

FSLG Phone Forum on June 27, 2013 at 2 p.m.(EST) to Discuss Key FICA Replacement Plans Policy Issues.

Phone Forum for FICA Replacement Plans

Date: June 27, 2013

Time: 2 p.m. Eastern Time

What: During this 60 minute presentation we will cover:

- Social Security Coverage laws
- Qualified Employer's Retirement systems
- Defined Benefit and Defined Contribution Plan
- Revenue Procedure 91-40
- FICA replacement plans

Please register as soon as possible because space is limited.

If you have any travel reimbursement or allowance payments questions, please e-mail them to: te.ge.fslg.outreach@irs.gov, and we will try to answer them during the phone forum. Please use the subject line: FICA Replacement Plans.

Register at:

<http://apps.irs.gov/app/scripts/exit.jsp?dest=http://ems.intellor.com/index.cgi?p=204717&t=71&do=register&s=&rID=418&edID=305>

IRS: Extra Time Granted for Tax-IRS: Exempt Bond Issuers Affected by Severe Storms and Tornadoes in Oklahoma.

Government entity issuers of tax-exempt bonds affected by the severe storms and tornadoes occurring in parts of Oklahoma may qualify for additional time to file certain returns related to tax-exempt bonds, qualified tax credit bonds, and specified tax credit bonds.

Following recent disaster declarations for individual assistance issued by the Federal Emergency Management Agency, affected government entities in covered disaster areas in Oklahoma will receive filing and payment relief.

Affected issuers who are required to file a Form 8038 series information return or a Form 8038-T in connection with an arbitrage payment, with a due date between May 18, 2013 and Sept. 29, 2013,

may file such returns and make such payments on or before Sept. 30, 2013.

Affected issuers may also file such returns and make such payments on or before Sept. 30, 2013, if the records necessary to make such filing or payment, the conduit borrower, the bond counsel, or other professional upon whom the issuer relies to make such filing or payment are located in a covered disaster area.

The IRS will abate any late-filing penalty that would otherwise apply. The IRS automatically provides this relief to affected issuers located in covered disaster areas. Issuers need not contact the IRS to get this relief. However, affected issuers should clearly indicate on the top of the return that such late filing or payment is the result of devastation caused by the severe storms and tornados in Oklahoma.

In addition, an affected issuer required to file a Form 8038 series information return or a Form 8038-T in connection with an arbitrage payment, due between May 18, 2013 and Sept. 29, 2013, may request authority to file a Form 8038 or Form 8038-T after Sept. 30, 2013, by requesting an extension under Revenue Procedures 2002-48 and 2005-40, which provide guidance on how issuers may request extensions of time to file Form 8038 series information returns and waivers of penalty associated with a late arbitrage payment. Affected issuers should request relief in accordance with these revenue procedures and clearly indicate that such late filing or payment was the result of devastation caused by the severe storms and tornados in Oklahoma.

In addition, a Form 8038-CP authorized to be filed by an affected issuer between May 18, 2013 and Sept. 29, 2013, but filed thereafter, will be immediately processed upon receipt.

At this time, IRS relief for affected issuers applies to the following covered disaster areas in Oklahoma: Cleveland, Lincoln, McClain, Oklahoma and Pottawatomie counties.

Lawmaker Seeks Discounted Health Plan Fee for Tax-Exempt, Nonprofit Hospitals.

Rep. Tim Walberg, R-Mich., has urged Treasury to classify health plans owned by nonprofit, tax-exempt hospitals or hospital systems in the same category as other nonprofit, tax-exempt health plans, which would give the hospital plans a 50 percent discount on the insurance plan fee required under the Affordable Care Act.

May 22, 2013

The Honorable Jacob Lew

Secretary of the Treasury

United States Department of the Treasury

1500 Pennsylvania Avenue, NW, Room 3330

Washington, DC 20220

RE: REG-118315-12: Health Insurance Providers Fee

Dear Secretary Lew:

I write on a matter of concern to a number of federally taxable regional health insurance plans owned by tax-exempt hospitals and health care systems. These hospital-owned health plans (HHPs) are unique because they are entirely owned and controlled by parents that are tax-exempt under section 501(a) of the Internal Revenue Code (IRC) and are further described in section 501(c). Despite paying taxes under the IRC, HHPs function more similarly to nonprofit entities because they must reinvest whatever marginal profits they produce each year into the hospital parent's charitable mission. HHPs were originally created as taxable entities due to the prevailing physician ownership model at the time of their founding. However, as the ownership model moved away from physician ownership, HHPs found it nearly impossible to convert to nonprofit status due to the evolving interpretation of section 501(m) of the IRC. As a result, HHPs will be assessed at unsustainable levels under REG-118315-12: Health Insurance Providers Fee ("the insurer fee") and will likely be forced to significantly limit services or exit the market altogether. Either outcome will negatively affect the communities that HHPs serve by impacting the charitable activities of their parent hospitals.

The recently released rules implementing Section 9010 of the Patient Protection and Affordable Care Act (ACA) failed to curtail the implementation of the insurer fee on this specific group of health plans. In § 57.4(a)(4)(iii) of the insurer fee, the ACA is interpreted as granting partial reductions for certain exempt activities to health insurers that are exempt from Federal income tax and meet section 501(c) requirements. I believe HHPs should be included in this category of health plans that receive partial reductions because, like other nonprofit health plans, HHP premiums are attributable to the exempt activities of their parent nonprofit, tax-exempt hospitals and health systems. I urge you to provide relief to these plans from the insurer fee, consistent with the treatment of other tax exempt providers.

I am concerned that these taxable health plans owned entirely by nonprofit, tax-exempt hospitals or health systems appear to be included in a group of health plans that receive no exemptions from the insurer fee, while other nonprofit insurance providers receive either a partial or full exemption. I believe HHPs should receive a 50 percent exemption from the insurer fee because they are an essential part of the communities they serve.

HHPs operate differently than traditional for-profit health plans and should be treated accordingly. The parent hospitals and health systems, exempt under Internal Revenue Code Section 501(c)(3) and Section 501(c)(4), are required to hold and use all of their assets and earnings for tax-exempt, charitable purposes. This requirement extends to the equity and earnings of wholly owned/controlled taxable subsidiaries, such as HHPs. Therefore, the cost of the insurer fee that a HHP will be required to pay under the proposed regulation will ultimately reduce the resources of the parent hospital or health system to fulfill their charitable missions. The imposition of the fee on these hospitals and health systems will detract from the organization's mission and the vital community services they provide. To impose the insurer fee on these community-based providers is not sustainable and will have a damaging effect on the communities that these plans serve.

I believe that if no relief is granted to these hospital-owned health plans in the final regulations, these types of health plans will be assessed approximately \$200 million in fees in 2014 under the insurer fee. This will make it impossible for these plans to continue to offer quality, locally-based compassionate health care. The imposition of the full insurer fee on these providers may drive HHPs from the marketplace, thus limiting the choices available in these areas.

Classifying these 28 health plans with other non-profit tax-exempt health insurers appears to be in alignment with the federal government's tax exempt policies. These plans share the same charitable

mission-driven agendas of their parent nonprofit health systems and should be treated in the same manner as other tax-exempt entities. Adding these plans to the 50 percent tax exempt category would increase the fees of the health plans remaining in the non-exempt category by only about 1.8 percent, resulting in a de minimis impact on the health insurance marketplace.

I greatly appreciate your willingness to continue refining your approach and hope you will grant these hospital-owned health plans a 50 percent exemption from the Health Insurance Providers Fee.

Sincerely,

Tim Walberg

Member of Congress

[IRS Rules Against Fla. CDD.](#)

In a precedent-setting decision that could have major ramifications for issuers, the Internal Revenue Service has ruled a Florida Community Development District is not a political subdivision that can issue tax-exempt bonds.

The decision, made in a 12-page technical advice memorandum the IRS' chief counsel's office sent to the Villages CDD on May 30, means that approximately \$364 million of its bonds could be declared taxable. It also threatens the tax-exempt status of bonds issued by thousands of organizations with similar structures around the country.

Capping a five-and-a-half year long examination, the IRS said that the Villages CDD board was controlled by the private developer for many years while the bonds were issued and was therefore not a political subdivision under Section 103 of the Internal Revenue Code.

"The mere delegation of sovereign power is not sufficient to create a political subdivision," the IRS said in the TAM. "If it were sufficient, then a clearly private entity with powers of eminent domain, including some railroads and utilities, could issue bonds without any political oversight."

"We believe that an entity that is organized and operated in a manner intended to perpetuate private control, and to avoid indefinitely responsibility to a public electorate, cannot be a political subdivision of a state," the IRS said.

Perry Israel, a lawyer based in Sacramento who is representing the CDD, said the district was disappointed in the TAM's conclusion and is concerned the IRS may be making new rules through the examination process.

Sources said the CDD has several options going forward including, settling with the IRS to preserve the tax-exempt status of the bonds, appealing to the agency's Office of Appeals, allowing the IRS to go after the bondholders who could in turn challenge the ruling in court, or seeking a legislative fix. The issuer does not have the ability to fight the IRS in a court, only taxpayers can do that, they added.

At least two lawmakers from Florida — Sen. Bill Nelson, a Democrat and Rep. Richard Nugent, a Republican — sent separate letters to the IRS ahead of its ruling urging the agency to consider the implications of any federal tax policy that might jeopardize the ability of CDDs to continue to issue

tax-exempt municipal bonds in Florida. They worried about the potential harmful impacts on Florida homeowners already saddled by a weak economy.

The district is still considering its options, Israel said.

The IRS noted that the TAM, like other agency rulings for a particular issuer, may not be used or cited as precedent for other issuers. But for months, market participants have been warning that if the agency takes the view that the CDD is not a subdivision, this could potentially hurt scores of other CDDs and special districts.

There are nearly 580 CDDs operating in Florida alone that have been relying on the assumption that they are political subdivisions that can issue tax-exempt bonds.

“The IRS seems to be adding a new requirement for an issuer to be a political subdivision,” said Scott Lilienthal, president of the National Association of Bond Lawyers and a partner with Hogan Lovells US LLP. “That new requirement doesn’t seem to be based on any existing authority. If the IRS wants to revisit the definition of a political subdivision then it should so through the formal rulemaking process and issue guidance on a prospective basis only.”

The Village Center CDD issued \$426.2 million of tax-exempt bonds from late November 1993 through June 1, 2004 to finance the acquisition of recreational and other facilities as well as a utility system for the Villages, a retirement community in Florida. The CDD is a commercial district encompasses more than 21,000 acres primarily located in Sumter County, Fla.

CDDs are authorized under Florida law to levy and collect special assessments to pay debt service on bonds and maintenance assessments to fund district operations.

Most recently the Villages CDD urged the IRS to end its audit after a review showed it didn’t overpay when purchasing four pieces of property with bond proceeds. The district said the valuations showed it had not been controlled by the developer.

by: JENNIFER DEPAUL

[IRS Releases Publication on Managing Taxpayer Clinics.](#)

Citations: Publication 3319

The IRS has released Publication 3319 (rev. May 2013), Low Income Taxpayer Clinic: 2014 Grant Application Package and Guidelines, explaining the requirements for the development, expansion, or continuation of a qualifying IRS low-income taxpayer clinic program and providing instructions on how to apply for a grant.

The publication is available at:

<http://www.irs.gov/pub/irs-pdf/p5066.pdf>

[IRS Accepting Applications for Low Income Taxpayer Clinic Grants.](#)

The Internal Revenue Service today announced the opening of the 2014 Low Income Taxpayer Clinic (LITC) grant application process.

The LITC grant program is a federal program administered by the Office of the Taxpayer Advocate at the IRS, led by National Taxpayer Advocate Nina E. Olson. The LITC program awards matching grants of up to \$100,000 per year to qualifying organizations to develop, expand, or maintain a low income taxpayer clinic. The LITC program funds organizations that serve low income individuals who have a tax dispute with the IRS (*i.e.*, a “controversy clinic”) and organizations that provide education and outreach to taxpayers who speak English as a second language (an “ESL clinic”). Applicants may apply as either type of organization, or both. Although LITCs receive partial funding from the IRS, LITCs, their employees, and their volunteers operate independently from the IRS. Examples of qualifying organizations include:

- Clinical programs at accredited law, business or accounting schools whose students represent low income taxpayers in tax disputes with the IRS; and
- Organizations exempt from tax under Internal Revenue Code Section 501(a) that represent low income taxpayers in tax disputes with the IRS or refer those taxpayers to qualified representatives, or that provide outreach and education for ESL taxpayers.

The IRS welcomes all applications and will ensure that each application receives full consideration. The IRS is particularly interested in receiving applications from organizations that will operate in areas that are currently underserved.

Currently underserved areas are as follows:

Identified States for New or Existing Clinics	
CONTROVERSY	ESL
Alaska, Alabama, Kansas, North Dakota, South Dakota	Alabama, Colorado, Connecticut, Georgia, Louisiana, Montana, New Mexico, North Dakota, South Dakota
Identified Metropolitan Areas for New Clinic Applications	
Los Angeles, California, including the following counties:	Los Angeles, Kern, Riverside, Ventura
Sacramento, California, including the following counties:	El Dorado, Placer, Sacramento, San Joaquin, Stanislaus
Philadelphia, Pennsylvania, including the following counties:	Berks, Delaware, Philadelphia
St. Louis, Missouri, including the following counties:	Cape Girardeau, Jefferson, St. Francois, St. Louis

Copies of the 2014 Grant Application Package and Guidelines, IRS [Publication 3319](#), can be downloaded from IRS.gov or ordered by calling 800-TAX-FORM (800-829-3676).

The IRS is authorized to award a multi-year grant not to exceed three years. For a new clinic or a clinic applying for the first year of a three-year grant, the clinic must submit the application electronically at www.grants.gov. For an existing clinic requesting funding for the second or third year of a multi-year grant, the clinic must submit the application electronically at www.grantsolutions.gov. All applicants must use the funding number of TREAS-GRANTS-0520-

4-001 and applications must be submitted electronically by July 12, 2013.

Questions about the LITC Program or grant application process can be addressed to the LITC Program Office at 202-622-4711 (not a toll-free call) or by email at LITCProgramOffice@irs.gov.

For more information about the organizations receiving funding in 2013, see [Publication 4134](#), Low Income Taxpayer Clinic List. This publication is also available by calling 800-TAX-FORM (800-82-3676), or can be found at your local IRS office.

IRS: Individual Isn't Entitled to Carryover Deductions From Conservation Easement Contribution.

Citations: Michael S. Mountanos v. Commissioner; T.C. Memo. 2013-138; No. 8158-10

The Tax Court, sustaining a gross valuation misstatement penalty, held that an individual isn't entitled to carryover deductions from a charitable contribution of a conservation easement on undeveloped and rugged land because the individual didn't show that the conservation easement had any value.

MICHAEL S. MOUNTANOS,

Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

UNITED STATES TAX COURT

Filed June 3, 2013

Wendy Abkin and Donald L. Feurzeig, for petitioner.

Christain A. Speck and Matthew D. Carlson, for respondent.

MEMORANDUM FINDINGS OF FACT AND OPINION

KROUPA, Judge: Respondent determined deficiencies exceeding \$1.1 million and section 66621 accuracy-related penalties regarding petitioner's Federal [*2] income tax for 2006, 2007 and 2008 (years at issue). We must decide two issues. The first issue is whether petitioner is entitled to carryover deductions from a charitable contribution of a conservation easement for the years at issue. We hold that he is not. The second issue is whether petitioner is liable for an accuracy-related penalty for each year at issue. We hold that he is.

FINDINGS OF FACT

Some of the facts have been stipulated and are so found. We incorporate the stipulation of facts, the first supplemental stipulation of facts, the second supplemental stipulation of facts and the accompanying exhibits by this reference. Petitioner resided in California when he filed the petition.

I. Blue Lakes Ranch

Petitioner owned 882 acres of largely undeveloped land in Lake County, California, known as Blue Lakes Ranch (the ranch) through the Michael S. Mountanos Living Trust. Petitioner bought the property for recreational use for his family, such as deer hunting. Except for one small area, Federal land surrounded the ranch. The access roads to the ranch ran through neighboring properties, including Federal land that the Bureau of Land Management (Land Management Bureau) managed. The neighboring property owners granted petitioner easements to pass over their land for purposes of accessing the ranch. [*3] The Land Management Bureau's easement granted limited access to the ranch for single-family use.

The Black Oak Springs Creek traverses the ranch. A permit is required to divert water from the Black Oak Springs Creek for private use. Petitioner did not have the required permit. The ranch also included other springs and two ponds.

The ranch was under a contract (Williamson Act contract) with Lake County that limited the ranch's use and development according to the California Land Conservation Act of 1965 (Williamson Act). Cal. Gov't Code secs. 51200-51297.4 (West 2012). In December 2005, petitioner conveyed a conservation easement on the ranch to Golden State Land Conservancy (Golden State), a California non-profit corporation. The ranch was still subject to the Williamson Act contract when petitioner established the conservation easement on the ranch. Neither the Williamson Act contract nor its terms are part of the record.

II. Tax Returns and Deficiency Notice

Petitioner timely filed an individual Federal income tax return for 2005 claiming a \$4,691,500 charitable contribution deduction for the conservation easement he placed on the ranch. Petitioner could use only \$1,343,704 of the deduction in 2005 because of the limitations of section 170(b)(1)(B). Petitioner [*4] filed returns and claimed a carryover deduction regarding the unused portion for each year at issue.

Respondent issued petitioner a deficiency notice disallowing the claimed carryover deductions. Petitioner timely filed a petition challenging respondent's determination.

