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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Number: **201012050**
Release Date: 3/26/2010

Date: December 30, 2009

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Uniform Issue List:
4941.00-00
1011.00-00

Legend:

A	=
B	=
Parent	=
Holding	=
C	=
zz	=
$yy	=
xx	=
nn percent	=
pp	=
uu percent	=
tt percent	=
Year	=
Date	=
Title	=

Dear :

This is in response to your ruling request dated August 8, 2008 regarding contributions to a private foundation and sections 4941 and 1011(b) of the Internal Revenue Code ("Code").

FACTS

You are an organization incorporated under the laws of the state of C. You are exempt from Federal income tax under section 501(a) of the Code as an organization described in section 501(c)(3), and are classified as a private foundation within the meaning of section 509(a). You state that A and B, husband and wife, plan to make substantial donations to you consisting of zz units of A's units in a closely held limited liability company ("LLC") organized under the laws of the state of C. Further, A and B may contribute more LLC units to you in the future. You state that the fair market value of the zz LLC units is approximately $yy million, and currently, A owns xx LLC units, which represents a nn percent ownership interest in the LLC. The LLC is an entity taxed as a partnership for federal income tax purposes and operates as an investment adviser

that manages large-cap equity portfolios. The LLC currently has operating liabilities that are less than two percent of the LLC's fair market value. You represent that as a limited liability company under the laws of the state of C, the LLC's members are not personally liable for its liabilities.

You represent that Holding, an entity in which A owns pp shares of stock equal to substantially less than one percent of the total outstanding shares of Holding, acquired LLC through its wholly-owned affiliate, the Parent. Parent is the managing member of the LLC and owns uu percent of its outstanding units. The remaining tt percent interest of LLC are held by employees of LLC other than A. A, co-founder and co-manager of the LLC since Year, serves as the LLC's Title. Additionally, there is an employment contract by and among A, the LLC and the Parent, which contains and memorializes A's current employment terms with the LLC. The employment contract expires on Date, with automatic successive one-year term renewals unless either party notifies the other of intent not to renew the employment contract. You represent that pursuant to the employment contract, A's entire LLC units are subject to certain put and call options. The Parent has the call option and A, the put option. In each year of the employment contract duration, the Parent has the call option upon 30 days prior notice to A to cause A to sell not more than 30,000 units of his LLC units and the Parent to purchase up to 30,000 units of A's LLC units for fair market value. Likewise, A has the put option upon 30 days prior notice to the Parent to cause the Parent to buy up to 30,000 units of A's LLC units and the Parent to purchase up to 30,000 units of A's LLC units for fair market value. Upon the termination of the employment contract, the Parent has the call option, after 90 days prior notice to A to cause A to sell at fair market value to the Parent, all but 20,000 units of A's LLC units. Likewise, A has the put option, after 90 days prior notice to the Parent to cause the Parent to purchase at fair market value from A, all or some portion of A's LLC units.

Upon the death of A, the Parent, after 90 days prior notice, has a call option, requiring A's estate to sell to Parent all or any of A's LLC units. Likewise, A's estate has a corresponding put option requiring the Parent to buy from A's estate such units. You represent that under no circumstances except with reason can the Parent object to A and B's plan to transfer LLC units to you. Furthermore, you represent that since A and B plan to contribute more LLC units in the future, it is possible a time will arrive when only you can exercise the put option if A and B transfers all A's LLC units to you, and upon such time if the Parent exercises a call option, it can only apply to the LLC units A and B transferred to you.

You represent that initially, the employment contract allowed A to retain the voting rights associated with the transferred LLC units however, the parties have agreed to amend the employment contract to provide you the voting rights over the transferred LLC units. Further, upon a call option by the Parent, it is in your complete discretion to decide whether the call option shall apply first to the transferred LLC units. Furthermore, you have the power to exercise the put option through A, who is required to allow you to exercise the put option with respect to your units before A or B exercise a put option to units they have retained. In addition, you represent that pursuant to the employment contract, A and B will not donate LLC units to you upon the Parent's notice to A of the Parent's intent to exercise a call option. You represent that you do not have any relationship with Holding or any of its affiliates except that A, one of your directors, owns pp shares in Holding, which amounts to substantially less than one percent of Holding's total outstanding shares and in addition, works for the LLC.

RULINGS REQUESTED

Based on the above facts, you request the following rulings:

1. That contributions by A and B to you, of A's interests in LLC will not be an act of self-dealing between A and B and you under section 4941(d)(1)(A) of the Code; and

2. That contributions by A and B to you, of A's interests in LLC will not result in any recognition of gain by A and B, except as provided in section 1011(b) of the Code and section 1.1011-2(a)(3) of the regulations (relating to the application of the "bargain sale" to donations of partnership and similar interests).

