distribution requirements under section 4942 of the Code for any taxable year in which it makes a transfer of all or a part of its 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) of the Code. However, where the transferor has disposed of all of its assets, the record-keeping requirements of section 4942(g)(3)(B) of the Code shall not apply during any period in which it has no assets.

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, such transferor foundation will not have terminated its foundation status under section 507(a)(1).

Section 1.507-1(b)(7) of the 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)) by a private foundation (whether or not any portion of such 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)(1) of the regulations provides that in the case of a significant disposition of assets to one or more private foundations within the meaning of paragraph (c) of this subsection, the transferee organization shall not be treated as a newly created organization.

Section 1.507-3(a)(2)(i) 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 value 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.

Section 1.507-3(a)(8)(i) and (ii) of the regulations provides that, in a section 507(b)(2) transfer, the provisions enumerated in subparagraphs (a) through (g) thereof apply to the transferee foundation with respect to the assets transferred to the same extent and in the same manner that they would have applied to the transferor foundation had the transfer described in section 507(b)(2) not been effected.

Section 1.507-3(a)(9)(i) of the regulations provides that, if a transferor private foundation transfers assets to a private foundation which is effectively controlled (within the meaning of section 1.482-1A(a)(3)), directly or indirectly, by the same person or persons who effectively control the transferor private foundation, 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.

Section 1.507-3(d) of the regulations provides that unless a private foundation gives notice under section 507(a)(1) of the Code, a transfer of assets described in section 507(b)(2) of the Code will not constitute a termination of the transferor's private foundation status.

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 pursuant to section 507(b)(2) of the Code unless the provisions of 507(a) become applicable.

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

Section 4942 of the Code requires a private foundation to make specified distributions of income for each taxable year, including the year in which it transfers substantial assets to another private foundation under section 507(b)(2).

Section 4942(g)(1)(A) of the Code defines a qualifying distribution as any amount (including that portion of reasonable and necessary administrative expenses) paid to accomplish one or more purposes described in section 170(c)(2)(B), other than any contribution to (i) an organization controlled by the foundation or one or more disqualified persons or (ii) a private foundation which is not an operating foundation, except as otherwise provided; or (B) any amount paid to acquire an asset used directly in carrying out one or more purposes described in section 170(c)(2)(B).

Section 4942(g)(3) of the Code requires that a grantor private foundation, in order to have a qualifying distribution for its grant to another private foundation, which is not an operating foundation under section 4942(j)(3) of the Code, must have adequate records, as required by section 4942(g)(3)(B) of the Code, to show that the grantee private foundation, in fact, subsequently made qualifying distributions that were equal to the amount of the grant and that were paid out of the grantee's own corpus within the meaning of section 4942(h) of the Code. Such grantee foundation's qualifying distributions out of corpus must be expended before the close of the grantee's first tax year after its tax year in which it received the grant.

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

Section 4945(d)(4) of the Code defines the term taxable expenditure to include any amount paid or incurred by a private foundation as a grant to an organization unless (A) the organization is described in subparagraphs (1), (2), or (3) of section 509(a) of the Code or is an exempt operating foundation as defined in section 4940(d)(2) of the Code, or (B) the private foundation exercises expenditure responsibility with to such grant in accordance with section 4945(h) of the Code. The exercise of expenditure responsibility requires the foundation that makes the transfer to keep detailed records of the way the payment is spent by the recipient foundation.

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 4946(a)(1) of the Code defines the term "disqualified person" as a person who is a substantial contributor to a private foundation, a foundation manager, an owner of more than 20% of a corporation or partnership which is a substantial contributor to the private foundation, a family member of persons described above, or a corporation, partnership, trust or estate of which persons described above own more than 35% of the combined voting power.

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 53.4945-6(c)(3) of the regulations provides that a transfer of assets of a private foundation under section 507(b)(2) of the Code is not a taxable expenditure if such transfer is to an organization described in section 501(c)(3) (other than an organization described in section 509(a)(4)) or treated as so described under section 4947(a)(1).

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

Under section 507(b)(2) of the Code, in the case of a transfer of assets of any private foundation 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 newly created organization. Thus, the transfer by B to C will constitute in the aggregate an "adjustment, organization, or reorganization" within the meaning of section 507(b)(2). Accordingly, the transfer by B to C will not be treated as a transfer to a newly created organization.