OPINION

We must decide whether petitioner is entitled to any portion of the claimed charitable contribution deduction for placing a conservation easement on the undeveloped and rugged land the ranch encompassed. A taxpayer may generally deduct any charitable contribution only if the contribution is verified under regulations the Secretary prescribed. Sec. 170(a)(1). A deduction for a charitable gift of property consisting of less than the donor's entire interest in that property is not generally allowed. Sec. 170(f)(3). An exception to the general rule is provided in the case of a "qualified conservation contribution." Sec. 170(f)(3)(B)(iii).

Respondent does not challenge that the conservation easement was a "qualified conservation contribution." Instead, respondent contends that the value [*5] of the conservation easement was overstated and therefore challenges the amount of the claimed charitable contribution deduction.²

I. Burden of Proof

We begin with the burden of proof. Deductions are a matter of legislative grace, and a taxpayer bears the burden of proving he or she is entitled to any claimed deductions. *INDOPCO, Inc. v. Commissioner*, 503 U.S. 79, 84 (1992). Moreover, the Commissioner's determination of value is

normally presumed correct, and the taxpayer bears the burden of proving that the determination is incorrect. See Rule 142(a); *Welch v. Helvering*, 290 U.S. 111, 115 (1933).

The burden of proof, however, on factual issues that affect the taxpayer's tax liability may shift to the Commissioner where the taxpayer complies with all requirements. Sec. 7491(a). Petitioner does not argue section 7491(a) shifts the burden of proof to respondent. Nor do we find that petitioner met the requirements of section 7491(a). Accordingly, petitioner bears the burden of proof.

[*6] II. Value of the Conservation Easement Placed on the

Ranch

We now consider the value of the conservation easement placed on the ranch. The amount of a charitable contribution of a conservation easement is the fair market value of the conservation easement when contributed. Sec. 1.170A-14(h)(3)(i), Income Tax Regs. The fair market value of a conservation easement is ideally based on the sales prices of comparable easements. Sec. 1.170A-14(h)(3), Income Tax Regs. Comparable sales are rarely available, however, because conservation easements are typically granted by deed or gift rather than sold. *Symington v. Commissioner*, 87 T.C. 892, 895 (1986). As an alternative, the "before-and-after" approach is often used instead. *Stanley Works & Subs. v. Commissioner*, 87 T.C. 389, 399 (1986). The fair market value of a conservation easement under this approach equals the difference between the fair market value of the easement-encumbered property before it is encumbered by the easement and after the easement is established. Sec. 1.170A-14(h)(3)(i) and (ii), Income Tax Regs. The parties agree that there are no sales of comparable easements and that the before-and-after method is the appropriate method to use in valuing the conservation easement.

Fair market value is defined as the "price at which the property would change hands between a willing buyer and a willing seller, neither being under any [*7] compulsion to buy or sell and both having reasonable knowledge of relevant facts." See sec. 1.170A-1(c)(2), Income Tax Regs. The fair market value of property must be evaluated in view of the property's highest and best use. *Stanley Works & Subs. v. Commissioner*, 87 T.C. at 400; sec. 1.170A-14(h)(3)(ii), Income Tax Regs.

A. Highest and Best Use

Accordingly, we now consider the highest and best use of the ranch before and after petitioner established the conservation easement. The highest and best use of the ranch is the highest and most profitable use for which it is adaptable and needed or likely to be needed in the reasonably near future. See *Olson v. United States*, 292 U.S. 246, 255 (1934); see also *Hilborn v. Commissioner*, 85 T.C. 677, 689 (1985). The highest and best use of property can be any realistic, objective potential use of the property. *Symington v. Commissioner*, 87 T.C. at 896. A property's highest and best use is presumed to be the use to which the land is currently being put absent proof to the contrary. See *United States v. L.E. Cooke Co., Inc.*, 991 F.2d 336, 341 (6th Cir. 1993); *Symington v. Commissioner*, 87 T.C. at 896. A proposed highest and best use different from the property's current use requires the taxpayer to demonstrate "closeness in time" and "reasonable probability" of the proposed use. *Hilborn v. Commissioner*, 85 T.C. at 689. [*8] Subsequent events are generally not considered in determining fair market value unless they were reasonably foreseeable on the valuation date. *Estate of Gilford v. Commissioner*, 88 T.C. 38, 52 (1987). We consider existing zoning, historic preservation and other laws and restrictions at the time contributed as well as economic feasibility in evaluating whether a proposed use was reasonably probable and likely in the near future. See, e.g., *Losch v. Commissioner*, T.C. Memo. 1988-230.

Petitioner presented reports and testimony of three expert witnesses to prove the highest and best

use of the ranch before and after he established the conservation easement.³ Petitioner's expert Mark Welch concluded that 287 acres of the ranch were suitable for vineyard use. Petitioner's expert Chris Bell concluded that the highest and best use of the ranch was vineyard use for 287 [*9] acres of it and residential development use for the remaining acreage. Petitioner's expert John Lazaro concluded that the ranch's highest and best use was for vineyard use and "subdivision."⁴ Both Mr. Bell and Mr. Lazaro determined that recreational use was the highest and best use of the ranch after petitioner established the conservation easement. Respondent did not call any expert witnesses. Respondent relied on cross-examination instead. We agree with petitioner's experts that the ranch's highest and best use was recreation after petitioner established the conservation easement. We find, however, that petitioner failed to show that either residential development and vineyard use, as Mr. Bell contends, or subdivision and vineyard use, as Mr. Lazaro contends, was the highest and best use of the ranch before petitioner established the conservation easement. We explain each reason we so find.

1. Vineyard Use

Petitioner failed to show that vineyard use was a legally permissible, physically possible and economically feasible use of the ranch. See the Appraisal [*10] Foundation, Standards of Professional Practice of the Appraisal Institute 154 (1997). More specifically, petitioner failed to demonstrate that the ranch had the necessary legal access for vineyard use. Access to the ranch required a right-of-way easement over Federal land. The Land Management Bureau granted petitioner a right-of-way easement to access the ranch but restricted the easement to "single-family use." Petitioner failed to present evidence showing that it was likely in the near future that the Land Management Bureau would modify the easement to allow access for vineyard use.

Second, petitioner failed to establish that the ranch possessed an adequate water supply for vineyard use. Mr. Welch's determination that there was sufficient water for vineyard use depended on using water from Black Oak Springs Creek. A permit was required, however, to use or divert the Black Oak Springs Creek water for private use. Petitioner lacked a permit. Respondent contends, and petitioner fails to dispute, that petitioner could not have obtained the required permit. In addition, petitioner failed to establish that he had the legal right to use water from other springs that his expert identified as a potential water source. In any event, petitioner failed to show that water from sources on the ranch other than Black Oak Springs was sufficient to support vineyard use.

[*11] Third, petitioner failed to show there was demand for 287 acres of vineyard-suitable property in Lake County. See, e.g., *Hughes v. Commissioner*, T.C. Memo. 2009-94. Mr. Welch and Mr. Bell noted in their reports that other vineyards had been developed in the Lake County area. This does not reveal, however, the demand or market conditions in Lake County for vineyard-suitable property when the conservation easement was placed on the ranch. Moreover, petitioner failed to otherwise introduce persuasive evidence, i.e., objective data and analysis, showing demand for 287 acres of vineyard-suitable property.

Finally, petitioner failed to show that vineyard use was economically feasible. See, e.g., *Losch v. Commissioner*, T.C. Memo. 1988-230. In this regard, the record is devoid of any study supported by data and analysis showing that vineyard use of the ranch would be economically feasible. To be sure, Mr. Welch estimated vineyard development on the ranch would cost \$23,500 per acre. He failed, however, to provide any data or analysis showing how he arrived at this number.

In conclusion, we find that petitioner failed to establish that vineyard use was reasonably probable in the near future so as to affect the value of the ranch when the conservation easement was placed on it.

[*12] 2. Residential Development

We now consider Mr. Bell's contention that the ranch's highest and best use was in part residential development. Mr. Bell opined that the ranch could be subdivided into up to 22 parcels for residential development. Mr. Bell failed to take into account, however, various legal restrictions prohibiting the subdivision of the ranch for residential development.

The Williamson Act contract made the ranch subject to the Williamson Act at the time the conservation easement was placed on the ranch. The Williamson Act's purpose is to preserve agricultural and open space land and to discourage premature urban development. Cal. Gov't Code sec. 51220. The Williamson Act accomplishes this by authorizing local governments to establish agricultural preserves and then to enter into long-term land conservation contracts with landowners within the preserves. Id. secs. 51230-51257.5.

These land conservation contracts limit the land to agricultural and compatible uses for 10 or more years and may also include terms and conditions more restrictive than those the Williamson Act requires. Id. secs. 51240, 51243, subd. (a). Each land conservation contract automatically renews for an additional year absent notice of non-renewal by the landowner or local government. Id. secs. 51244-51246. A contract may be cancelled before it lapses on its own terms only [*13] if certain stringent conditions are met. Id. secs. 51281-51285. The landowner receives preferential property tax rates in return for accepting the restrictions on the development and use of the land. Id. secs. 51240-51244.

The record does not reflect that petitioner or Lake County had given notice of non-renewal with respect to the Williamson Act contract before petitioner established the conservation easement. Additionally, petitioner did not argue or otherwise show that the Williamson Act contract could be cancelled. Accordingly, we consider whether residential development of the ranch would violate the Williamson Act and the Williamson Act contract.

The Williamson Act expressly prohibits the subdivision of land it governs except for transfers to immediate family members and for purposes of agricultural laborer housing. Id. secs. 51230.1, 51230.2. The Williamson Act also prohibits the land it governs from being used as a residential subdivision. Id. sec. 51238.1(a), (c)(4). More generally, the subdivision or use of land the Williamson Act governs for residential development purposes is antithetical to the act's purpose, which is to preserve agricultural and open space land and to prevent its conversion to urban uses. See id. sec. 51220; see also *Sierra Club v. City of Hayward*, 623 P.2d 180, 186 (Cal. 1981). Thus, residential development of the ranch would have violated the Williamson Act.

[*14] Petitioner also failed to show that residential development would not violate the Williamson Act contract. As previously mentioned, a land conservation contract entered into in accordance with the Williamson Act may restrict the use of a property to a greater extent than that provided in the Williamson Act. Cal. Gov't Code secs. 51240, 51243, subd. (a). The Williamson Act contract was not introduced into evidence. Accordingly, petitioner failed to show that the Williamson Act contract permitted the residential development of the ranch (or vineyard use).⁵

Subdividing land subject to the Williamson Act for residential development purposes is also prohibited by section 66474.4(a) of the Subdivision Map Act.

[*15] Cal. Gov't Code. sec. 66410 (West 2009).⁶ That section was amended to require local governments to deny the approval of a tentative map or parcel map for land governed by the Williamson Act in two situations. 1999 Cal. Legis. Serv. ch. 1018 (S.B. 985) (West). The first situation is where parcels following a subdivision of such land would be too small to sustain their

agricultural use. Id. The second situation is where the subdivision of land would “result in residential development not incidental to the commercial agricultural use of the land.”⁷ Id. Additionally, legislative history to the amendment states that it was intended to clarify “that a landowner’s right to subdivide is subject to the Williamson Act * * * and that, therefore, the subdivision of enrolled lands for residential purposes is prohibited by both the Williamson Act and Section 66474.4 of the [California] Government Code”. Id.

[*16] We find that petitioner failed to establish that subdividing the ranch for residential development was a probable use of the ranch in the near future at the time petitioner established the conservation easement.

3. Subdivision

Mr. Lazaro concluded that subdivision was in part the ranch’s highest and best use but did not specify a purpose or use for which the ranch would be subdivided. Like Mr. Bell, Mr. Lazaro failed to take into account that the Williamson Act prohibits subdivision of land except for two narrow exceptions requiring stringent conditions be met. Cal. Gov’t Code secs. 51230.1, 51230.2. Additionally, it is unclear whether the Williamson Act contract would allow the ranch to be subdivided. As discussed, the Williamson Act contract is not in the record and it could have contained more restrictive terms on subdivision than the Williamson Act.⁸ Accordingly, petitioner failed to show that “subdivision” was a reasonably probable use of the ranch in the near future and therefore was not, in part, its highest and best use before he established the conservation easement.

We ultimately find that petitioner failed to show that the before and after highest and best use of the ranch differed.

[*17] B. Before-and-After Analysis

We now consider the fair market value of the ranch. Petitioner contends that the ranch’s fair market value after he established the conservation easement was less than its fair market value before he established the conservation easement. Petitioner’s contention is predicated on the ranch’s losing its potential highest and best uses; i.e., residential development and vineyard use as Mr. Bell contends or subdivision and vineyard use as Mr. Lazaro contends. Because we found that petitioner failed to prove that the ranch’s before and after highest and best use differed, it follows that petitioner also failed to show that the conservation easement diminished the ranch’s after fair market value. Thus, petitioner failed to show that the conservation easement had any value. We hold therefore that petitioner is not entitled to the claimed charitable contribution carryover deductions for the years at issue.

III. Accuracy-Related Penalty

Respondent determined a 40% gross valuation misstatement penalty for each year at issue. A taxpayer may be liable for a 40% penalty on that portion of an underpayment of tax that is attributable to one or more gross valuation misstatements. Sec. 6662(h). A gross valuation misstatement exists if the value or adjusted basis of any property claimed on a tax return is 400% or more of the [*18] amount determined to be the correct amount of such value or adjusted basis.⁹ Sec. 6662(h)(2)(A)(i). The value or adjusted basis of any property claimed on a tax return that is determined to have a correct value or adjusted basis of zero is considered to be 400% or more of the correct amount. Sec. 1.6662-5(g), Income Tax Regs.

Respondent bears the burden of production on the applicability of the accuracy-related penalty in that he must come forward with sufficient evidence indicating that it is proper to impose the penalty.

See sec. 7491(c); see also *Higbee v. Commissioner*, 116 T.C. 438, 446 (2001). Petitioner claimed a \$4,691,500 charitable contribution deduction on his 2005 tax return for the fair market value of the conservation easement conveyed to Golden State. The actual fair market value of the conservation easement, as we previously determined, was zero. Petitioner therefore claimed a value that was 400% or more of the correct amount. We conclude that respondent has met his burden of production.

[*19] A taxpayer generally is not liable for an accuracy-related penalty if the taxpayer acted with reasonable cause and in good faith with respect to any portion of the underpayment. Sec. 6664(c)(1); sec. 1.6664-4(a), Income Tax Regs. The reasonable cause exception does not apply, however, in the case of a gross valuation overstatement with respect to property for which a charitable contribution deduction was claimed under section 170. Sec. 6664(c)(3). Accordingly, we find that petitioner is liable for the gross valuation misstatement penalty for the underpayments for the years at issue.

We have considered all the arguments of the parties, and, to the extent we have not addressed them, we find them to be irrelevant, moot or meritless.

To reflect the foregoing,

Decision will be entered for respondent.

FOOTNOTES

1 All section references are to the Internal Revenue Code in effect for the years at issue, and all Rule references are to the Tax Court Rules of Practice and Procedure, unless otherwise indicated.

2 Respondent also asserts that petitioner did not meet certain substantiation requirements. In particular, he asserts that petitioner did not acquire a “contemporaneous written acknowledgment” from the donee organization or a “qualified appraisal” as required. See sec. 170(f)(8)(A); sec. 1.170A-13(c), Income Tax Regs. We need not address these grounds for disallowing the claimed charitable contribution deduction, nor do we, because of our holding below that petitioner failed to establish that the conservation easement had any value.

3 As the trier of fact, the Court must weigh the evidence the experts presented in light of their demonstrated qualifications in addition to all other credible evidence. *Estate of Christ v. Commissioner*, 480 F.2d 171, 174 (9th Cir. 1973), *aff’d* 54 T.C. 493 (1970). We are not bound by the opinion of any expert witness, especially when that opinion is contrary to our judgment. *Estate of Kreis v. Commissioner*, 227 F.2d 753, 755 (6th Cir. 1955), *aff’d* T.C. Memo. 1954-139; *Chiu v. Commissioner*, 84 T.C. 722, 734 (1985). Rather, we may accept or reject expert testimony as we find appropriate in our best judgment. *Helvering v. Nat’l Grocery Co.*, 304 U.S. 282, 294-295 (1938); *Seagate Tech., Inc. & Consol. Subs. v. Commissioner*, 102 T.C. 149, 186 (1994). Moreover, even if we accept the general methodology of an expert witness, we may reject that expert’s ultimate conclusion if not supported in the record. *Owensby & Kritikos, Inc. v. Commissioner*, 819 F.2d 1315, 1331 (5th Cir. 1987), *aff’d* T.C. Memo. 1985-267.

4 We note that we give little to no weight to Mr. Lazaro’s report and testimony because petitioner failed to establish that he was qualified to appraise real estate. Although Mr. Lazaro has been a real estate broker for a number of years, he does not hold an appraisal designation from a recognized professional appraiser organization. Additionally, the record does not reflect that Mr. Lazaro has any formal training or education in appraising real estate or that he regularly performs real estate appraisals.