LAW

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

Section 4941(d)(1)(A) of the Code defines the term "self-dealing" to include any direct or indirect sale or exchange of property between a private foundation and a disqualified person.

Under section 4941(d)(1)(A) of the Code, a sale or exchange of property between a private foundation and a disqualified person(s) is an act of self-dealing.

Under section 4941(d)(2)(A) of the Code, a transfer of property is treated as a sale or exchange if the property is subject to a mortgage or similar lien which the private foundation assumes or which a disqualified person placed on the property within the 10-year period ending on the date of the transfer.

Sections 4946(a)(1)(A) & (B) of the Code provides that the term "disqualified person" includes a substantial contributor to a private foundation and a foundation manager.

Under section 4946(b)(1) of the Code, a foundation manager, for purposes of sections 4940, means with respect to any private foundation, 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(a)(1)(F) of the Code describes a disqualified person as including a partnership in which persons described in section 4946(a)(1)(A), (B), (C), or (D) own more than 35 percent of the profits interests.

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.

Section 53.4941(d)-2(a)(1) of the Foundation and Similar Excise Taxes Regulations ("foundation regulations") provides, in relevant part, that the sale or exchange of property between a private

foundation and a disqualified person shall constitute an act of self-dealing. Similarly, the sale of stock or other securities by a disqualified person to a private foundation in a bargain sale shall be an act of self-dealing regardless of the amount paid for such stock or other securities.

Section 53.4941(d)-2(a)(2) of the foundation regulations provides, in relevant part, that the term "'similar lien' shall include, but is not limited to, deeds of trust and vendors' liens, but shall not include any other lien if such lien is insignificant in relation to the fair market value of the property transferred."

Section 61(a) of the Code provides, in part, that, except as otherwise provided, gross income means all income from whatever source derived.

Under section 752(d) of the Code, in the case of a sale or exchange of an interest in a partnership, liabilities shall be treated in the same manner as liabilities in connection with the sale or exchange of property not associated with partnerships.

Under section 1011(b) of the Code, with respect to bargain sale to a charitable organization, If a deduction is allowable under section 170 (relating to charitable contributions) by reason of a sale, then the adjusted basis for determining the gain from such sale shall be that portion of the adjusted basis which bears the same ratio to the adjusted basis as the amount realized bears to the fair market value of the property. Under section 1.1011-2(a)(3) of the regulations, if property is transferred subject to an indebtedness, the amount of the indebtedness must be treated as an amount realized for purposes of determining whether there is a sale or exchange to which section 1011(b) of the Code and this section, section 1011(b), shall apply, even though the transferee does not agree to assume or pay the indebtedness.

Section 170(e)(1)(B)(ii) of the Code provides in part that, in the case of a charitable contribution to or for the use of a private foundation (as defined in section 509(a)) other than a private foundation described in subsection 170(b)(1)(F), the amount of any charitable contribution of property otherwise taken into account under section 170 shall be reduced by the amount of gain which would have been long-term capital gain if the property contributed had been sold by the taxpayer at its fair market value at the time of the contribution.

Under section 1.170A-1(c)(1) of the regulations, if a charitable contribution is made in property other than money, the amount of the contribution is the fair market value of the property at the time of the contribution reduced as provided in section 170(e)(1) of the Code and section 1.170A-4.

Under section 1.170A-4(c)(2)(i) of the regulations, for purposes of applying the reduction rules of section 170(e)(1) of the Code and this section to the contributed portion of the property in the case of a bargain sale, there shall be allocated under section 1011(b) to the contributed portion of the property that portion of the adjusted basis of the entire property that bears the same ratio to the total adjusted basis as the fair market value of the contributed portion of the property bears to the fair market value of the entire property. For purposes of applying section 170(e)(1) to the contributed portion of the property in such a case, there shall be allocated to the contributed portion the amount of gain that is not recognized on the bargain sale but that would have been recognized if such contributed portion had been sold by the donor at its fair market value at the time of its contribution to the charitable organization.

Section 1.170A-4(c)(2)(ii) of the regulations provides that the term "bargain sale", as used in this subparagraph, means a transfer of property which is in part a sale or exchange of the property and in part a charitable contribution, as defined in section 170(c) of the Code of the property.

