Internal Revenue Service

Department of the Treasury

Washington, DC 20224

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Person to Contact:

Telephone Number:

Refer Reply To:
CC:PSI:9-PLR-111955-01
Date:
September 23, 2002

Re:

LEGEND:

Taxpayer =
Country 1 =
Country 2 =
Foundation =

Dear :

This is in response to your letter dated February 22, 2001, and subsequent correspondence, from your authorized representative, requesting a ruling under section 2055 of the Internal Revenue Code.

The following facts have been submitted and representations made. Taxpayer is a citizen of Country 1 and a resident alien of the United States. Taxpayer created a charitable foundation (Foundation) that is organized and operates as a stiftung in Country 2.

The Foundation's purposes are charitable. To accomplish its charitable purposes, the Foundation will make grants to other charitable organizations both within and outside of the United States, and in some cases will provide direct financial support to needy individuals referred by charities. The Foundation will be funded primarily by Taxpayer. The Foundation does not intend to apply for an exemption under section 501(c)(3). The Foundation's charter meets the requirements of section 508(e) and contains the requirements of sections 4941 through 4945.

Taxpayer intends to execute a Will that will designate the Foundation as the primary beneficiary of his estate. Under the Will, the Foundation is to receive property primarily consisting of an interest in a partnership that holds real property that is organized and operated in Country 2. The Foundation's charter indicates that the partnership interest will be the Foundation's primary asset. The partnership historically has generated more than sufficient annual income for its partners to allow the Foundation to meet its

section 4942 qualifying distribution requirements. While the Foundation cannot sell or pledge the partnership interest without the consent of the other partners, it has received informal written assurance from a bank located in Country 2 that it could obtain loans on an unsecured basis sufficient to pay several years worth of section 4942 distributions.

A ruling has been requested that the proposed bequest to the Foundation will qualify for an estate tax deduction under section 2055.

LAW and ANALYSIS:

Section 501(c)(3) exempts from federal income tax organizations organized and operated exclusively for charitable purposes.

Section 508(a) provides generally that organizations shall not be treated as described in section 501(c)(3) unless they apply for recognition of exemption in a timely manner.

Section 508(d)(2) and section 1.508-2(b)(1) of the Income Tax Regulations provide that no gift or bequest made to an organization shall be allowed as a deduction under section 2055 if such gift or bequest is made – (A) to a private foundation or a trust described in section 4947 in a taxable year for which it fails to meet the requirements of section 508(e), or (B) to any organization in a period for which it is not treated as an organization described in section 501(c)(3) by reason of section 508(a).

Section 1.508-2(b)(1)(viii) provides that since a charitable trust described in section 4947(a)(1) is not required to file a notice under section 508(a), section 508(d)(2)(B), and section 1.508-2(b)(1)(i)(b) are not applicable to such a trust.

Section 508(e)(1) provides that a private foundation shall not be exempt from taxation under section 501(a) unless its governing instrument includes provisions the effects of which are – (A) to require its income for each taxable year to be distributed at such time and in such manner as not to subject the foundation to tax under section 4947 and (B) to prohibit the foundation from engaging in any act of self-dealing (as defined in section 4941(d)), from retaining any excess business holdings (as defined in section 4943(c)), from making any investments in such manner as to subject the foundation to tax under section 4944, and from making any taxable expenditures (as defined in section 4945(d)).

Section 2055(a)(3) provides that for purposes of the tax imposed by section 2001, the value of the taxable estate shall be determined by deducting from the value of the gross estate the amount of all bequests, legacies, devises, or transfers to a trustee or trustees, but only if such contributions or gifts are to be used by such trustee or trustees, exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, such trust, would not be

disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and such trustee or trustees, do not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

Section 20.2055 -1(a)(3) of the Estate Tax Regulations provides, in pertinent part, that a deduction is allowed under section 2055(a) from the gross estate of a decedent who was a citizen or resident of the United States at the time of his death for the value of property included in the decedent's gross estate and transferred by the decedent by will to a trustee or trustees, if the transferred property is to be used exclusively for religious, charitable, scientific, literary, or educational purposes (or for the prevention of cruelty to children or animals), if no substantial part of the activities of such transferee is carrying on propaganda, or otherwise attempting, to influence legislation, and if, in the case of transfers made after December 31, 1969, such transferee does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

Section 20.2055-1(a) provides, in pertinent part, that the deduction under section 20.2055-1(a)(3) is not limited, in the case of estates of residents of the United States, to transfers to trustees for use within the United States. Nor is the deduction subject to percentage limitations such as are applicable to the charitable deduction under the income tax.

Section 2055(d) provides that the amount of the deduction under section 2055 for any transfer shall not exceed the value of the transferred property required to be included in the gross estate.

Section 2055(e)(1) provides that no deduction shall be allowed under section 2055 for a transfer to or for the use of an organization or trust described in section 508(d) or 4948(c)(4) subject to the conditions specified in such sections.

Section 4942 generally requires a private foundation to made annual charitable distributions of at least 5 percent of the aggregate fair market value of its investment assets.

Section 4943(d)(3)(B) provides that the term “business enterprise” does not include a trade or business at least 95 percent of the gross income of which is derived from passive sources.

Section 4947(a)(1) provides that for purposes of sections 507-509 (other than sections 508(a), (b), and (c)) and for purposes of chapter 42, a trust which is not exempt from taxation under section 501(a), all of the unexpired interests in which are devoted to one or more of the purposes described in section 170(c)(2)(B), and for which a deduction was allowed under section 170, 545(b)(2), 556(b)(2), 642(c), 2055, 2106(a)(2), or 2522 (or the corresponding provisions of prior law), shall be treated as an organization

described in section 501(c)(3). Under section 53.4947-1(a) the basic purpose of section 4947 is to prevent these trusts from being used to avoid the requirements and restrictions applicable to private foundations.