5 We note that where a party who has the burden of proof fails to introduce evidence within his control and which, if true, would be favorable to him, it gives rise to a presumption that, if produced, the evidence would be unfavorable. *Wichita Terminal Elevator Co. v. Commissioner*, 6 T.C. 1158, 1165 (1946), *aff'd*, 162 F.2d 513 (10th Cir. 1947). *Wichita Terminal* does not apply, however, where the evidence is equally available to both parties. *Kean v. Commissioner*, 469 F.2d 1183, 1187 (9th Cir. 1972), *aff'g* on this issue, *rev'g* on another issue 51 T.C. 337 (1968); *Dang v. Commissioner*, T.C. Memo. 2002-117. The record reflects that the Williamson Act contract is a public record and thus was equally available to respondent. Accordingly, we do not draw an adverse inference from petitioner's failure to introduce it into evidence. On the other hand, the Court cannot determine that petitioner's proposed residential development use of the ranch complies with the Williamson Act contract.

6 The Subdivision Map Act, Cal. Gov't Code sec. 66410 (West 2009), governs the procedure for subdividing land. A tentative and a final map are required for all subdivisions dividing land into five or more parcels. *Id.* sec. 66426.

7 Petitioner does not claim nor has he shown that any proposed residential development would be incidental to the commercial or agriculture use of the ranch.

8 See *supra* note 7.

9 We note that for returns filed after Aug. 17, 2006, the applicable percentage in sec. 6662(h)(2)(A)(i) was changed from 400% to 200%. See Pension Protection Act of 2006, Pub. L. No. 109-280, sec. 1219(a)(2)(A), 120 Stat. at 1083. The change in percentage does not, however, affect our analysis because the penalty for a gross valuation misstatement applies to any portion of an underpayment for the year to which a deduction is carried that is attributable to a gross valuation misstatement for the year in which the carryover of the deduction arises. Sec. 1.6662-5(c), Income Tax Regs.

IRS LTR: Community Trust, Corporation Treated as Single Entity.

Citations: LTR 201322046

The IRS ruled that a community trust and a state nonprofit corporation that supports the trust's charitable activities will be treated as a single entity and that funds of either organization should be treated as parts of a single-entity community trust.

Contact Person: * * *

Identification Number: * * *

Telephone Number: * * *

Uniform Issue List: 170.19-00

Release Date: 5/31/2013

Date: March 8, 2013

Employer Identification Number: * * *

LEGEND:

Corporation = * * *

Counties = * * *

State = * * *

Foundation = * * *

Date = * * *

Date1 = * * *

Dear * * *:

This letter supersedes our letter dated November 19, 2012, which was in reply to your letter of Date, requesting a ruling that you and Corporation may be treated as a single entity and that funds created within either Foundation or Corporation that otherwise meet the requirements of Treas. Reg. § 1.170A-9(f)(11) (2011) will be treated as component parts of a single entity community trust.

FACTS

You are a community trust created in Date1 to serve the charitable needs of the Counties. You have historically operated as a community trust. You have been recognized as an organization exempt under I.R.C. § 501(c)(3). You are organized pursuant to a Resolution and Declaration of Trust ("trust document").

According to the trust document, you are organized for the purpose of accepting gifts, grants, bequests or devises to be held in trust, the principal or income available for distribution for any charitable, religious, educational, literary, scientific or public welfare to any charitable organization. Your current trustees are certain banks located in Counties.

You have a distribution committee that is composed of representatives of the Counties. Your distribution committee is the board of directors of the Corporation. The distribution committee and the trustee have determined that reorganizing your organization into a joint corporate/trust structure will allow you to attract more contributions and advance your charitable mission.

Accordingly, your distribution committee and trustees formed Corporation, a State nonprofit corporation. The Corporation is operated exclusively for religious, charitable, scientific, literary and educational purposes and to support your charitable activities.

Corporation's original Articles of Incorporation and Bylaws stated that its purpose is to receive money and other property by gift, administer funds, and make distributions for charitable purposes for the benefit of the residents of the Counties. It has been described to the local community as your affiliate since its inception.

According to your trust document and the bylaws of the Corporation all gifts, devises and bequests of property are made subject to the terms and conditions of these documents.

Your trust document and organizing documents of the Corporation require that both organizations be subject to a common governing body. Specifically, the board of directors of the Corporation

serves as the distribution committee of the trust, thus giving the distribution committee control over the Corporation.

Your trust document and Corporation's organizing documents state that all gifts, devises and bequests of property are made subject to the terms and conditions of the resolution. Your distribution committee and board of directors of the Corporation each have the responsibility to ensure that the application and distribution of funds are made exclusively for one or more of your charitable purposes.

Further, your trust document and Corporation's organizing documents each give their boards of directors the power to modify conditions or restrictions concerning the distributions of income and principal for charitable purposes and to remove any trustee that has breached its fiduciary duty or failed to produce a reasonable return of net income.

RULING REQUESTED

You and Corporation may be treated as a single entity; funds of either organization which otherwise meet the requirements of Treas. Reg. § 1.170A-9(f)(11)(ii) should be treated as component parts of a single community trust; that by virtue of the combination of you and Corporation as component parts of a single community trust, the Corporation is included under and takes on all the entitlements of your status as a tax exempt organization under I.R.C. § 501(c)(3); and that you and Corporation as a single community trust, may operate and file a single Form 990 Return of Organization Exempt From Income Tax Return under your E.I.N.

LAW

I.R.C. § 6033 describes the general filing requirements for exempt organizations and in particular specifies certain information required by § 501(c)(3) organizations, in § 6033(b).

Treas. Reg. § 1.170A-9(f)(11)(i) states that any organization that meets the requirements in Treas. Reg. § 1.170A-9(f)(11)(iii) through (vi) will be treated as a single entity, rather than as an aggregation of separate funds. In addition, all funds associated with such organization (whether a trust, not-for-profit corporation, unincorporated association, or a combination thereof), which meet the requirements of Treas. Reg. § 1.170A-9(f)(11)(ii), will be treated as component parts of such organization.

Treas. Reg. 1 170A-9(f)(11)(ii) provides that, to be treated as a component part of a community trust referred to in paragraph (f)(11)(i) of this section, a trust or fund: (A) must be created by gift, bequest, legacy, devise, or other transfer to a community trust which is treated as a single entity under Treas. Reg. § 1.170A-9(f)(11); and (B) may not be directly or indirectly subjected by the transferor to any material restriction or condition with respect to the transferred assets.

Treas. Reg. § 1.170A-9(f)(11)(iii) provides that the organization must be commonly known as a community trust, fund, foundation or other similar name conveying the concept of a capital or endowment fund to support charitable activities in the community or area it serves.

Treas. Reg. § 1.170A-9(f)(11)(iv) provides that all funds of the organization must be subject to a common governing instrument or a master trust or agency agreement, which may be embodied in a single document or several documents containing common language. In addition, if a community trust adopts a new governing instrument (or creates a corporation) to put into effect new provisions (applying to future transfers to the community trust), the adoption of such new governing instrument (or creation of a corporation with a governing instrument) which contains common

language with the existing governing instrument shall not preclude the community trust from meeting the requirements of this paragraph.

Treas. Reg. § 1.170A-9(f)(11)(v) provides: (A) that the organization must have a common governing body or distribution committee, which either directs or monitors the distribution of all the funds exclusively for charitable purposes. In addition, the governing body must have the power in the governing instrument, or other applicable document: (B)(1) to modify any restriction or condition on the distributions of funds for any specified charitable purposes or to specified organizations if in the sole judgment of the governing body, such restriction or condition becomes, in effect, unnecessary, incapable of fulfillment, or inconsistent with the charitable needs of the community or area served; (B)(2) to replace any participating trustee, custodian, or agent for breach of fiduciary duty under state law; and (B)(3) to replace any participating trustee, custodian, or agent for failure to produce a reasonable return of net income over a reasonable period of time.

Treas. Reg. § 1.170A-9(f)(11)(v)(E) provides that the governing body must commit itself to exercise these powers in the best interests of the community trust.

Treas. Reg. § 1.170A-9(f)(11)(v)(F) provides that the governing body must commit itself to obtain information and take other appropriate steps with the view to seeing that each participating trustee, custodian or agent, with respect to each restricted trust or fund that is, and with respect to the aggregate of the unrestricted trusts or funds that are, a component part of the community trust, administers such trust or fund in accordance with the terms of its governing instrument and accepted standards of fiduciary conduct to produce a reasonable return of net income, with due regard to safety of principal, in furtherance of the exempt purposes of the community trust.

Treas. Reg. § 1.170A-9(f)(11)(vi) provides that the organization must prepare periodic financial reports treating all of the funds held by the community trust, either directly or in component parts, as funds of the organization.

Treas. Reg. § 1.170A-9(f)(12)(i) indicates, that those entities which fail to qualify as component parts of a community trust will be treated as a separate entity for purposes of Subchapter A of Chapter 61 of Subtitle F . . . I.R.C. § 6033 if the Form 990 filed annually by the community trust included financial information with respect to such fund and treated such fund in the same manner as other component parts. They will be treated as the entity's separate returns and the first such return filed by the community trust will be treated as the notification required of the separate entity for purposes of § 508(a).

ANALYSIS

Treas. Reg. § 1.170A-9(f)(11)(i) states, in part, that any organization that meets the four requirements in Treas. Reg. § 1.170A-9(f)(11)(iii) through (vi) will be treated as a single entity, rather than as an aggregation of separate funds.

You have been established under the name Foundation for nearly a century. You and Corporation are both named for the community they serve and are commonly known in the community as endowment funds that support charitable activity in that community. Therefore, you meet the requirement of Treas. Reg. § 1.170A-9(f)(11)(iii).

Your trust document and the Corporation's organizing documents state that all gifts, devises and bequests of property are made subject to the terms and conditions of these documents. Therefore, all the donor funds will be subject to a common governing instrument or a master trust or agency agreement, which may be embodied in several documents containing common language, within the

meaning of Treas. Reg. § 1.170A-9(f)(11)(iv). Accordingly, you meet this requirement.

Your trust document and the organizing documents of the Corporation each state that your distribution committee and Board of Directors of the Corporation, which are required to be the same people, have the responsibility to ensure that the application and distribution of funds are made exclusively for one or more of your charitable purposes. Thus, you satisfy the requirement of Treas. Reg. § 1.170A-9(f)(11)(v) that a common governing body monitor the distribution of all funds for charitable purposes.

Your trust document and the organizing documents of the Corporation each give their boards of directors the power to modify conditions or restrictions concerning the distributions of income and principal for charitable purposes and to remove any trustee that has breached its fiduciary duty or for failure to produce a reasonable return of net income. Therefore, you meet the requirement of Treas. Reg. § 1.170A-9(f)(11)(v).

Your trust document and the organizing documents of the Corporation require that each organization prepare annual reports. You have continuously prepared such reports in which you treated your component funds as your funds. Similarly, you expect to report the funds and assets of Corporation as part of a single entity. Therefore, both you and Corporation meet this requirement of Treas. Reg. § 1.170A-9(f)(11)(vi).

Although you and Corporation will continue to be legally separate entities, you will be treated as a single entity rather than as an aggregation of separate funds for federal tax law purposes because you meet the requirements described in Treas. Reg. §§ 1.170A-9(f)(11)(iii) through (vi), as required by Treas. Reg. § 1.170A-9(f)(11)(i),

Once a single entity is identified, the component part provisions of the regulations determine whether a particular fund or trust may be considered part of the single entity. All funds associated with an organization (whether a trust, non-for-profit corporation, unincorporated association or a combination) that are treated as a single entity, and which meet the requirements of Treas. Reg. § 1.170A-9(f)(11)(ii), will be treated as component parts of such organization. Treas. Reg. § 1.170A-9(f)(11)(i).

RULING

Based on your facts and representations:

You and Corporation will be treated as a single entity under Treas. Reg. § 1.170A-9(f)(11)(i). In addition, funds of either such organization which otherwise meet the requirements under Treas. Reg. § 1.170A-9(f)(11)(ii), should be treated as a component parts of a single entity community trust; that by virtue of the combination of you and Corporation as component parts of a single entity community trust, Corporation is included under and takes on all the entitlements of your status as a tax exempt organization under I.R.C. § 501(c)(3); and that you and Corporation as a single entity community trust, operate and file returns under your E.I.N. listed in the heading of this letter.

This ruling will be made available for public inspection under I.R.C. § 6110 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. I.R.C. § 6110(k)(3) 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,

Ronald Shoemaker

Manager, Exempt Organizations

Technical Group 2

[IRS LTR: Multi-Employer Plan With One Non-Church Member Can't Qualify as Church Plan.](#)

Citations: LTR 201323042

The IRS ruled that a multi-employer plan that included at least one employer that was not a tax-exempt church cannot qualify as a church plan under section 414(e) nor can a subsequent plan, as a continuation of the original plan, qualify as a church plan.

U.I.L 414.08-00

Date: March 12, 2013

Refer Reply To: T:EP:RA:T3

LEGEND:

Organization A = * * *

Church B = * * *

Constitution C = * * *

Board D = * * *

Organization E = * * *

Committee F = * * *

Committee G = * * *

Plan X = * * *

Plan Y = * * *

State S = * * *

Dear * * *:

This is in response to correspondence dated March 11, 2005, as supplemented by correspondence dated October 24, 2005, November 23, 2011, February 3, 2012, February 15, 2012, April 24, 2012, May 11, 2012, and May 24, 2012, submitted by you on behalf of Organization A, concerning whether Plan X qualifies as a church plan under section 414(e) of the Internal Revenue Code ("Code").

The following facts and representations have been submitted under penalty of perjury in support of the rulings requested:

Organization A is a tax-exempt entity under section 501(c)(3) of the Code. Its principal offices are located in State S. Church B is a church for purposes of determining church plan status. Constitution C mandates that Organization A meet Church B's requirements for its affiliate organizations.

Board D consists solely of individuals ratified by State S synods of Church B. Board D has the power to adopt resolutions, appoint and remove Organization A's president, approve Organization A's budget, and designate committees to act on behalf of the board.

Constitution C declares Organization A's affiliation with Church B. Church B plays a significant role in governance of Organization A. In addition to Church B's role in the selection of Board D, Organization A's executive committee includes the bishop of the three State S synods of Church B. These synods of Church B provide financial support to Organization A. Organization A is included in a directory of Church B's ministries. Services provided by Organization A are provided as part of the social ministry of Church B.

Organization A has been recognized as an affiliated organization of Church B by annual filings with the Internal Revenue Service ("Service") and is covered under a group ruling issued to Church B.

Organization A adopted Plan X for the benefit of its eligible employees on January 1, 1966. Plan X is a tax-qualified plan under section 401(a) of the Code. It is represented that Plan X does not benefit any Organization A employees engaged in unrelated trade or businesses. Plan X allows various tax-exempt organizations to sponsor Plan X for the benefit of their employees.

The Preamble of Plan X states that Plan X is for the exclusive benefit of the employees (and their beneficiaries) of the plan sponsor and participating agencies, originally effective as of July 1, 1970.

Section 1.1 of Plan X is the definitions section of Plan X. Section 1.1(r) of Plan X states that an "Employer" means the Lead Sponsor and any health or welfare agency that is exempt from taxation under Section 501(c)(3) or 501(c)(4) of the Code which has adopted the Plan as may be provided under Article XV. Section 1.1(kk) defines the "Lead Sponsor" as Organization E and any successor thereto.

Section 15.1 of Plan X states that any health or welfare agency that is exempt from taxation under section 501(c)(3) or 501(c)(4) of the Code that is not an Employer may, with the consent of the Lead Sponsor, adopt and sponsor the Plan for the benefit of its Employees and become an Employer

hereunder by causing an appropriate written instrument evidencing such adoption to be executed in accordance with the requirements of its organizational authority.

Section 16.1 of Plan X states that the Lead Sponsor reserves the right at any time and from time to time, by means of a written instrument executed in the name of the Lead Sponsor by its duly authorized representatives, to amend or modify the Plan and, to the extent provided therein, to amend or modify the funding agreement.

Section 16.2 of Plan X states that if an Employer should disagree with any general amendment made to the Plan by the Lead Sponsor, the Employer shall have 60 days following such amendment in which to notify the Lead Sponsor of its disagreement and its intention either to terminate the Plan with respect to its Employees, as provided in section 16.4, or to withdraw from the Plan and set up its own plan with its own funding arrangement, as provided in section 16.13.

Section 16.3 of Plan X states that the Lead Sponsor reserves the right, by means of a written instrument executed in the name of the Lead Sponsor by its duly authorized representatives, at any time to terminate the Plan. In the event that Lead Sponsor terminates the Plan, each Employer under the Plan must elect either to terminate the Plan with respect to its Employees and proceed as provided in Section 16.4 or to set up its own plan with its own funding arrangement.

Section 16.4 of Plan X states that each employer may, by action of its board of directors or other governing body, elect to terminate the Plan solely with respect to its own Employees and Participants. Except as otherwise provided in section 16.2 or 16.3, such termination may be effectuated only on January 1, or July 1 of any year, and only after the Employer has given the Lead Sponsor at least three months advance notice of its intent to terminate.

On May 11, 2012, your representative sent a letter that included the most recent determination letter for Plan X, the Eighteenth Amendment to the prior plan document, and the current plan document. The Eighteenth Amendment is effective January 1, 1997, and states in relevant part that Plan X is a collection of single employer plans maintained for the exclusive benefit of eligible employers of health or welfare agencies exempt from taxation under section 501(c)(3) or 501(c)(4) of the Code that, with the consent of the Lead Sponsor, adopt and sponsor Plan X for the benefit of their respective employees and their beneficiaries. These employers are set forth on the Schedule of Adopting Employers that immediately precedes Appendix A of Plan X.

The Eighteenth Amendment goes on to state that each adopting employer: (1) maintains a separate single employer plan only with respect to its own respective employees; (2) makes contributions to fund the benefits only of its own employees, which assets are separately accounted for in Pension Fund sub-accounts segregated from any and all other adopting employers' contributions; and (3) has received a separate favorable determination from the Service on the tax-qualified status of its plan.