Rev. Rul. 78-197, 1978-1 C.B. 83, provides that a taxpayer with voting control of a corporation and an exempt private foundation who donates shares of the corporation's stock to the foundation and, pursuant to a prearranged plan, causes the corporation to redeem the shares from the foundation does not realize income as a result of the redemption. The Internal Revenue Service (the "Service") will treat the proceeds as income to the donor under facts similar to those in the Palmer v. Commissioner, 62 T.C. 684 (1974), *aff'd on other grounds*, 523 F.2d 1308 (8th Cir. 1975), *acq.* 1978-1 C.B.2. In Palmer, the taxpayer donated stock in a closely held corporation to a private foundation. The Tax Court refused to re-characterize the gift and redemption as a sale or redemption between the taxpayer and the corporation followed by a gift of the proceeds to the corporation because the foundation was not legally bound to redeem the stock when it received the shares. The fact that the taxpayer held voting control over both the corporation and the foundation did not affect this result.

Rauenhorst v. Commissioner, 119 T.C. 157, 164 (2002), states that under the assignment of income doctrine, a transfer in the form of a gift of appreciated property may be disregarded for tax purposes if the substance of the transfer is an assignment of a right to income.

Ebben v. Commissioner, 783 F.2d 906 (9th Cir. 1986), provides that a contribution of a property that is subject to nonrecourse debt is a sale subject to the basis allocation rule of section 1011(b) of the Code.

ANALYSIS

RULING 1

The issue is whether A and B's contributions to you, a private foundation, will amount to self-dealing as prohibited by section 4941 of the Code. For a transaction to amount to self-dealing for the purposes of Chapter 42, among other characteristics, the parties to the self-dealing transaction must consist of a private foundation and a disqualified person. Under section 4946 (a)(1)(B), a disqualified person for the purpose of section 4941 includes a foundation manager of a private foundation. Section 4946(b) defines a foundation manager to include an officer, director, or trustee of a foundation. Because A and B are two of your directors, they are each disqualified persons with respect to you within the meaning of section 4946. We also note that LLC is not a disqualified person with respect to you as the total combined holdings of A, B, and any other disqualified person does not exceed 35 percent of the profits interest of the LLC. In order to be considered a disqualified person under section 4946(a)(1)(F), the holdings of certain disqualified persons must exceed 35 percent of the profits interest of a partnership.

The term "self-dealing" is defined in section 4941(d)(1)(A) of the Code to include any direct or indirect sale or exchange or leasing, of property between a private foundation and a disqualified person. Section 53.4941(d)-2(a)(1) of the foundation regulations provides that the sale of stock or other securities by a disqualified person to a private foundation in a "bargain sale" shall be an act of self-dealing regardless of the amount paid for such stock or other securities. Moreover, section 4941(d)(2)(A) states that a transfer of property by a disqualified person to a private

foundation shall be treated as a sale or exchange if the property is subject to a mortgage or similar lien which the private foundation assumes or which a disqualified person placed on the property within the 10-year period ending on the date of the transfer. It is further provided that the term "'similar lien' shall include, but is not limited to, deeds of trust and vendors' liens, but shall not include any other lien if such lien is insignificant in relation to the fair market value of the property transferred."

As discussed above in more detail, A and B plan to transfer units of LLC to you. The LLC itself is subject to certain section 752 liabilities that amount to less than two percent of LLC's fair market value. You represent that upon receipt of the LLC units, you shall assume no indebtedness, lien, mortgage or liability as a result of the transfer. Although the LLC is taxed as a partnership for federal income tax purposes, it is a limited liability company organized in the state of C and as such, its members are not personally liable for the LLC's liabilities. You also represent that the liabilities were placed on the LLC by the LLC, not by A or B. Given that the liabilities make up less than two percent of the LLC's fair market value, these section 752 liabilities are insignificant in comparison to the fair market value of the property to be transferred; therefore, these liabilities are not considered a "similar lien" for purposes of section 4941(d)(2)(A). Because (1) the liabilities are not a "similar lien" for purposes of section 4941, (2) you will not assume the liabilities, and (3) no disqualified person placed the liabilities on the LLC, the transfer is not considered a sale or exchange solely for purposes of section 4941(d)(1)(A).

Because the transfer will not result in a sale or exchange of property under section 4941(d)(1)(A) the transfer will not amount to a "bargain sale" solely for purposes of section 53.4941(d)-2(a)(1) of the foundation regulations. Therefore, A and B's transfer of the LLC units to you is not self-dealing under section 4941(d)(1)(A).

Further, although there are certain put and call options associated with the LLC units pursuant to A's employment contract, upon your receipt of the LLC units, you will own the LLC units outright with all voting rights. You will have the power to exercise the put option through A to sell the LLC units in order to raise the necessary funds to perform your charitable activities, without any restriction or objection from A and B. Furthermore, should the Parent exercise its call options, you will have the first right of refusal, or acceptance, over A and B, to either sell or refuse to sell your LLC units to the Parent before the call option will apply to the LLC units still in A's holdings.