Section 4948(b) provides that section 507(relating to termination of private foundation status), section 508 (relating to special rules with respect to section 501(c)(3) organizations), and chapter 42 (other than this section) shall not apply to any foreign organization that has received substantially all of its support (other than gross investment income) from sources outside the United States.

Section 53.4948-1(b) provides that section 507 (relating to terminations of private foundation status), section 508 (relating to special rules with respect to section 501(c)(3) organizations), and chapter 42 (other than section 4948) shall not apply to any foreign organization that from the date of its creation has received at least 85 percent of its support (as defined in section 509(d), other than section 509(d)(4)) from sources outside the United States. For purposes of this paragraph, gifts, grants, contributions, or membership fees directly or indirectly from a United States person (as defined in section 7701(a)(30)) are from sources within the United States.

Section 301.7701-4(a) of the Definitions Regulations generally defines trusts as arrangements whereby trustees take title to property for the purpose of protecting or conserving it for the beneficiaries (who cannot share in the discharge of this responsibility and, therefore, are not “associates in a joint enterprise for the conduct of business for profit”) under the ordinary rules applied in chancery and probate courts.

Estate of Swan v. Commissioner, 24 T.C. 829 (1955), acq.,1956-2 C.B. 8, aff'd in part and rev'd in part on other grounds, 247 F.2d 144 (2d Cir. 1957), considered the application of the federal estate tax to two stiftungs, one organized under the laws of the Principality of Liechtenstein and the other, under the laws of Switzerland. Although the laws of neither country recognized trusts, the stiftungs were found to be comparable to trusts under U.S. law rather than corporations, and were treated accordingly. Id. at 856-858.

ANALYSIS:

In determining whether the proposed bequest to the Foundation will qualify for the federal estate tax charitable deduction under section 2055, we must first determine whether the transfer satisfies section 2055(e)(1). This section disallows an estate tax charitable deduction for a gift to an organization described in section 508(d) or section 4948(c)(4), subject to the conditions specified in such sections.

Because Taxpayer, through his bequest, is providing substantially all of the Foundation’s support, the Foundation will not be described in section 4948(b). Accordingly, the Foundation will be subject to section 508(d) and not to section 4948(c)(4). Section 508(d)(2)(B) disallows a charitable deduction for a contribution to

any organization during a period in which the organization is not treated as described in section 501(c)(3) by reason of section 508(a). Under section 1.508-2(b)(1)(viii), contributions to charitable trusts described in section 4947(a)(1) are not subject to this rule. Thus, the question is whether the Foundation will be described in section 4947(a)(1). If so, then contributions to the Foundation will be deductible regardless of when or whether the Foundation applies for recognition of exemption under section 501(c)(3). Otherwise, the Foundation would have to apply for and receive recognition of exemption for the period in which the gift is made in order for the gift to be deductible.

The Foundation will be described in section 4947(a)(1) because: (1) the Foundation will be a trust; (2) the Foundation will not be exempt from tax under section 501(a); (3) all of the Foundation's assets will be devoted to charitable purposes; and (4) as discussed below, a deduction will be allowable under section 2055(a) for the proposed gift to the Foundation. We conclude that the Foundation is in the nature of a trust because it lacks associates and will not engage in the conduct of business for profit. See also, Estate of Swan v. Commissioner, supra, regarding the characterization of stiftungs organized under the laws of Liechtenstein and Switzerland as trusts for federal tax purposes.

Regarding section 501(a) status, the Foundation does not plan to apply for recognition of exemption. We conclude that the Foundation's purposes and planned operations are charitable. As discussed below, an estate tax charitable deduction will be allowable under section 2055 for the proposed bequest to the Foundation. Therefore, sections 2055(e)(1) and 508(d)(2)(B) will not disallow the deduction (based, in part, on our finding below that the Foundation will meet the section 508(e) requirements), because the Foundation will be described in section 4947(a)(1).

Section 508(d)(2)(A) disallows a deduction for a gift to a private foundation or a section 4947 trust in a taxable year for which the foundation or trust fails to meet the requirements of section 508(e). We find that the Foundation meets the section 508(e) requirements. In this regard, we find that the arrangement regarding the special representative will not necessarily result in any self-dealing.

The Foundation's charter specifically indicates that the Foundation expects to receive a bequest of Taxpayer’s interest in the partnership at his death. While such gift (subject to sale or pledge restrictions) could adversely affect the Foundation's ability to meet the section 4942 requirements, we find that it will not necessarily result in section 4942 violations under the facts and circumstances as represented herein.

For purposes of section 2055(e)(1), we conclude that sections 508(d) and 4948(c)(4) will not bar the deduction, under section 2055(a), of your proposed bequest to the Foundation. Accordingly, based upon the facts provided and the representations made, the proposed bequest to the Foundation will qualify for a charitable deduction under section 2055.

This ruling is subject to the following: (1) at the time of Taxpayer's death, Taxpayer is either a citizen or resident alien of the United States; (2) during Taxpayer's lifetime, the Foundation operates in a manner that meets with the requirements of section 2055 and chapter 42 of the Code; (3) the terms of the bequest to the Foundation under Taxpayer's Will satisfies the requirements of section 2055 and the applicable regulations; and (4) at Taxpayer's death, the Foundation, the partnership interest, and the other assets bequeathed to the Foundation, conform with the facts and representations made herein.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. This ruling is directed only to the taxpayer(s) requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative. A copy of this letter must be attached to any tax return to which it is relevant.

Sincererely
James F. Hogan
Senior Technician Reviewer, Branch 9
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure - Copy for section 6110 purposes