Prior to March 15, 2005, Board D appointed Committee F to handle functions of Plan X. Committee F consists of members appointed by Board D. Committee F was charged with various tasks related to the funding and administration of Plan X. However, the administration or funding of Plan X was not the principal purpose or function of Committee F.

Effective March 15, 2005, pursuant to a resolution adopted on March 15, 2005 by Board D, Board D appointed Committee G. Committee G consists of three Board D members and two vice-presidents of Organization A. Board D members constitute the majority of Committee G. The principal purpose and function of Committee G is the administration and funding of Plan X. Committee G is responsible for determining which benefits are offered to employees of Organization A, determining how to best provide such benefits, determining the level of benefits provided to the employees of Organization A

and establishing funding policies for Plan X.

Effective January 1, 2010, Plan X, as adopted by Organization A, was restated and renamed Plan Y.

On January 12, 2012, Plan Y filed a statement as part of its amended 2007 Form 5500 filing, electing ERISA coverage pursuant to section 410(d) of the Code, effective January 1, 2007.

In accordance with Revenue Procedure 2011-44, Notice to Employees with reference to Plan X was provided on November 22, 2011. This notice adequately explained to participants of Plan X the consequences of church plan status.

Based on the above facts and representations, you request a ruling that Plan X is a church plan within the meaning of section 414(e) of the Code effective March 15, 2005, and for all prior years of the Plan's operation.

Section 414(e) was added to the Code by section 1015 of ERISA. Section 1017(e) of ERISA provided that section 414(e) applied as of the date of ERISA's enactment. However, section 414(e) was subsequently amended by section 407(b) of the Multiemployer Pension Plan Amendments Act of 1980, Pub. Law 96-364, to provide that section 414(e) was effective as of January 1, 1974.

Section 414(e)(1) of the Code generally defines a church plan as a plan established and maintained for its employees (or their beneficiaries) by a church or a convention or association of churches which is exempt from taxation under section 501 of the Code.

Section 414(e)(2) of the Code provides, in part, that the term "church plan" does not include a plan that is established and maintained primarily for the benefit of employees (or their beneficiaries) of such church or convention or association of churches who are employed in connection with one or more unrelated trades or businesses (within the meaning of section 513 of the Code); or if less than substantially all of the individuals included in the plan are individuals described in section 414(e)(1) of the Code or section 414(e)(3)(B) of the Code (or their beneficiaries).

Section 414(e)(3)(A) of the Code provides that a plan established and maintained for its employees (or their beneficiaries) by a church or a convention or association of churches includes a plan maintained by an organization, whether a civil law corporation or otherwise, the principal purpose or function of which is the administration or funding of a plan or program for the provision of retirement benefits or welfare benefits, or both, for the employees of a church or a convention or association churches, if such organization is controlled by or associated with a church or a convention or association of churches.

Section 414(e)(3)(B) of the Code generally defines "employee" of a church or a convention or association of churches to include a duly ordained, commissioned, or licensed minister of a church in the exercise of his or her ministry, regardless of the source of his or her compensation, and an employee of an organization, whether a civil law corporation or otherwise, which is exempt from tax under section 501 of the Code, and which is controlled by or associated with a church or a convention or association of churches.

Section 414(e)(3)(C) of the Code provides that a church or a convention or association of churches which is exempt from tax under section 501 of the Code shall be deemed the employer of any individual included as an employee under subparagraph (B).

Section 414(e)(3)(D) of the Code provides that an organization, whether a civil law corporation or otherwise, is associated with a church or a convention or association of churches if it shares common religious bonds and convictions with that church or convention or association of churches.

Section 1.414(e)-1(c) of the Federal Income Tax Regulations ("Regulations") states that the term church plan does not include a plan which, during the plan year, is maintained by two or more employers unless each of the employers is a church that is exempt from tax under section 501(a) of the Code. The Regulations also state that the employees of each employer must not be employed by an unrelated trade or business.

Based on the language of Plan X described above, Plan X was a multiple employer plan when it was established and was a multiple employer plan until January 1, 1997, when the Eighteenth Amendment to Plan X provided that Plan X is a collection of single employer plans. Thus, effective January 1, 1997, Plan X is no longer a multiple employer plan, but it cannot become a church plan, because it was not established as a church plan. In addition the Plan, in its current form, Plan Y, cannot be a church plan, because it is merely a continuation of Plan X.

Since Plan X was a multiple employer plan, not all of whose participating employers were church plans when established, it failed to satisfy section 1.414(e)-1(c) of the Regulations which states that the term church plan does not include a plan which, during the plan year, is maintained by two or more employers unless each of the employers is a church that is exempt from tax under section 501(a).

There is at least one employer that had employees that participated in Plan X that was not a church that is exempt from tax under section 501(a). Therefore, we find that neither Plan X nor Plan Y, as a continuation of Plan X, is or can become a church plan.

This letter expresses no opinion as to whether Plan X satisfies the requirements of section 401(a) of the Code.

No opinion is expressed as to the tax treatment of the transaction described herein under the provisions of any other section of either the Code or regulations which may be applicable thereto.

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

A copy of this letter has been sent to your authorized representative in accordance with a power of attorney on file in this office.

If you have any questions regarding this letter, please contact * * *. Please address all correspondence to SE:T:EP:RA:T3.

Sincerely yours,

Laura B. Warshawsky, Manager

Employee Plans Technical Group 3

Enclosures:

Deleted copy of ruling letter

Notice of Intention to Disclose

IRS LTR: IRS Rules on Status of Church Plan, Grantor Trust.

Citations: LTR 201323043

The IRS determined that a plan providing employees and former employees health and life insurance benefits is a church plan, that the trust funding the insurance premium payments is a grantor trust and is not a welfare benefit fund, and that contributions to or premiums paid by the trust are not includable in participants' gross income.

U.I.L: 414.08-00

Date: March 15, 2013

Refer Reply To: T:EP:RA:T2

LEGEND:

Convention B = * * *

Association C = * * *

State A = * * *

Board R = * * *

Denomination D = * * *

Local Denomination D Associations = * * *

Denomination D Associations = * * *

Union W = * * *

Brotherhood P = * * *

Policy J = * * *

Convention G = * * *

Committee O = * * *

Committee N = * * *

Board D = * * *

Plan X = * * *

Resolution H = * * *

Committee U = * * *

Trust T = * * *

Foundation F = * * *

Dear * * *:

This letter is in response to your letter dated December 11, 2003, as supplemented by correspondence dated December 13, 2004, July 8, 2005, August 2, 2005, September 27, 2005, December 1, 2005, November 29, 2006, December 18, 2006, March 1, 2007, and February 23, 2012, submitted on your behalf by your authorized representative regarding the church plan status of Plan X within the meaning of section 414(e) of the Internal Revenue Code (Code). In addition, you have requested rulings under sections 79, 83, 106, 402(b), 419, and 671 of the Code and section 301.7701-4(a) of the Procedure and Administration Regulations (P&A Regulations).

The following facts and representations have been submitted on your behalf:

Convention B was originally incorporated pursuant to State A statutes under the name of Association C in 1852. Association C's name was changed to Convention B on December 20, 19* * *. Article I of Convention B's Amended and Restated Articles of Incorporation provides that Convention B constitutes a body corporate and shall have the full power to institute, pursue, adopt, and carry into effect such measures as to them may be thought best for the promotion of morality, benevolence, and religion, not inconsistent with the laws of State A. Convention B is comprised of and offers services to Denomination D churches across State A. The Local Denomination D Associations are comprised of and offer services to most of the same Denomination D churches but in a regional area of State A. Denomination D member churches of Convention B are also typically members of their Local Denomination D Associations.

Both Convention B and the Local Denomination D Associations have the general purpose of assisting Denomination D member churches in carrying out their mission of evangelism, missions, and ministries and work closely together to promote those ends. The Local Denomination D Associations receive grants and missionary assistance funding from Convention B. Convention B and the Local Denomination D Associations maintain collaborative efforts in training and participation in evangelism/missions and ministries/church development and leadership development and the promotion of the unity and fellowship among and between Denomination D member churches.

Convention B staff often serves as consultants with the local Denomination D associations in helping them with their needs and to develop strategies to meet their perceived needs. As a result of such planning, specific training events are planned and implemented locally, regionally and statewide in which the staff of Convention B and Local Denomination D Associations participate. The consulting work is done on-site, per e-mail, letters or phone calls as needed. The Local Denomination D Association leadership in collaboration with the staff of Convention B negotiate dates, resources, personalities, locations, funding, promotion and other logistics, needed to make such training effective and efficient for mutually desired outcomes in evangelism, missions, ministries and church and leadership development.

Article II of Convention B's Amended and Restated Articles of Incorporation provide that it shall be a medium through which the Denomination D churches, in their sovereign capacity, can work together in promoting all denominational enterprises which they deem necessary in carrying out the Great Commission. Article II further provides that Convention B shall not carry on any activities not permitted to be carried on by a corporation exempt from federal income tax under section 501(c)(3) of the Code.

Convention B receives its funding from the various Denomination D churches throughout State A which are affiliated with and/or working in cooperation with Convention B. It is represented that Denomination D churches that comprise the membership of Convention B are churches as defined in section 414(e)(1) of the Code and are treated as organizations described in section 501(c)(3) of the

Code. It is also represented that the Local Denomination D Associations are organizations described in section 501(c)(3) of the Code.

Article III of Convention B's Amended and Restated Articles of Incorporation provides, in general, that Convention B shall have full power to admit, elect, or appoint its members and officers, to select such times and places for its meetings, and the transaction of its business, and to make such bylaws, rules, and ordinances for its own government. Article III further provides that Convention B shall elect a board of directors to be known as the Executive Board (now called Board R), which shall have charge of the work of Convention B between the meetings, and which shall appoint all officers and agencies that may be required in its work.

Article IV of Convention B's Amended and Restated Articles of Incorporation provides that upon dissolution of Convention B, Board R shall, after paying or making provision for the payment of all liabilities of Convention B, dispose of all of the assets of Convention B exclusively for one or more exempt purposes consistent with the purposes of Convention B.

Convention B's Constitution provides that the membership of Convention B shall consist of messengers from cooperating affiliated Denomination D churches.

Article IV of Convention B's Constitution provides that on the occasion of the annual meeting, the messengers of cooperating Denomination D churches of Convention B shall elect by ballot, a president, a first and second vice president, a secretary and one assistant secretary. The President and the Vice President and Secretaries of Convention B shall be the officers of Board R. Board R members must be members of a Denomination D church for at least one year prior to nomination or appointment.

Article VII of Convention B's Constitution provides, in general, that Board R shall consist of members from each cooperating Denomination D District Association, plus eight at-large members from the geographical regions of State A.

The eight at-large members shall be elected from any cooperating affiliated Denomination D church. These members shall be nominated by Committee O of Convention B. Committee O is one of the governing committees of Convention B.

Members of Board R are elected by Convention B. Any vacancies on Board R not filled at the annual meeting of Convention B or which occur during the year shall be filled by Board R upon recommendation of Committee O. The retiring President of Convention B shall be an at-large member of Board R for one year immediately following his term of office. The president of Union W and the president of Brotherhood P shall serve as ex-officio members of Board R.

Article VIII of Convention B's Constitution provides that Board R shall have charge of the work of Convention B between its sessions, and shall appoint all officers and agencies that may be required in its work.

Article IX provides, in part, that no person shall be eligible for election or appointment until he has been a member of a State A Denomination D church for at least one year prior to nomination or appointment.

The messengers from the cooperating Denomination D churches approve the membership on the various governing committees of Convention B.

On May 6, 20* * * Board R approved an employment policy, Policy J, which sets forth a preferential hiring policy for hiring members of Denomination D churches. Policy J provides that it is the policy

and intent of Convention B from the effective date of this policy to hire and retain for all full-time and professional contract positions, where possible, persons who are members in good standing of Denomination D churches which are affiliated with and/or working in cooperation with Convention B and Convention G. Convention G is described as a cooperative ministry agency serving Denomination D churches on a world-wide basis. Policy J also states that it is the policy of Convention B to expect all of its employees to conduct themselves in a Christ-like manner both on and off the job so that their lives reflect Christian values, and to assist Denomination D members and State A Denomination D churches in their ministry. Policy J further provides that failure to adhere to this conduct standard may result in disciplinary action up to and including termination of employment.

Plan X was established in 19*** by Board R to provide health and life insurance coverage to Convention B's retired employees and has always been maintained by Convention B for such employees. All former employees (i.e., retirees) who meet the applicable eligibility criteria established by Convention B can participate in Plan X and are eligible to receive benefits under Plan X. Currently, as premiums become due, Convention B pays all applicable health and life insurance premiums to Board D of Convention G for retirees (including the missionary/pastor employees whose employment was transferred to the Local Denomination D Associations) from its general assets. Retirees may be required to pay a portion of premiums in the future. Convention G is a vehicle through which its affiliated member conventions can purchase insurance coverage such as the coverage provide for under Plan X.

With respect to Plan X membership, it is represented that the majority of the participants are either employees or former employees (i.e., retirees) of Convention B. It is further represented that there is a group of missionary/pastor employees most of whom, if not all, were employed by Convention B in the 19**s. In 19*** the employment of these missionary/pastor employees was transferred to various Local Denomination D Associations in State A, which share common religious bonds and convictions with Convention B. You state that this group of employees has been grandfathered into Plan X and is a finite group that has not and will not increase in size. There are no other participants in Plan X other than the above described two groups.

You also represent that none of the Plan X participants engage in unrelated trades or businesses within the meaning of section 513 of the Code.

Plan X provides retiree health and life insurance coverage for employees who retire after meeting certain age and service conditions.

Plan X has been historically administered by an informal committee of several employees and officers of Convention B. However, on December *** 20** Board R approved Resolution H that provides that Convention B resolved to amend Plan X to provide that a benefits committee, Committee U shall act as the administrator to maintain and administer Plan X. Committee U shall have the authority to address all administrative issues relating to Plan X including interpreting Plan X provisions. Committee U is comprised of four members who are appointed by Board R and such members may be removed and new members added at any time in the discretion of Board R. All members of Committee U shall share common religious bonds and convictions with Convention B and its related churches. Committee U shall have no activities other than the administration of Plan X and shall meet as often as necessary to administer Plan X.

In connection with Plan X, Convention B has been authorized to establish and fund Trust T. Convention B intends to make a substantial contribution to Trust T to fund future retiree health and life insurance premium payments pursuant to Plan X. Convention B may make future contributions, from time to time, to fund premium costs of Plan X. Convention B, a tax-exempt entity, will not take a

deduction for contributions to Trust T. No employee contributions, if made under Plan X, will be held in Trust T. As retiree health and life insurance premiums become due on a monthly basis, Convention B intends to direct the trustee of Trust T to pay the applicable health and life insurance premiums directly to Board D.

Trust T is intended to be a grantor Trust under section 671 of the Code. Trust T will be revocable. However, Trust T may only be revoked on termination of Plan X or dissolution of Convention B. If Trust T is revoked because of termination of Plan X or dissolution of Convention B, the remaining trust assets may be returned to Convention B provided all obligations under Plan X have been satisfied. Convention B may terminate Plan X at any time.

Participants and their dependents have no preferred claim on, or any beneficial ownership interest in, any Trust T assets, and all rights created under Plan X in Trust T are unsecured contractual rights against Convention B. No benefits or assets under Trust T may be assigned, anticipated, or alienated by participants.

Trust T provides that the principal and income of Trust T are subject to the claims of Convention B's general creditors in the event of insolvency. If Convention B becomes insolvent, the trustee will immediately cease distributions and hold Trust T assets for the benefit of Convention B's creditors.

Foundation F will serve as the trustee of Trust T.

Specifically, Trust T contains the following provisions:

Paragraph 1(b) of Trust T's governing document provides that Trust T shall be revocable by Convention B. However, Convention B may only revoke Trust T upon the termination of Plan X or dissolution of Convention B.

Paragraph 1(c) provides that Trust T is intended to be a grantor trust, of which Convention B is the grantor, within the meaning of subpart E, part I, subchapter J, chapter 1, subtitle A of the Code and shall be construed accordingly.

Paragraph 1(d) provides that the principal of Trust T and any earnings thereon, shall be held separate and apart from other funds of Convention B and shall be used exclusively for the uses and purposes of Plan X participants and general creditors as provided in Trust T's governing document. Plan X participants and their beneficiaries shall have no preferred claim on, or any beneficial ownership interest in, any assets of Trust T. Any rights created under Plan X and Trust T's governing documents shall be mere unsecured contractual rights of the Plan X participants against Convention B.

Paragraph 1(d) also provides that any assets held by Trust T will be subject to the claims of Convention B's general creditors under federal and state law in the event of insolvency of Convention B.

Paragraph 3(a) provides that Convention B will be considered "Insolvent" if (i) Convention B is unable to pay its debts as they become due, or (ii) Convention B is subject to a pending proceeding as a debtor under the United States Bankruptcy Code. This paragraph also provides that the Trustee shall cease payment of insurance benefits on behalf of Plan X participants and their beneficiaries or dependents if Convention B is insolvent.

Paragraph 3(b)(3) provides that if at any time the Trustee has determined that Convention B is insolvent, the Trustee shall discontinue payments under Plan X and shall hold Trust T assets for the benefit of Convention B's general creditors.

Paragraph 4 provides that if Trust T is revoked because of the termination of Plan X or dissolution of Convention B, the remaining Trust T assets may be returned to Convention B provided all of Convention B's obligations under Plan X as of such date have been satisfied.