RULING 2

In respect of the above transaction, the issue is whether A and B will recognize an income or gain as a result of their transfers/contributions to you. In the event of such transfers/contributions by a taxpayer; the Service, under two hypotheses; can attribute income or gain to a taxpayer, and they include the assignment of income doctrine and the bargain sale rules.

Under the assignment of income doctrine, for tax purposes, the law may overlook a transfer in the form of a gift of appreciated property, if the substance of the transfer is an assignment of a right to income. Rauenhorst v. Commissioner, 119 T.C. 157, 164 (2002). In addition, pursuant to Rev. Rul. 78-197, the Service will apply the assignment of income doctrine only if, at the time

of the transfer, the charitable donee is legally bound, or can be compelled, to sell the contributed property.

Pursuant to the above facts, and applying the above laws, the assignment of income doctrine does not apply to A and B's transfer of the LLC units to you. Neither the earnings of the LLC nor sale proceeds of the contributed LLC units is attributable to A and B. The transferred LLC units are subject to a call or put options exercisable not only at the Parent and at A's discretion but also at your discretion. Further, you represent that A and B will not donate the LLC units to you, if at the time of the donation, A and B had knowledge that the Parent has delivered notice under the employment agreement of the Parent's intent to exercise its call option. The mere fact that your LLC units may be callable at some future date following the transfer is not a basis, applying the anticipatory assignment of income doctrine, if at the time of the transfer you are not legally bound, or cannot be compelled, to transfer the LLC units to the Parent. In addition, A and B will retain no rights or interest in the donated LLC units and you will bear the risk of any change in the value of the LLC units from the date of the transfer until either A , the Parent, or you through A, exercises an option. Therefore, the Service holds that the assignment of income doctrine is inapplicable to A and B's transfers/contributions of their LLC units to you.

However, under the bargain sale rules, the Service holds that A and B's transfer of the LLC units that are subject to liabilities is a bargain sale, thus, A and B must recognize a gain or income under section 1011(b) of the Code and section 1.1011-2(a)(3) of the regulations. Nonetheless, you, upon receiving the LLC units, will assume no indebtedness, lien, mortgage, or liability. Pursuant to section 1011(b), with respect to bargain sale to a charitable organization, If a deduction is allowable under section 170 (relating to charitable contributions) by reason of a sale, then the adjusted basis for determining the gain from such sale shall be that portion of the adjusted basis which bears the same ratio to the adjusted basis as the amount realized bears to the fair market value of the property. Furthermore, under section 1.1011-2(a)(3) if property is transferred subject to an indebtedness, the amount of the indebtedness must be treated as an amount realized for purposes of determining whether there is a sale or exchange to which section 1011(b) shall apply, even though the transferee does not agree to assume or pay the indebtedness.

So pursuant to section 1011(b) of the Code and section 1.1011-2(a)(3) of the regulations, upon the contribution of an encumbered property to a charity, the transfer is treated as a bargain sale. As a rule, to the extent that the fair market value of the encumbered property exceeds the amount of the liabilities, there is a charitable contribution. However, to the extent that liabilities of the contributed property exceed the portion of the basis that is allocated to the sales portion, gain is realized. See Ebben v. Commissioner, 783 F.2d 906 (9th Cir. 1986) in which the court held that the contribution of property subject to nonrecourse debt is a sale subject to basis allocation rule of section 1011(b)). A and B already accepted that under sections 1011(b) and 1.1011-2(a)(3), A and B will realize taxable gain or income as the transaction amounts to a bargain sale however, you assert you will assume no liability for the donated LLC units interest. We agree. In your case, the transfer of LLC units that are subject to section 752 liabilities of the LLC, is a bargain sale, and therefore will result in A and B's recognition of gain or income under the provisions of sections 1011(b) and 1.1011-2(a)(3) even though you will assume no liability for the donated/contributed property.

RULINGS

Based on the information submitted, we rule as follows:

1. A and B's transfer of the LLC units to you will not constitute self-dealing under section 4941(d)(1)(A) of the Code; and

2. That contributions by A and B to you, of A's interests in LLC will not result in any recognition of gain by A and B, except as provided in section 1011(b) of the Code and section 1.1011-2(a)(3) of the regulations (relating to the application of the "bargain sale" to donations of partnership and similar interests).

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

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 by others as precedent.

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes in these facts. This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept in your permanent records.

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.

In accordance with the Power of Attorney currently on file with the Internal Revenue Service, we are sending a copy of this letter to your authorized representative.

Sincerely,

Robert W. Malone
Acting Manager,
Exempt Organizations
Technical Group 3

Enclosure
Notice 437