Because B is not terminating its existence and assuming 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.

Under section 507(e) of the Code, the value of B's assets after it has transferred all of its assets to C will be zero. Thus, B's voluntary notice of termination of its private foundation status pursuant to section 509(a)(1) will not result in tax under section 507(c) of the Code.

Because B and C are effectively controlled by the same persons, C should be treated as if it were B for purposes of sections 507 through 509 and Chapter 42 of the Code. Therefore, the rulings requested under sections 4940, 4941, 4942, and 4944 would be provided because these rulings are consistent with the approach in section 1.507-3(a)(9)(i) of the regulations which is, in effect, to disregard the change in form of the organization for purposes of Chapter 42.

Because B is transferring all of its assets to C pursuant to a merger, and B and C are controlled by the same persons, C will be treated as B. The transfer will be treated as not having taken place for expenditure responsibility purposes under section 4945(h) of the Code. Thus, the transfer will not be a taxable expenditure under section 4945(d)(4). Therefore, B need not exercise expenditure responsibility with regard to the merger.

Subsequent to the merger, C will be treated as if it were B. Therefore, C will succeed to B's duty to exercise expenditure responsibility with respect to any outstanding grants of B for which expenditure responsibility is required and B would be relieved of any duty to exercise expenditure responsibility after the merger. B has represented that it currently has no grants for which expenditure responsibility is required. Based upon this representation, C would not assume any expenditure responsibility obligations as a result of the transfer.

As a result of the merger, C will be treated as B for purposes of Chapter 42. Therefore, the distribution requirements of section 4942 for the year of transfer should be regarded as satisfied by both B and C if, treating B and C as a single organization, the aggregate qualifying distributions for such year by B and C would satisfy its distribution requirement. Because C is treated as taking over B's obligations as of the date of merger, it follows that as of that date B will no longer have any such obligations.

Because B and C are controlled by the same persons, for purposes of Chapter 42 of the Code and sections 507 through 509 of the Code, C will be treated, subsequent to the transfer of all of B's assets, as if it were B. Thus C can succeed to B's excess qualifying distributions carryover for purposes of section 4942 of the Code.

Because B, as an organization described in section 501(c)(3) of the Code, is not a disqualified person with respect to C, the transfer of assets to C will not constitute an act of self-dealing within the meaning of section 4941 of the Code.

Because B will dispose of all of its assets, the recordkeeping requirements of section 4942(g)(3)(B) will not apply during any period in which it has no assets. Therefore, B's recordkeeping under section 4942(g)(3)(B) will not apply after the merger since B will have disposed of all of its assets.

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

1. The transfer of the assets of B to C pursuant to the merger constitutes a transfer of assets described in section 507(b)(2) of the Code and will not result in termination of B's status as a private foundation under section 507(a) of the Code.

2. Neither the transfer of assets of B to C pursuant to the merger, nor any subsequent notice of termination of B will result in the imposition of the termination tax under section 507(c) of the Code.

3. Because C and B are controlled by the same person, C will be treated as if it were B for purposes of Chapter 42, section 507 and section 509 of the Code.

4. As the result of the proposed merger, C will succeed to B's excess qualifying distribution carryover as of the effective date of the merger.

5. C will succeed to the aggregate tax benefit of B.

6. The contemplated transaction will not constitute an act of self-dealing and therefore will not result in the imposition of tax under section 4941of the Code.

7. The proposed transfer of the assets of B to C pursuant to the merger will not subject B to any tax under section 4942 of the Code for a failure to distribute income.

8. B will not be required to comply with the record-keeping requirements of section 4942(g)(3)(B) of the Code with respect to the transfer of all of its assets to C pursuant to the merger after the transfer of all of its assets.

9. The contemplated transaction will not be a taxable expenditure under section 4945 of the Code and therefore will not subject B to tax under section 4945 of the Code, nor will B be required to exercise expenditure responsibility over the assets transferred to C.

We are informing the Ohio TE/GE office of this action. Please keep a copy of this ruling in 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.

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,

Gerald V. Sack

Gerald V. Sack
Manager, Exempt Organizations
Technical Group 4