In its submission for rulings, Convention B has indicated that it plans to request a ruling from the Department of Labor that Plan X is a church plan for purposes of the Employee Retirement Income Security Act (ERISA). Pursuant to ERISA section 4(b)(2), the ERISA Title 1 provisions do not apply to an employee benefit plan that is a church plan with respect to which no election has been made under section 410(d) of the Code.

In a facsimile dated February * * * 20* * * it is represented that the notice required by Revenue Procedure 2011-44 was not issued to participants because Revenue Procedure 2011-44 applies to qualified retirement plans and not to retiree health insurance plans. Plan X is a retiree health and life insurance plan.

Based on the foregoing facts you request the following rulings:

1. That Trust T will be classified as a Trust under section 301.7701-4(a) of the P&A Regulations;
2. That Trust T is a Grantor Trust under section 671 of the Code;
3. That Trust T is not a welfare benefit fund under section 419(e)(1) of the Code;
4. That the contributions to Trust T will not be includible in the Participants' gross income under either section 83 of the Code or section 402(b) of the Code;
5. That the premiums paid under Plan X from Trust T will be excluded from gross income of retirees under sections 106(a) and 79 of the Code to the same extent as if paid directly by Convention B; and
6. That Plan X as described herein is a church plan under section 414(e) of the Code.

With respect to ruling request number one, section 301.7701-4(a) of the P&A Regulations provides that, generally, an arrangement will be treated as a trust if it can be shown that the purpose of the arrangement is to vest in trustees responsibility for the protection and conservation of property for beneficiaries who cannot share in the discharge of the responsibility and, therefore, are not associates in a joint enterprise for the conduct of business for profit.

Section 671 of the Code provides that if the grantor or another person is treated as the owner of any portion of a trust, there shall then be included in computing the taxable income and credits of the grantor or the other person those items of income, deductions, and credits against tax of the trust which are attributable to that portion of the trust to the extent that such items would be taken into account in computing the taxable income or credits against the tax of an individual.

Sections 673 through 677 of the Code specify the circumstances that cause a grantor to be treated as the owner of any portion of a trust.

Section 677(a)(2) of the Code provides that the grantor is treated as the owner of any portion of a trust whose income without the approval or consent of an adverse party is, or in the discretion of the grantor or a non-adverse party, or both, may be distributed or accumulated for future distribution to the grantor.

Section 1.677(a)-1(d) of the Income Tax Regulations (I.T. Regulations) provides that under section 677 of the Code a grantor is treated as the owner of a portion of a trust whose income is, or in the

discretion of the grantor or a non-adverse party or both, may be applied in the discharge of the legal obligation of the grantor.

Section 1.671-2(e)(1) of the I.T Regulations provides that for purposes of subchapter J, a grantor includes any person to the extent such person either creates a trust, or directly or indirectly makes a gratuitous transfer of property to a trust.

In this case, Convention B will transfer assets to Foundation F, the trustee, who will have responsibility for the management, protection, conservation, and investment of the assets. Neither the Plan X participants nor their beneficiaries share in this responsibility. Accordingly, with respect to ruling request number one, we conclude that Trust T will be classified as a trust for federal tax purposes under section 301.7701-4(a) of the P&A Regulations.

With respect to ruling request number two, the purpose of Trust T is to provide benefits to Plan X participants and their beneficiaries. However, if Convention B becomes insolvent, Foundation F has an obligation to cease payments from Trust T and hold Trust T's assets for the benefit of Convention B's creditors. Convention B is the grantor of Trust T because it creates and funds Trust T. As determined in ruling request number three below, and based solely on the facts described herein, Trust T is not a "welfare benefit fund" within the meaning of section 419(e)(1) of the Code. Accordingly, because the principal and income of Trust T can be applied to discharge legal obligations of Convention B, Convention B will be treated as the owner of Trust T under section 671 of the Code and section 1.677(a)-1(d) of the I.T. Regulations.

With respect to ruling request number three, section 419(a) of the Code provides that employer contributions to a welfare benefit plan are not deductible under Chapter 1 of the Code, but if they would otherwise be deductible, then they are deductible (subject to the limitation of section 419(b) of the Code) under section 419 of the Code for the taxable year in which paid.

Section 419(e) of the Code defines "welfare benefit fund" to include any fund that is part of a plan of an employer and through which the employer provides welfare benefits to employees. Section 419(e)(2) of the Code defines "welfare benefit" as any benefit other than a benefit with respect to which section 83(h) of the Code applies, section 404 of the Code applies (determined without regard to section 404(b)(2) of the Code), or section 404A of the Code applies. Section 419(e)(3)(A) of the Code provides that the term "fund" includes any organization described in section 501(c)(9) of the Code. Pursuant to section 419(e)(3)(B) of the Code, the term "fund" also includes any trusts not exempt from tax.

In the present case, Trust T is not exempt from tax. Trust T is subject to claims of Convention B's general creditors in the event of the insolvency of Convention B, and so its assets are not irrevocably set aside, apart from the claims of Convention B's creditors, for the provision of welfare benefits under Plan X. Accordingly, we conclude that Trust T is not a welfare benefit fund within the meaning of section 419(e)(1) of the Code. This conclusion is based on the assumption that Plan X is not subject to the provisions of title 1 of ERISA.

With respect to ruling request number four, section 83 of the Code provides, if, in connection with the performance of services, property is transferred to any person other than the service recipient, the excess of the fair market value of the property, on the first day that the rights to property are either transferable or not subject to substantial risk of forfeiture, over the amount paid for the property is included in the service provider's gross income for the first taxable year in which the rights to the property are either transferable or not subject to a substantial risk of forfeiture.

Section 1.83-3(e) of the I.T. Regulations states that the term "property" includes real and personal

property, other than money or an unfunded and unsecured promise to pay money or property in the future. Thus, a promise to pay money or property in the future is “property” if it is either funded or secured. The term “property” also includes a beneficial interest in assets (including money) that are transferred or set aside from the claims of creditors of the transferor, such as in a trust or escrow account. In the case of a transfer of a life insurance contract, or other contract providing life insurance protection, only cash surrender value of the contract is considered to be property.

Section 1.83-3(a)(1) of the I.T. Regulations states that a “transfer” of property occurs when a person acquires a beneficial interest in the property, disregarding any lapse restriction as defined in section 1.83-3(i) of the I.T. Regulations.

Section 83(c)(1) of the Code states that the rights of a person in property are subject to a substantial risk of forfeiture if the person’s rights to full enjoyment of the property are conditioned on the future performance of services by any individual. Section 1.83-3(c)(1) of the I.T. Regulations further states that whether a risk of forfeiture is substantial or not depends on the facts and circumstances. A substantial risk of forfeiture exists where rights in property that are transferred are conditioned, directly or indirectly, on the future performance (or refraining from performance) of substantial services by any person, or the occurrence of a condition related to the purpose of the transfer, and the possibility of forfeiture is substantial if the condition is not satisfied.

Section 402(b) of the Code generally provides that contributions to an employees’ trust that is not exempt under section 501(a) of the Code are included in the gross income of the employee in accordance with section 83 of the Code except that the value of the employee’s interest in the trust is substituted for the fair market value of the property for purposes of section 83 of the Code.

In this case, Convention B is providing life and health insurance benefits for participants in Plan X and Trust T contains employer contributions for these benefits. However, Trust T is subject to the claims of the general creditors of Convention B. Further, participants in Plan X have no preferred claim on, or any beneficial ownership interest in, Trust T’s assets. Plan X participants may not anticipate, assign, or alienate any of Trust T’s assets. Accordingly, the amounts set aside on behalf of participants in Plan X for life and health benefits are not “property” and there is no “transfer of property” to the participants within the meaning of section 83(a) of the Code.

Based solely on the facts presented, we conclude, with respect to your ruling request number four that the contributions to Trust T will not be includible in the Plan X participants’ gross income under either section 83 of the Code or section 402(b) of the Code.

As to ruling request number five, section 106(a) of the Code provides that the gross income of an employee does not include employer-provided coverage under an accident or health plan.

Section 1.106-1 of the I.T. Regulations states that the gross income of an employee does not include contributions which his employer makes to an accident or health plan for compensation (through insurance or otherwise) to the employee for personal injuries or sickness incurred by the employee, the employee’s spouse, or the employee’s dependents as defined in section 152 of the Code. The employer may contribute to an accident or health plan either by paying the premium on a policy of accident or health insurance covering one or more of the employees or by contributing to a separate trust or fund which provides accident or health benefits directly or through insurance to one or more employees. However, if the insurance policy, trust or fund provides other benefits in addition to accident or health, section 106 of the Code applies only to the portion of the contributions allocable to accident or health benefits.

Revenue Ruling 62-199, 1962-2 C.B. 38, provides that the exclusion under section 106 of the Code

for employer-provided accident or health plan coverage applies to retired employees as well as active employees.

Section 79(a) of the Code generally provides that an employee must include in gross income an amount equal to the cost of group-term life insurance on the life of the employee under a policy (or policies) carried directly or indirectly by his or her employer, but only to the extent that the cost exceeds: (1) the sum of the cost of \$50,000 of insurance; and, (2) the amount, if any, paid by the employee toward the purchase of the insurance.

For purposes of section 79 of the Code, section 79(e) of the Code provides that the term “employee” includes a former employee.

Section 1.79-0 of the I.T. Regulations provides, in part, that a policy of life insurance is “carried directly or indirectly” by an employer if the employer pays any cost of the life insurance directly or through another person.

In this case, Convention B will make contributions to Trust T that will be used by Trust T, in connection with Plan X, to pay premiums for health insurance and life insurance on the lives of Convention B’s retired employees. Retirees are employees for purposes of sections 106 and 79 of the Code. Pursuant to section 1.106-1 of the I.T. Regulations, the health insurance coverage will be provided by the employer since Convention B is paying the cost of health insurance through a separate trust. Pursuant to section 1.79-0 of the I.T. Regulations, the life insurance coverage will be carried directly or indirectly by the employer since Convention B is paying the cost of insurance through Trust T. Thus, the fact that the premiums for retiree health insurance and life insurance are paid to the insurance company by Trust T rather than Convention B does not change the taxation to the retirees under sections 106 and 79 of the Code.

Therefore, based solely on the facts presented, we conclude, with regard to ruling request number five, that the cost of health insurance coverage provided to retired employees of Convention B as a result of premiums paid under Plan X from Trust T will be excluded from gross income of retirees under section 106 of the Code to the same extent as if paid directly by Convention B; and the cost of group term life insurance coverage provided to retired employees of Convention B as a result of premiums paid under Plan X from Trust T will be excluded from the gross income of retirees under section 79 of the Code to the same extent as if paid directly by Convention B.

As to ruling request number six, section 414(e) was added to the Code by section 1015 of ERISA. Section 1017(e) of ERISA provided that section 414(e) of the Code applied as of the date of ERISA’s enactment. However, section 414(e) of the Code was subsequently amended by section 407(b) of the Multiemployer Pension Plan Amendment Act of 1980, Pub. Law 96-364, to provide that section 414(e) of the Code was effective as of January 1, 1974.

Section 414(e)(1) of the Code generally defines a church plan as a plan established and maintained for its employees (or their beneficiaries) by a church or by a convention or association of churches which is exempt from taxation under section 501 of the Code.

Section 414(e)(2) of the Code provides, in part, that the term “church plan” does not include a plan that is established and maintained primarily for the benefit of employees (or their beneficiaries) of such church or convention or association of churches who are employed in connection with one or more unrelated trades or businesses (within the meaning of section 513 of the Code); or if less than substantially all of the individuals included in the plan are individuals described in section 414(e)(1) of the Code or section 414(e)(3)(B) of the Code (or their beneficiaries).

Section 414(e)(3)(A) of the Code provides that a plan established and maintained for its employees (or their beneficiaries) by a church or by a convention or association of churches includes a plan maintained by an organization, whether a civil law corporation or otherwise, the principal purpose or function of which is the administration or funding of a plan or program for the provision of retirement benefits or welfare benefits, or both, for the employees of a church or a convention or association of churches, if such organization is controlled by or associated with a church or a convention or association of churches.

Section 414(e)(3)(B) of the Code defines “employee” of a church or a convention or association of churches to include a duly ordained, commissioned, or licensed minister of a church in the exercise of his or her ministry, regardless of the source of his or her compensation, and an employee of an organization, whether a civil law corporation or otherwise, which is exempt from tax under section 501 of the Code, and which is controlled by or associated with a church or a convention or association of churches.

Section 414(e)(3)(C) of the Code provides that a church or a convention or association of churches which is exempt from tax under section 501 of the Code shall be deemed the employer of any individual included as an employee under subparagraph (B).

Section 414(e)(3)(D) of the Code provides that an organization, whether a civil law corporation or otherwise, is associated with a church or a convention or association of churches if the organization shares common religious bonds and convictions with that church or convention or association of churches.

Section 414(e)(3)(E) of the Code provides, in general, that if an employee who is included in a church plan separates from the service of a church or a convention or association of churches or an organization described in clause (ii) of paragraph(3)(B), the church plan shall not fail to meet the requirements of this subsection merely because the plan (i) retains the employee’s accrued benefit or account for the payment of benefits to the employee or his beneficiaries pursuant to the terms of the plan, or (ii) receives contributions on the employee’s behalf after the employee’s separation from service but only for a period of 5 years after such separation, unless the employee is disabled (within the meaning of the disability provisions of the church plan or, if there are no such provisions in the church plan, within the meaning of section 72(m)(7) of the Code) at the time of such separation from service.

In this case, Convention B qualifies as a church or association of churches for purposes of the church plan rules. Additionally, all of the employees that participant in Plan X share the same common bonds and convictions of Denomination D churches, and Convention B is a nonprofit organization described under section 501(c)(3) of the Code which is exempt from tax under section 501(a) of the Code.

Convention B was created to institute, pursue, adopt and carry into effect such measures for the promotion of morality, benevolence and religion consistent with the laws of State A. Convention B receives its funding from various Denomination D churches throughout State A which are affiliated with and/or working in cooperation with Convention B.

To the extent that some participants in Plan X are not employees of Convention B but are employed by Local Denomination D Associations, and in view of the fact that there are common religious bonds between Local Denomination D Associations and Convention B, and that Convention B receives its funding from various Denomination D churches, we conclude that the Local Denomination D Associations are associated with a church or a convention or association of churches within the meaning of section 414(e)(3)(D) of the Code, that the employees of the Local Denomination D

Associations meet the definition of employee under section 414(e)(3)(B) of the Code and that they are deemed to be employees of a church or a convention or association of churches by virtue of being employees of an organization which is exempt from tax under section 501 of the Code and which is controlled by or associated with a church or a convention or association of churches.

In addition, the fact that Convention B may make contributions to Trust T and Trust T will then pay premiums directly under Plan X on behalf of retired employees who may have been retired for over five years does not take away the Plan's status as a church plan because benefits under Plan X fully accrued while the retiree was an active employee and no contributions are made with respect to any periods after the employee's separation from service.

Based on the foregoing facts and representations, with respect to ruling request number six, we conclude that Plan X is a church plan within the meaning of section 414(e) of the Code.

No opinion is expressed as to the tax treatment of the transaction described herein under the provisions of any other section of either the Code or regulations, which may be applicable thereto.

This ruling is directed only to the Taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

A copy of this letter ruling is being sent to your authorized representative pursuant to a Power of Attorney on file in this office.

If you have any questions regarding this letter, please contact ***, I.D. Number ***, at ***. Please address all correspondence to SE:T:EP:RA:T3.

Sincerely yours,

Laura B. Warshawsky, Manager

Employee Plans Technical Group 3

IRS LTR: Prep School's Defined Benefit Plan Is Church Plan.

Citations: LTR 201322051

The IRS ruled that a tax-exempt college preparatory school's defined benefit plan is a church plan within the meaning of section 414(e) and has been a church plan since January 1, 1974.

U.I.L 414.08-00

Date: March 8, 2013

Refer Reply To: T:EP:RA:T3

LEGEND:

School S = ***

State A = ***

City P = * * *

Society J = * * *

Year B = * * *

Religion C = * * *

Directory C = * * *

Conference C = * * *

Plan X = * * *

Dear * * *

This is in response to your letters dated, December 11, 2007, November 1, 2011, and January 8, 2013, submitted on your behalf by your authorized representative, in which you request a ruling that Plan X is a church plan described in Section 414(e) of the Internal Revenue Code of 1986, as amended (the "Code").

The following facts and representations have been submitted under penalty of perjury in support of the ruling requested.

School S is a private non-profit college preparatory school formed under the non-profit corporation law of State A. School S was founded in Year B in City P as a Society J secondary school for young men. The governing body of School S is a Board of Trustees which consists of no fewer than 18 or more than 25 members of which no less than one-third plus one shall be members of Society J, which is a religious order of men. The Bylaws of School S provide that the Board of Trustees has the power and authority to (1) appoint or remove the President of School S; (2) approve diplomas, certificates and awards; (3) approve and adopt all major changes or renovations in the educational programs of School S; (4) review and take appropriate action as to the Budget, which shall be submitted to it upon recommendation of the President; (5) institute and promote major fund raising efforts of School S; and (6) authorize any changes in tuition and fees within School S.

The Bylaws of School S provide that the Board of Trustees has the authority to elect the President of School S by a two-thirds majority of the Board of Trustees and by a majority of the members of Society J then on the Board of Trustees, subject to the approval by the Provincial of the Society J Province in which School S is located.

The Bylaws require a vote of a two-thirds majority of the Board of Trustees and a vote of a majority of the members of the Society J then on the Board to approve any action effecting a change in the essential character of School S as a Religion C Society J secondary school.

School S is listed in Directory C and, consequently, is exempt from federal income taxes under section 501 of the Code, pursuant to group rulings issued to Conference C by the Internal Revenue Service (the "IRS").

School S has maintained Plan X, a defined benefit pension plan, since September 15, 19* * *. Plan X covers all employees of School S after their completion of one year of service. None of the eligible participants in Plan X are or can be considered employed in connection with one or more unrelated trades or businesses with the meaning of section 513 of the Code. All the eligible participants are employed by School S. Plan X does not include any employees of for-profit entities.

Prior to May 15, 20***, Plan X was administered by School S. By resolutions adopted on May 15, 20***, the Board of Trustees of School S established a benefits committee (the "Committee"), the sole purpose of which is to have the exclusive authority to control and manage the operation and administration of Plan X as well as any successor retirement plan that the Board may hereafter establish. The resolutions provide that the Board of Trustees shall appoint the members of the Committee, subject to the requirement that at all times the Committee must consist of not less than three members, the majority of whom must be vowed members of Society J. The resolutions further provide that the members of the Committee will serve at the pleasure of and are subject to removal by the Board of Trustees at any time with or without cause.

In accordance with Revenue Procedure 2011-44, Notice to Employees with reference to Plan X was provided on October ***, 20***. This notice explained to participants of Plan X the consequences of church plan status.

You represent that School S has not made an election under Code Section 410(d) to be subject to the provisions of the Code relating to vesting, funding, participation and other standards applicable to other retirement plans.

Based on your submission and the above facts and representations, you request a ruling that Plan X is a church plan, within the meaning of Section 414(e) of the Code, retroactively effective for all prior years that the Plan has been in effect.

Section 414(e) was added to the Code by section 1015 of ERISA. Section 1017(e) of ERISA provided that section 414(e) applied as of the date of ERISA's enactment. However, section 414(e) was subsequently amended by section 407(b) of the Multiemployer Pension Plan Amendments Act of 1980, Pub. Law 96-364, to provide that section 414(e) was effective as of January 1, 1974.

Section 414(e)(1) of the Code generally defines a church plan as a plan established and maintained for its employees (or their beneficiaries) by a church or by a convention or association of churches which is exempt from taxation under section 501 of the Code.

Section 414(e)(2) of the Code provides, in part, that the term "church plan" does not include a plan that is established and maintained primarily for the benefit of employees (or their beneficiaries) of such church or convention or association of churches who are employed in connection with one or more unrelated trades or businesses (within the meaning of section 513 of the Code); or if less than substantially all of the individuals included in the plan are individuals described in section 414(e)(1) of the Code or section 414(e)(3)(B) of the Code (or their beneficiaries).

Section 414(e)(3)(A) of the Code provides that a plan established and maintained for its employees (or their beneficiaries) by a church or by a convention or association of churches includes a plan maintained by an organization, whether a civil law corporation or otherwise, the principal purpose or function of which is the administration or funding of a plan or program for the provision of retirement benefits or welfare benefits, or both, for the employees of a church or a convention or association of churches, if such organization is controlled by or associated with a church or a convention or association of churches.

Section 414(e)(3)(B) of the Code defines "employee" of a church or a convention or association of churches to include a duly ordained, commissioned, or licensed minister of a church in the exercise of his or her ministry, regardless of the source of his or her compensation, and an employee of an organization, whether a civil law corporation or otherwise, which is exempt from tax under section 501 of the Code, and which is controlled by or associated with a church or a convention or association of churches.

Section 414(e)(3)(C) of the Code provides that a church or a convention or association of churches which is exempt from tax under section 501 of the Code shall be deemed the employer of any individual included as an employee under subparagraph (B).

Section 414(e)(3)(D) of the Code provides that an organization, whether a civil law corporation or otherwise, is associated with a church or a convention or association of churches if the organization shares common religious bonds and convictions with that church or convention or association of churches.

Revenue Procedure 2011-44, 2011-39 I.R.B. 446, supplements the procedures for requesting a letter ruling under section 414(e) of the Code relating to church plans. The revenue procedure: (1) requires that plan participants and other interested persons receive a notice in connection with a letter ruling request under section 414(e) of the Code for a qualified plan; (2) requires that a copy of the notice be submitted to the IRS as part of the ruling request; and (3) provides procedures for the IRS to receive and consider comments relating to the ruling request from interested persons.

In order for an organization that is not itself a church or a convention or association of churches to have a qualified church plan, it must establish that its employees are employees or deemed employees of a church or convention or association of churches under section 414(e)(3)(B) of the Code by virtue of the organization's control by or affiliation with a church or convention or association of churches. Employees of any organization maintaining a plan are considered to be church employees if the organization: (1) is exempt from tax under section 501 of the Code; and (2) is controlled by or associated with a church or convention or association of churches. In addition in order to be a church plan, the administration or funding (or both) of the plan must be by an organization described in section 414(e)(3)(A) of the Code. To be described in section 414(e)(3)(A) of the Code, an organization must have as its principal purpose the administration or funding of the plan and must also be controlled by or associated with a church or convention or association of churches.

In view of the common religious bonds between School S and Society J, the inclusion of School S in Directory C, and the indirect control of School S by Society J through the Board of Trustees, we conclude that School S is associated with a church or convention or association of churches within the meaning of section 414(e)(3)(D) of the Code, that the employees of School S meet the definition of employee under section 414(e)(3)(B) of the Code, and that they are deemed to be employees of a church or a convention or association of churches by virtue of being employees of an organization which is exempt from tax under section 501 of the Code and which is controlled by or associated with a church or a convention or association of churches.

The administrative control of Plan X is vested in the Committee. The Committee is controlled by and shares common religious bonds with Society J through its control by the Board of Trustees and the common religious bonds of the members of the Committee with Society J. The sole purpose of the Committee is to have exclusive authority to control and manage the operation and administration of Plan X as well as any successor retirement plan that the Board of Trustees may hereafter establish. Thus, the administration of Plan X satisfies the requirements regarding church plan administration under section 414(e)(3)(A) of the Code.

Accordingly, in regard to your ruling request, we conclude that Plan X is a church plan as defined in section 414(e) of the Code and has been a church plan since January 1, 1974.

This letter expresses no opinion as to whether Plan X, satisfies the requirements for qualification under section 401(a) of Code.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

No opinion is expressed as to the tax treatment of the transaction described herein under the provisions of any other section of either the Code or regulations which may be applicable thereto.

Pursuant to a power of attorney on file with this office, a copy of this letter ruling is being sent to your authorized representative.

If you have any questions regarding this letter, please contact * * *. Please address all correspondence to SE:T:EP:RA:T3.

Sincerely yours,

Laura B. Warshawsky, Manager

Employee Plans Technical Group 3

Enclosures:

Deleted Copy of Ruling Letter

Notice of Intention to Disclose

FASB Seeks to Improve Reporting of Nonprofit Operations.

The Financial Accounting Standards Board on May 29 took steps to bring more clarity to the ways in which nonprofit entities communicate information about their operations and financial performance.

At a meeting in Norwalk, Conn., Lee Klumpp, a practice fellow at FASB, told the board that the presentation of an intermediate measure of operations could improve a nonprofit entity's ability to "tell its story and promote further comparability among nonprofits." He added that an intermediate operating measure that is based on a "current operating classification scheme" could provide more meaningful information for users of nonprofit financial statements.

The board tentatively decided to define an intermediate operating measure on the basis of a nonprofit entity's mission, which would be based on whether resources are used to carry out an entity's purpose for existence.

Klumpp said the mission of a nonprofit entity is central to how the organization is created, managed, and governed, and how the organization obtains and retains its tax-exempt status with the IRS.

FASB members also agreed that the operating measure should be defined by an availability concept that involves the resources available for the current activities of the nonprofit entity.

Regarding presentation, the board tentatively decided that a nonprofit entity should present in its statement of activities all revenues that are available to support the entity's mission. A board majority favored presenting those revenues on a gross basis before specific amounts are designated for future period operations.

FASB member Lawrence Smith said that presenting operating measures on a gross basis would help

to characterize the decisions made by a nonprofit entity's governing board regarding the funding of future operations. "Those decisions are very important to portray on the face of the financial statements," he added.

According to FASB, the proposed presentation approach would report the amounts of previously unavailable funding resources that an entity's governing board would designate for use in the current reporting period.

[IRS: Revised Publication 3112 IRS e-file Application and Participation.](#)

This publication provides important information for Tax Professionals and Authorized IRS e-file Providers regarding applying and participating in IRS e-file. All participants should read this publication to become familiar with the requirements for continued participation.

This edition of Publication 3112, IRS e-file Application and Participation, replaces the previous edition last revised in March 2009. The IRS communicated most of the changes on its Web site on IRS.gov as they occurred since the last revision of this publication.

The publication is available at:

<http://www.irs.gov/pub/irs-pdf/p3112.pdf>

[IRS Issues Guidance on Empowerment Zone Designation Extensions.](#)

The IRS has issued guidance on how a state or local government amends the nomination of an empowerment zone to provide for a new termination date of December 31, 2013, as provided for by section 1391, as amended by the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, and the American Taxpayer Relief Act of 2012. (Notice 2013-38; 2013-25 IRB 1)

The full notice is available at:

<http://www.irs.gov/pub/irs-drop/n-13-38.pdf>

[IRS Issues Median Gross Income Guidance.](#)

Revenue Procedure 2013-27 provides guidance with respect to the United States and area median gross income figures that are to be used by issuers of qualified mortgage bonds, as defined in § 143(a) of the Internal Revenue Code, and issuers of mortgage credit certificates, as defined in § 25(c), in computing the housing cost/income ratio described in § 143(f)(5).

<http://www.irs.gov/pub/irs-drop/rp-13-27.pdf>

IRS Corrects Errors in Proposed Regs on Community Health Needs Assessment Requirements.

The IRS has corrected errors in the preamble to and in the text of proposed regulations (REG-106499-12) that provide guidance to charitable hospital organizations on the community health needs assessment requirements and related excise tax and reporting obligations.

Community Health Needs Assessments for

Charitable Hospitals; Correction

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1 and 53

[REG-106499-12]

RIN 1545-BL30

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Correction to a notice of proposed rulemaking.

SUMMARY: This document contains corrections to a notice of proposed rulemaking that was published in the Federal Register on Friday, April 5, 2013. The proposed regulations provide guidance to charitable hospital organizations on the community health needs assessment requirements, and related excise tax and reporting obligations, enacted as part of the Patient Protection and Affordable Care Act of 2010. These proposed regulations also clarify the consequences for failing to meet these and other requirements for charitable hospital organizations.

FOR FURTHER INFORMATION CONTACT: Amy F. Giuliano at (202) 622-6070 (not a toll free number).

SUPPLEMENTARY INFORMATION:

Background

The notice of proposed rulemaking (REG-106499-12) that is the subject of these corrections provides guidance to charitable hospital organizations under sections 501(r), 4959, 6012, and 6033 of the Internal Revenue Code.

Need for Correction

As published April 5, 2013 (78 FR 20523), the notice of proposed rulemaking (REG-106499-12) contains errors that may prove to be misleading and are in need of clarification.

Correction of Publication

Accordingly, the notice of proposed rulemaking (REG-106499-12), that was the subject of FR Doc. 2013-07959, is corrected as follows:

1. On page 20523, in the preamble, column 3, under the paragraph heading “Paperwork Reduction Act”, line 3 from the top of the paragraph, the language “Return of Organization Exempt from” is corrected to read “Return of Organization Exempt From”
2. On page 20526, in the preamble, column 2, under the paragraph heading “e. Activities Unrelated to the Operation of a Hospital Facility”, lines 11 and 12 of the first full paragraph, the language “organization operates. Similarly, section 1.501(r)-2 of these proposed regulations” is corrected to read “organization operates. Similarly, § 1.501(r)-2 of these proposed regulations”.
3. On page 20537, in the preamble, column 3, under the paragraph heading “Special Analyses”, line 9 from the top of the page, the language “§ 1.501(r)-3 and § 1.6033-2(a)(2)(ii)(l) of” is corrected to read “Effective/Applicability Dates”, line 9 from the top of the page, the language “§ 1.501(r)-3 and § 1.6033-2(a)(2)(ii)(l) of”.
4. On page 20537, in the preamble, column 3, under the paragraph heading “Special Analyses”, line 3 of the second full paragraph, the language “2(a)(2)(ii)(l) of the regulations requires” is corrected to read “2(a)(2)(ii)(l) of the regulations requires”

§ 1.501(r)-1 [Corrected]

5. On Page 20539, column 1, paragraph (c)(3), the last sentence of the paragraph, the language “In addition, a partnership agreement includes provisions of Federal, state, or local law, as in effect before March 23, 2010, that govern the affairs of the partnership or are considered under such law to be part of the agreement.” is corrected to read “In addition, a partnership agreement includes provisions of federal, state, or local law, as in effect before March 23, 2010, that govern the affairs of the partnership or are considered under such law to be part of the agreement.”

§ 1.6012-3 [Corrected]

6. On page 20543, column 3, paragraph (a)(10) in the heading, the language “Hospital organizations organized as trust with noncompliant hospital facilities.” is corrected to read “Hospital organizations organized as trusts with noncompliant hospital facilities.”.

Alvin Hall

Assistant Director

Legal Processing Division

Associate Chief Counsel

(Procedure and Administration)

Corporation Owned by Indian Tribe Not Exempt From Taxes, Tax Court Holds.

Citations: Uniband Inc. v. Commissioner; 140 T.C. No. 13; No. 4718-06

The Tax Court held that a state-chartered corporation owned by an Indian tribe wasn’t exempt from corporate income tax, that consolidated returns it filed with another corporation the tribe owned were invalid, and that the corporation had to reduce its wage and employee expense deductions by the amount of the Indian employment credits it was entitled to claim.

Uniband Inc., a Delaware corporation, was wholly owned by the Turtle Mountain Band of Chippewa Indians for the years at issue. Uniband filed consolidated returns with another corporation, TMMC, which was also owned by the tribe for the 1995-1998 tax years. The consolidated returns offset Uniband's income with TMMC's losses. The IRS found that the consolidated returns were invalid and that Uniband's tax liability should be calculated separately from TMMC's. The IRS also found that Uniband was entitled to the Indian employment credit under section 45A, which it hadn't claimed. The IRS applied the credit and reduced Uniband's deductions for wages by the amount of the credit. The adjustments resulted in Uniband's liability for tax deficiencies, which it challenged in the Tax Court.

Tax Court Judge David Gustafson rejected Uniband's argument that it was exempt from income tax as an integral part of an Indian tribe. While agreeing that the tribe itself was exempt from income tax, the court found that Uniband was a separate taxable entity. Gustafson explained that the tribe's immunity from tax didn't extend to Uniband, nor was the tribe or Uniband exempt from tax under any treaty, as Uniband had attempted to argue. The court also held that Uniband wasn't entitled to tribal sovereign immunity.

The Tax Court also rejected Uniband's claim that it was entitled to tax exemption based on its similarity to corporations established under section 17 of the Indian Reorganization Act of 1934. The court found that Uniband differed in several ways from section 17 corporations, which are exempt from tax. Gustafson explained that as a state-chartered corporation, Uniband lacked the special relation to the tribe that exists with a section 17 corporation.

The court also found that Uniband wasn't entitled to file a consolidated return with its sister corporation, TMMC, noting that the tribe that owned both corporations was not itself a corporation. The returns were also invalid because the tribe did not file them, consent to them, or report its items on the purported consolidated returns.

The Tax Court agreed with the IRS that Uniband wasn't entitled to deduct all of its wage and employee business expenses under section 162. The court concluded that Uniband's deductions were reduced according to the amount of the section 45A credit it was entitled to claim. The court noted that section 280C(a) disallows a deduction for wages or salaries paid or incurred for the tax year that equal the sum of the credits determined for that year under section 45A. The court declined to interpret section 280C as limiting the deductions to the extent the credits are currently allowed after applying the general business credit limitation under section 38(c)(1).

LTR: IRS Approves Organization's Set-Aside Program.

Citations: LTR 201321028

The IRS approved an organization's set-aside funding program for restoration of a historic building that will be dedicated entirely to the organization's exempt purposes when the work is finished, saying the project can better be accomplished using a set-aside than by making an immediate payment.

Contact Person - ID Number: * * *

Contact Telephone Number: * * *

UIL LIST: 4942.03-07

Release Date: 5/24/2013

Date: December 27, 2012

Employer Identification Number: * * *

LEGEND:

Q = Name of Facility

R = City, State

u = \$ Cost of Project

v = \$ Amount of Set Aside

w = \$ Set-Aside Year 1

x = \$ Set-Aside Year 2

y = \$ Set-Aside Year 3

z = \$ Set-Aside Year 4

Dear * * *

WHY YOU ARE RECEIVING THIS LETTER

This is our response to your September 18, 2012, and your subsequent amendment thereto, requesting approval of a set-aside under Internal Revenue Code section 4942(g)(2). You've been recognized as tax-exempt under section 501(c)(3) of the Code and have been determined to be a private operating foundation under sections 509(a) and 4942(j)(3).

OUR DETERMINATION

Based on the information furnished, your set-aside program is approved under Internal Revenue Code section 4942(g)(2). As required under section 4942(g)(2), the set aside amount must be paid within the 60-month period after the date of the first set-aside.

DESCRIPTION OF SET-ASIDE REQUEST

You previously acquired a historic property, Q, located in R. You propose to restore Q at an estimated total cost of \$u. When you acquired Q, a portion of it was leased out to commercial tenants and the remaining part was vacant. After restoration the building Q, will be dedicated in its entirety to your exempt purposes.

The first floor will be used for orientation space, exhibition space, a gift shop and public space. The second floor will provide office space for various existing functions of your organization, and an exhibition space in the rear. The upper floor will contain exhibition spaces and spaces for organ recitals and receptions. A second exit from Q will also be built to meet a Fire Code requirement.

The project can better be accomplished using a set-aside than by making an immediate payment, because long-term expenditures must be made requiring more than one year's income to assure their continuity. You intend to restore Q using no outside financing. This is a major project

demanding the accumulation of funds in earlier years for expenditure in later years. The predesign and design phases of the project will occupy the initial two years of the set-aside period. The final, construction phase of the project will be carried out in the third, fourth and fifth years of the set-aside period. You have requested an initial set-aside of \$w for the fiscal year ending March 31, 20***, with additions of \$x, \$y, and \$z, for the fiscal years March 31, 20***, March 31, 20*** and March 31, 20***, respectively, the total set-aside requested being \$v. The set aside requested for each year is expected to be sufficient to ensure that you qualify that year as a private operating foundation under section 4942(j)(3).

You expect that the project will be completed by December 31, 20***, and you have affirmed that all the amounts to be set aside will actually be paid within 60 months of the date of the first set-aside.

BASIS FOR OUR DETERMINATION

Internal Revenue Code section 4942(g)(2)(A) states that an amount set aside for a specific project, which includes one or more purposes described in section 170(c)(2)(B), may be treated as a qualifying distribution if it meets the requirements of section 4942(g)(2)(B).

Section 4942(g)(2)(B) of the Code states that an amount set aside for a specific project will meet the requirements of this subparagraph if, at the time of the set-aside, the foundation establishes that the amount will be paid within five years and either clause (i) or (ii) are satisfied.

Section 4942(g)(2)(B)(i) of the Code is satisfied if, at the time of the set-aside, the private foundation establishes that the project can better be accomplished using the set-aside than by making an immediate payment.

Section 4942(j)(3) of the Code requires that private operating foundations must spend at least 85% of its adjusted net income or its minimum investment return, whichever is less, directly for the active conduct of its exempt activities (the income test) in order to remain a private operating foundation.

Section 53.4942(a)-3(b)(1) of the Foundations and Similar Excise Taxes Regulations provides that a private foundation may establish a project as better accomplished by a set-aside than by immediate payment if the set-aside satisfies the suitability test described in section 53.4942(a)-3(b)(2).

Section 53.4942(a)-3(b)(2) of the Foundations and Similar Excise Taxes Regulations provides that specific projects better accomplished using a set-aside include, but are not limited to, projects where relatively long-term expenditures must be made requiring more than one year's income to assure their continuity.

In Revenue Ruling 74-450, 1974-2 C.B. 388, an operating foundation converted a portion of newly acquired land into a public park under a four-year construction contract. The construction contract payments were to be made mainly during the final two years. This constituted a "specific project." The foundation's set-aside of all its excess earnings for four years was treated as a qualifying distribution under Internal Revenue Code section 4942(g)(2).

WHAT YOU MUST DO

Your approved set-aside(s) will be documented on your records as pledges or obligations to be paid by the date specified. The amounts set aside will be taken into account to determine your minimum investment return under Internal Revenue Code section 4942(e)(1)(A), and the income attributable to your set aside(s) will also be taken into account in computing your adjusted net income under section 4942(f) of the Code.

ADDITIONAL INFORMATION

This determination is directed only to the organization that requested it. Internal Revenue Code section 6110(k)(3) provides that it may not be used or cited as a precedent.

Please keep a copy of this letter in your records.

If you have any questions, please contact the person listed in the heading of this letter.

Sincerely,

Holly O. Paz

Director, Exempt Organizations

Rulings and Agreements

LTR: IRS Rules on Transfer of Assets Between Foundations.

Citations: LTR 201321025

The IRS ruled that the transfer of assets from one private foundation to another will not affect either foundation's tax-exempt status, will not give rise to termination taxes or net investment income taxes, will not be an act of self-dealing, and will not constitute a jeopardizing investment

Contact Person: * * *

Identification Number: * * *

Telephone Number: * * *

Uniform Issues List Numbers: 501.03-00, 507.00-00, 507.05-00,
507.06-00, 507.09-00, 512.00-00, 4940.00-00, 4941.04-00, 4942.03-05,
4942.05-00, 4944.00-00, 4945.04-00

Release Date: 5/24/2013

Date: February 27, 2013

Employer Identification Number: * * *

LEGEND:

B = * * *

C = * * *

D = * * *

M = * * *

Dear * * *:

This responds to your letter dated May 31, 2012, in which you requested rulings on the application of Parts I and II of Subchapter F of Chapter 1, I.R.C. §§ 501-509, and Subchapter A of Chapter 42, Subtitle D, §§ 4940-4948, to the transaction described below.

FACTS

M is a trust organized exclusively for charitable purposes, and has been recognized exempt from federal income taxation as an organization described in § 501(c)(3). M is classified as a private non-operating foundation within the meaning of § 509(a). M was created by, and originally funded with a contribution from, B. B and her husband, C, (jointly, the “Founders”), are M’s sole trustees. You stipulate that B is a substantial contributor to M within the meaning of § 507(d)(2)(A), that C is a substantial contributor to M within the meaning of § 507(d)(2)(B)(iii), that B and C are M’s foundation managers within the meaning of § 4946(b), and, consequently, that B and C are disqualified persons with respect to M within the meaning of § 4946(a)(1)(A) and (B).

You are organized as a not-for-profit corporation under state law. You have been recognized exempt from federal income taxation as an organization described in § 501(c)(3), and are classified as a private operating foundation described in § 4942(j)(3). M and you do not share the same tax year. Your officers and directors are B, C, and D. D is an unrelated person who has provided legal services to you, B, C, and M. You stipulate that B is a substantial contributor to you within the meaning of § 507(d)(2)(A), that C is a substantial contributor to you within the meaning of § 507(d)(2)(B)(iii), that B, C, and D are foundation managers with respect to you within the meaning of § 4946(b), that B and C are disqualified persons with respect to you within the meaning of § 4946(a)(1)(A) and (B), and that D is a disqualified person with respect to you within the meaning of § 4946(a)(1)(B).

You represent that the Founders, as M’s sole Trustees and as two of your three directors, effectively control both M and you (collectively, “the Foundations”) within the meaning of §§ 1.482-1(a)(3) and 1.507-3(a)(9)(i).

You represent that both of the Foundations have made timely tax filings on their respective Returns of Organizations Exempt from Income Tax, Forms 990-PF, for all applicable years, and that both have complied with all applicable state filing obligations throughout their respective terms of existence. Neither of the Foundations has undertaken any activities that would be inconsistent with tax-exempt status as a § 501(c)(3) organization, nor made any changes to their respective governing documents since the filing of their Applications for Tax-Exempt Status, Form 1023. There have been no willful repeated acts (or failures to act), nor any willful and flagrant act (or failure to act), within the meaning of § 507(a)(2)(A), with respect to either of the Foundations that would give rise to liability for tax under Chapter 42 of the Code, and neither Foundation has received a notification from the Secretary of the Treasury described in § 507(a)(2)(B). Neither Foundation has previously terminated its status as a private foundation. M has made qualifying distributions in sufficient amount to avoid imposition of excise tax under § 4942. You have made qualifying distributions in connection with the conduct of your exempt mission to qualify as a private operating foundation under § 4942(j)(3).

You represent that all grants made, or to be made, by M prior to the transfer of its remaining assets to you, as described below, have been grants to public charities. You have not made grants to other organizations. Neither Foundation has incurred any “taxable expenditure” within the meaning of § 4945(d), and neither Foundation has previously made any grant or other disposition of funds that would require the exercise of expenditure responsibility within the meaning of § 4945(d)(4)(B).

Under the Declaration of Trust that serves as M's governing instrument, M's trustees are empowered to make distributions in their discretion from Trust income and principal to "Qualified Charitable Recipients" ("QCRs"). QCRs are defined as organizations described in § 170(c)(1) or (2) which are exempt from tax under § 501(c)(3). The Trust instrument makes reference to suggested types of QCR donees, but the Trustees are empowered to make distributions to any charitable organization qualifying as a QCR, without regard to its mission or purposes. You, as an organization described in §§ 170(c)(2) and 501(c)(3), are a QCR within the meaning of M's Trust instrument, and, as such, are eligible under the Trust instrument to receive grants from M. Prior to, and except for, the transfer of its remaining assets to you as described below, all of M's grants have been made or will have been made to unrelated grantees that are treated as public charities under the Code.

Your corporate purposes are described in your Articles of Organization as including "the provision of educational, vocational, social, psychological, and financial assistance to homeless individuals and families," as well as making distributions to other § 501(c)(3) organizations. Since you were first organized, you have provided education and practical job-skills training to disadvantaged persons and those who have suffered displacement from recent economic upheavals with the objective of equipping them to survive in the current economy, to enter or re-enter the work-force, and to lead productive and satisfying lives. You have provided free career development services to unemployed and underemployed individuals, and have offered such individuals skill assessment, career planning, computer training, interview and resume help, financial planning, job search planning, and other assistance.

Over the past several years, the Founders have concluded that the services you provide have been increasingly needed, in part because of the large number of people displaced by recent economic upheaval and recession. The population in need of such services has been underserved by other organizations and the need and demand for the services you provide have increased. At the same time, economic circumstances have made fundraising from third parties more difficult. The Founders have determined that the exempt purposes of both Foundations will be best served by concentrating their efforts and charitable resources on your work and mission, and by eliminating the duplication and administrative burden of operating two separate private foundations.

M's only activities have consisted of grants made to unrelated QCRs, the missions of most of which are unrelated to your mission. The Trustees have determined that the best use of M's remaining charitable funds, in furtherance of its exempt purpose, would be to provide assistance to you in carrying out the activities which form the basis of your exempt purposes. Therefore, the Founders, as Trustees of M and as your Directors, with the concurrence of your third director, have determined that it is in the best interests of both Foundations to contribute all of M's remaining net funds to you, to discontinue any of M's further activities or grants, and to continue to operate you in furtherance of your exempt purposes.

After making some final grants to unrelated public charities, M will transfer all of its remaining assets to you. M's Trustees will reserve a final amount for estimated debts and expenses, including taxes due, if any, under § 4940, and, thereafter, transfer the balance of M's remaining net assets to you (the "Transfer"). The Transfer will involve substantially all of M's net assets, including all accumulated income and undistributed trust principal. Any amounts remaining after the final payment of taxes, expenses, and fees, will also be transferred to you. Following these transfers, M will retain no assets and will cease to operate.

M will file a Form 990-PF for the year of the disposition of its assets. No sooner than at least one day after the Transfer, M's Trustees will provide notice pursuant to § 507(a)(1) to the Manager, Exempt Organizations Determinations, TE/GE, of M's intent to terminate its private foundation status, in the form and manner prescribed by § 1.507-1(b) and other applicable regulations.

Following the Transfer, you will continue to operate as a private operating foundation engaged in the active conduct of activities in furtherance of your exempt purposes. You expect to use the transferred funds as well as your other assets exclusively in furtherance of your exempt purposes. The Founders expect that your qualifying distributions, substantially all in the form of expenditures incurred in carrying out your exempt activities, will continue to exceed your net income and minimum investment returns. You will also take responsibility for all liabilities, if any, under Chapter 42 that may be imposed or in effect with respect to either M or you after the Transfer date.

While you will continue to provide services free of charge, your management has determined that your exempt purposes can be further served by expanding your services to include fee-based training and certification programs in widely-used computer programs. These services have been identified as particularly valuable to your core mission, which is helping displaced and disadvantaged persons acquire the skills needed to obtain meaningful and lasting employment. The fees paid for such services will help you recover the costs of those programs as well as provide a source of revenue to support your ongoing operations and pro bono services.

The legal services with respect to the Transfer will be provided by a law firm in which D is a partner with a profits interest of less than 35%. D, as one of your directors, is a disqualified person with respect to you. You represent that the law firm will charge reasonable fees for the legal services provided in connection with the Transfer, the termination of M and its status as a private foundation, and the application for a private letter ruling. The services provided by the law firm will be limited solely to such services as are reasonably necessary to carrying out the exempt purposes of the Foundations, and shall not be excessive.

RULINGS REQUESTED

You have requested the following rulings:

1. The transfer of substantially all of M's net assets to you (the "Transfer") will not adversely affect the status of M or you as tax-exempt organizations described in § 501(c)(3).
2. The Transfer will be a transfer described in § 507(b)(2).
3. The Transfer will not terminate M's private foundation status and will not cause M to incur any liability for the § 507(c) termination tax.
4. Following the Transfer, M will be eligible to terminate its private foundation status through the "voluntary termination" procedures of § 507(a)(1).
5. Pursuant to § 1.507-7(b)(1), the date for determining the value of M's assets, for purposes of calculating the termination tax under § 507(c), shall be the date proper notification is given, in the manner prescribed in the regulations, of M's intention voluntarily to terminate its private foundations status (hereinafter, "Notice").
6. Provided that such Notice is given at least one day after the Transfer, and at a time when M's net remaining assets are valued at zero dollars (\$0.00), then the amount of termination tax due under § 507(c)(2) upon the termination of M's status as a private foundation shall be zero dollars (\$0.00).
7. Pursuant to § 507(b)(2), you will not be treated as a newly created organization as a result of the Transfer.
8. You, as transferee of substantially all of M's net assets, shall be treated as possessing those attributes and characteristics of M described in subparagraphs (2), (3), and (4) of § 1.507-3(a).

9. The Founders, as the only Trustees of M, and as two of your three Directors, and as foundation managers and substantial contributors of both Foundations, effectively control both Foundations within the meaning of §§ 1.482-1(a)(3) and 1.507-3(a)(9). Accordingly, for purposes of Chapter 42, you, the transferee Foundation, will be treated as though you were M, the transferor Foundation.
10. The Transfer will not be a realization event for M, and will not give rise to any gross investment income or capital gain net income, within the meaning of § 4940, with respect to either M or you.
11. You, as transferee, may use any excess § 4940 tax paid by M, the transferor, to offset your § 4940 tax liability.
12. The Transfer will not constitute self-dealing and will not subject either of the Foundations, or any of their respective officers, directors, or Trustees, as the case may be, to tax under § 4941.
13. The providing of reasonable and necessary legal services with respect to the Transfer by a law firm in which D is a partner, and the payment of reasonable compensation for such services by the Foundations, will not be an act of self-dealing within the meaning of § 4941(d), notwithstanding the status of D as a disqualified person with respect to you.
14. M will not be required to meet the qualifying distribution requirements of § 4942 for the taxable year of the Transfer provided that your distributable amount for the year of the Transfer is increased by M's distributable amount for the year of the Transfer, and M's qualifying distributions made during the taxable year of the Transfer, if any, will be carried over to you, and may be used by you to meet your minimum distribution requirements under § 4942 for the year.
15. The Transfer will not constitute a jeopardizing investment within the meaning of § 4944.
16. The Transfer will not be a taxable expenditure within the meaning of § 4945(d), and there will be no expenditure responsibility requirements that must be exercised under § 4945(d)(4) or (h) with respect to the Transfer.
17. The payment of reasonable legal fees to the attorneys for M and you for services with respect to the Transfer, and the IRS fee for this Private Letter Ruling will not be treated as taxable expenditures within the meaning of § 4945(d)(5).
18. Your operation of state licensed postsecondary career training programs for a fee will not adversely affect your tax-exempt status under § 501(c)(3) or your status as a private operating foundation under § 4942(j)(3).
19. The fees you receive from payments by users for your certification classes will not be considered gross income derived from an unrelated trade or business for purposes of § 512(a)(1).
20. From and after the effective date of the Transfer, you will continue to exist as an organization that is exempt from taxation under § 501(c)(3) and which will qualify as a private operating foundation under § 4942(j)(3).

LAW

I.R.C. § 501(a) exempts from federal income taxation organizations described in § 501(c).

I.R.C. § 501(c)(3) describes organizations organized and operated exclusively for charitable, educational, and other designated exempt purposes.

Treas. Reg. § 1.501(c)(3)-1(d)(3)(i) provides that the term “educational,” as used in § 501(c)(3), includes the instruction and training of the individual for the purpose of improving or developing his capabilities.

I.R.C. § 509(a) provides that an organization described in § 501(c)(3) is a private foundation unless it is described in § 509(a)(1), (2), (3), or (4).

I.R.C. § 507(a) provides that, except as provided in subsection (b), the status of any organization as a private foundation shall be terminated only if (1) it notifies the Secretary of its intent to accomplish such termination, or (2) with respect to such organization, 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, and the Secretary notifies such organization that it is liable for the tax imposed by subsection (c), and either such organization pays the tax (or any portion not abated under subsection (g)) or the entire amount of such tax is abated under subsection (g).

Treas. Reg. § 1.507-1(b)(1) provides that in order for a private foundation to terminate its private foundation status under § 507(a)(1), an organization must submit a statement to the Internal Revenue Service (“Service”) of its intent to terminate its private foundation status under § 507(a)(1). Such statement must set forth in detail the computation and amount of tax imposed under § 507(c). Unless the organization requests abatement of such tax pursuant to § 507(g), full payment of such tax must be made at the time the statement is filed under § 507(a)(1).

I.R.C. § 507(c) imposes an excise tax on each terminating private foundation equal to the lower of the aggregate tax benefit resulting from the § 501(c)(3) status of such foundation, or the value of the net assets of such foundation.

I.R.C. § 507(e) and Treas. Reg. § 1.507-7(a) provide that, for purposes of § 507(c), the value of the net assets shall be determined at whichever time such value is higher: (1) the first day on which action is taken by the organization which culminates in its ceasing to be a private foundation, or (2) the date on which it ceases to be a private foundation.

Treas. Reg. § 1.507-7(b)(1) provides that, in the case of a termination under § 507(a)(1), the date for determining the value of the foundation’s assets for purposes of calculating the termination tax under § 507(c) shall be the date on which the foundation gives the notification described in § 507(a)(1).

I.R.C. § 507(b)(2) provides that, in the case of a transfer of assets of a 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 a newly created organization.

Treas. Reg. § 1.507-3(c)(1) provides that, for purposes of § 507(b)(2), the terms “other adjustment, organization, or reorganization” shall include any partial liquidation or any other significant disposition of assets to one or more private foundations, other than transfers for full and adequate consideration or distributions out of current income.

Treas. Reg. § 1.507-3(c)(2) provides that the term “significant disposition of assets to one or more private foundations” includes any disposition (or series of related dispositions) by a private foundation to one or more private foundations of 25 percent or more of the fair market value of the net assets of the transferor foundation at the beginning of the taxable year in which the transfers occur.

Treas. Reg. § 1.507-1(b)(6) provides that when a foundation transfers all or part of its assets to one or more other private foundations pursuant to a transfer described in § 507(b)(2) and § 1.507-3(c), such transferor foundation will not have terminated its private foundation status under § 507(a)(1).

Treas. Reg. § 1.507-1(b)(7) provides that neither a transfer of all the assets of a private foundation nor a significant disposition of assets by a private foundation shall be deemed to result in a termination of the transferor private foundation under § 507(a) unless the transferor private foundation elects to terminate pursuant to § 507(a)(1) or § 507(a)(2) is applicable.

Treas. Reg. § 1.507-3(d) provides that unless a private foundation voluntarily gives notice pursuant to § 507(a)(1), a transfer of assets described in § 507(b)(2) will not constitute a termination of the transferor's private foundation status under § 507(a)(1).

Treas. Reg. § 1.507-4(b) provides that private foundations which make transfers described in § 507(b)(2) are not subject to the tax imposed under § 507(c) with respect to such transfers unless the provisions of § 507(a) become applicable.

Treas. Reg. § 1.507-3(a)(1) provides that, in the case of a transfer of assets of a private foundation to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization, or reorganization, including a significant disposition of assets to one or more private foundations within the meaning of § 1.507-3(c), the transferee organization shall not be treated as a newly created organization. Rather, the transferee organization shall be treated as possessing those attributes and characteristics of the transferor organization which are described in subparagraphs (2), (3), and (4) of this paragraph.

Treas. Reg. § 1.507-3(a)(2)(i) provides that a transferee organization to which this § 1.507-3(a) applies shall succeed to the aggregate tax benefit of the transferor organization in an amount equal to the amount of such aggregate tax benefit 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 shall be determined at the time of the transfer.

Treas. Reg. § 1.507-3(a)(3) provides that, for purposes of § 507(d)(2), in the event of a transfer of assets described in § 507(b)(2), any person who is a "substantial contributor" (within the meaning of § 507(d)(2)) with respect to the transferor foundation shall be treated as a "substantial contributor" with respect to the transferee foundation, regardless of whether such person meets the \$5,000-two percent test with respect to the transferee organization at any time.

Treas. Reg. § 1.507-3(a)(4) provides that if a private foundation incurs liability for one or more of the taxes imposed under Chapter 42 (or any penalty resulting therefrom) prior to, or as a result of, making a transfer of assets described in § 507(b)(2) to one or more private foundations, in any case where transferee liability applies each transferee foundation shall be treated as receiving the transferred assets subject to such liability to the extent that the transferor foundation does not satisfy such liability.

Treas. Reg. § 1.507-3(a)(5) provides that, except as provided in subparagraph (9) of this paragraph, a private foundation is required to meet the distribution requirements of § 4942 for any taxable year in which it makes a § 507(b)(2) transfer of all or part of its net 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 § 4942(g). However, where the transferor has disposed of all of its assets, the recordkeeping requirements of § 4942(g)(3)(B) shall not apply during any period in which it has no assets. Such requirements are applicable for any taxable year other

than a taxable year during which the transferor has no assets.

Treas. Reg. § 1.507-3(a)(9)(i) provides that if a private foundation transfers all of its net assets to one or more private foundations which are effectively controlled (within the meaning of § 1.482-1A(a)(3)), directly or indirectly, by the same person or persons who effectively control the transferor private foundation, for purposes of Chapter 42 (§ 4940 et seq.) and part II of Subchapter F of Chapter 1 of the Code (§§ 507 through 509), such a transferee private foundation shall be treated as if it were the transferor.

I.R.C. § 511(a)(1) imposes a tax for each taxable year on the unrelated business taxable income (as defined in § 512) of organizations described in § 501(c).

I.R.C. § 512(a)(1) provides that the term “unrelated business taxable income” means the gross income derived by any organization from any unrelated trade or business (as defined in § 513) regularly carried on by it less certain deductions and subject to certain modifications.

I.R.C. § 513(a) provides that the term “unrelated trade or business” means, in the case of an organization subject to the tax imposed by § 511, any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or functions constituting the basis for its exemption under § 501.

Treas. Reg. § 1.513-1(d)(2) provides that a trade or business is “related” to exempt purposes, in the relevant sense only where the conduct of the business activities bears a causal relationship to the achievement of exempt purposes (other than through the production of income); and the trade or business is “substantially related,” for purposes of § 513, only if the causal relationship is a substantial one. Thus, for the conduct of a trade or business from which a particular amount of gross income is derived to be substantially related to purposes for which exemption is granted, the production or distribution of the goods or the performance of the services from which the gross income is derived must contribute importantly to the accomplishment of those purposes. Whether activities productive of gross income contribute importantly to the accomplishment of any purpose for which an organization is granted exemption depends in each case upon the facts and circumstances involved.

I.R.C. § 4940(a) imposes on each private foundation which is exempt from taxation under § 501(a) for the taxable year a tax equal to 2 percent of the net investment income of such foundation for the taxable year.

Rev. Rul. 2002-28, 2002-1 C.B. 941, holds that when a private foundation transfers all of its assets to one or more private foundations in a transfer described in § 507(b)(2) the transfers do not give rise to net investment income and are not subject to tax under § 4940(a). The transferee foundations may use their proportionate share of any excess § 4940 tax paid by the transferor to offset their own § 4940 tax liability.

I.R.C. § 4941(a)(1) imposes a tax on each act of self-dealing between a disqualified person and a private foundation.

I.R.C. § 4946(a)(1) provides that the term “disqualified person,” with respect to a private foundation, includes a person who is —

(A) a substantial contributor to the foundation,

(B) a foundation manager (within the meaning of subsection (b)(1)),

(C) an owner of more than 20 percent of —

(i) the total combined voting power of a corporation,

(ii) the profits interest of a partnership, or

(iii) the beneficial interest of a trust or unincorporated enterprise, which is a substantial contributor to the foundation,

(D) a member of the family of any individual described in subparagraph (A), (B), or (C),

(E) a corporation of which persons described in subparagraph (A), (B), (C), or (D) own more than 35 percent of the combined voting power,

(F) a partnership in which persons described in subparagraph (A), (B), (C), or (D) own more than 35 percent of the profits interest, and

(G) a trust or estate in which persons described in subparagraph (A), (B), (C), or (D) hold more than 35 percent of the beneficial interest.

Treas. Reg. § 53.4946-1(a)(8) provides that, for purposes of § 4941, the term “disqualified person” shall not include any organization described in § 501(c)(3) other than an organization described in § 509(a)(4).

Treas. Reg. § 53.4941(d)-1(b)(4) provides that a transaction between a private foundation and an organization which is not controlled by the foundation (within the meaning of subparagraph (5) of this paragraph) and which is not described in § 4946(a)(1)(E), (F), or (G) because persons described in § 4946(a)(1)(A), (B), (C), or (D) own no more than 35 percent of the total combined voting power or profits or beneficial interest of such organization, shall not be treated as an indirect act of self-dealing between the foundation and such disqualified person solely because of the ownership interest of such persons in such organization.

I.R.C. § 4941(d)(1)(E) provides that the term “self-dealing” includes any direct or indirect payment of compensation (or payment or reimbursement of expenses) by a private foundation to a disqualified person.

I.R.C. § 4941(d)(2)(E) and Treas. Reg. § 53.4941(d)-3(c)(1) provide that the payment of compensation (and the payment or reimbursement of expenses) by a private foundation to a disqualified person for personal services which are reasonable and necessary to carrying out the exempt purpose of the private foundation shall not be an act of self-dealing if the compensation (or payment or reimbursement) is not excessive.

Treas. Reg. § 53.4941(d)-3(c)(2) provides examples illustrating the provisions of § 4941(d)(2)(E). In Example (1), M, a partnership, is a firm of 10 lawyers engaged in the practice of law. A and B, partners in M, serve as trustees to private foundation W and, therefore, are disqualified persons. In addition, A and B own more than 35 percent of the profits interest in M, thereby making M a disqualified person. M performs various legal services for W from time to time as such services are requested. It is concluded that the payment of compensation by W to M shall not constitute an act of self-dealing if the services performed are reasonable and necessary for the carrying out of W’s exempt purposes and the amount paid by W for such services is not excessive.

I.R.C. § 4942(a) imposes a tax on the undistributed income of a private foundation (other than an operating foundation under § 4942(j)(3)) for any taxable year which has not been distributed before

the first day of the second (or any succeeding) taxable year following such taxable year.

I.R.C. § 4942(c) defines “undistributed income” for any taxable year as the amount by which the distributable amount for such taxable year exceeds the qualifying distributions made out of such distributable amount for such taxable year.

I.R.C. § 4942(d) defines “distributable amount” as the amount equal to the sum of the minimum investment return, plus certain other amounts, reduced by the sum of the taxes imposed on such private foundation for the taxable year under subtitle A and § 4940.

I.R.C. § 4942(g)(1)(A) provides that the term “qualifying distribution” means any amount (including that portion of reasonable and necessary administrative expenses) paid to accomplish one or more purposes described in § 170(c)(2)(B), other than a contribution to (i) an organization controlled directly or indirectly by the foundation or by one or more disqualified persons with respect to the foundation, except as provided in paragraph (3), or (ii) a private foundation which is not an operating foundation under § 4942(j)(3), except as provided in paragraph (3).

I.R.C. § 4942(g)(3) provides that the term “qualifying distribution” includes a contribution to a § 501(c)(3) organization described in paragraph (1)(A)(i) or (ii) if —

(A) not later than the close of the first taxable year after its taxable year in which such contribution is received, such organization makes a distribution equal to the amount of such contribution and such distribution is a qualifying distribution (within the meaning of paragraph (1) or (2), without regard to this paragraph) which is treated under subsection (h) as a distribution out of corpus (or would be so treated if such § 501(c)(3) organization were a private foundation which is not an operating foundation), and

(B) the private foundation making the contribution obtains adequate records or other sufficient evidence from such organization showing that the qualifying distribution described in subparagraph (A) has been made by such organization.

I.R.C. § 4942(i) and Treas. Reg. § 53.4942(a)-3(e) provide for a carry-over of the amount by which qualifying distributions during the five preceding taxable years (other than amounts required to be distributed out of corpus under § 4942(g)(3)) have exceeded the distributable amounts for such years.

I.R.C. § 4942(j)(3) provides that, for purposes of § 4942, the term “operating foundation” means any organization —

A. which makes qualifying distributions (within the meaning of paragraph (1) and (2) of subsection (g)) directly for the active conduct of the activities constituting the purpose or function for which it is organized and operated equal to substantially all of the lesser of —

- i. its adjusted net income (as defined in subsection (f), or
- ii. its minimum investment return; (the “income test”) and

B.

- i. substantially more than half of the assets of which are devoted directly to such activities or to functionally related businesses (as defined in paragraph (4)), or to both, or are stock of a corporation

which is controlled by the foundation and substantially all of the assets of which are so devoted (the “assets test”),

ii. which normally makes qualifying distributions (within the meaning of paragraph (1) or (2) of subdivision (g)) directly for the active conduct of the activities constituting the purpose or function for which it is organized and operated in an amount not less than two-thirds of its minimum investment return (as defined in subsection (e)) (the “endowment test”), or

iii. substantially all of the support (other than gross investment income as defined in § 509(e)) of which is normally received from the general public and from 5 or more exempt organizations which are not described in § 4946(a)(1)(H) with respect to each other or the recipient foundation, not more than 25 percent of the support (other than gross investment income) of which is normally received from any one such exempt organization and not more than half of the support of which is normally received from gross investment income (the “support test”).

Notwithstanding the provisions of subparagraph (A), if the qualifying distributions (within the meaning of paragraph (1) or (2) of subsection (g)) of an organization for the taxable year exceed the minimum investment return for the taxable year, clause (ii) of subparagraph (A) shall not apply unless substantially all of such qualifying distributions are made directly for the active conduct of the activities constituting the purpose or function for which it is organized and operated.

Treas. Reg. § 53.4942(b)-1(b)(1) provides, generally, that qualifying distributions are not made by a foundation “directly for the active conduct of activities constituting its charitable, educational, or other similar exempt purpose” unless such qualifying distributions are used by the foundation itself, rather than by or through one or more grantee organizations which receive such qualifying distributions directly or indirectly from such foundation. However, administrative expenses (such as staff salaries and traveling expenses) and other operating costs necessary to conduct the foundation’s exempt activities (regardless of whether they are “directly for the active conduct” of such activities) shall be treated as qualifying distributions expended directly for the active conduct of such exempt activities if such expenses and costs are reasonable in amount. Conversely, administrative expenses and operating costs which are not attributable to exempt activities, such as expenses in connection with the production of investment income, are not treated as qualifying distributions. Expenses attributable to both exempt and nonexempt activities shall be allocated to each such activity on a reasonable and consistently applied basis.

Treas. Reg. § 53.4942(a)-2(d)(4)(i) provides, in part, that where the deductions with respect to property used for a charitable, educational, or other similar exempt purpose exceed the income derived from such property, such excess shall not be allowed as a deduction, but may be treated as a qualifying distribution.

I.R.C. § 4942(j)(4)(A) provides that the term “functionally related business” includes a trade or business which is not an unrelated trade or business (as defined in § 513).

Rev. Rul. 2002-28, 2002-1 C.B. 941, provides that, when a private foundation transfers all of its assets to one or more private foundations in a transfer described in § 507(b)(2), the transfers do not constitute qualifying distributions for the transferor foundation under § 4942. The transferee foundations assume their proportionate share of the transferor foundation’s undistributed income under § 4942 and reduce their own distributable amount for purposes of § 4942 by their proportion share of the transferor’s excess qualifying distributions under § 4942(i).

I.R.C. § 4944(a)(1) imposes a tax on any amount invested by a private foundation in a manner that jeopardizes the carrying out of any of the foundation’s exempt purposes.

Rev. Rul. 2002-28, 2002-1 C.B. 941, holds that, when a private foundation transfers all of its assets to one or more private foundations in a transfer described in § 507(b)(2), the transfers do not constitute investments jeopardizing the transferor foundation's exempt purposes and are not subject to tax under § 4944(a)(1).

I.R.C. § 4945(a)(1) imposes a tax on any "taxable expenditure" made by a private foundation.

I.R.C. § 4945(d)(4) provides that the term "taxable expenditure" includes any amount paid or incurred as a grant to a private non-operating foundation unless the grantor foundation exercises expenditure responsibility with respect to such grant in accordance with § 4945(h).

I.R.C. § 4945(d)(5) provides that the term "taxable expenditure" includes any amount paid or incurred by a private foundation for any purpose other than one specified in § 170(c)(2)(B).

I.R.C. § 4945(h) provides that the expenditure responsibility referred to in § 4945(d)(4) means that a 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 it was made; (2) to obtain full and complete reports from the grantee on how the funds are spent; and (3) to make full and detailed reports with respect to such expenditures to the Secretary.

Rev. Rul. 2002-28, 2001-1 C.B. 941, provides that, when a private foundation transfers all of its assets to one or more private foundations effectively controlled by the same persons that effectively control the transferor, the transferee foundation is treated as the transferor foundation rather than as the recipient of an expenditure responsibility grant. Therefore, there are no expenditure responsibility requirements that must be exercised under § 4945(d)(4) or (h) with respect to the transfers to the transferee foundation. The transferor foundation is required to exercise expenditure responsibility over the transferor's outstanding grants until it disposes of all of its assets. Thereafter, during any period in which the transferor foundation has no assets, the transferor foundation is not required to exercise expenditure responsibility over any outstanding grants. However, the transferor foundation must still meet the § 4945(h) reporting requirements for the outstanding grants for the year in which the transfer was made.

Treas. Reg. § 53.4945-6(b)(1)(v) provides that any payment which constitutes a qualifying distribution under § 4942(g) ordinarily will not be treated as taxable expenditures under § 4945(d)(5).

Treas. Reg. § 53.4945-6(b)(2) provides that any expenditures for unreasonable administrative expenses, including compensation, consultant fees, and other fees for services rendered will ordinarily be taxable expenditures under § 4945(d)(5) unless the foundation can demonstrate that such expenses were paid or incurred in the good faith belief that they were reasonable and that the payment or incurrence of such expenses in such amounts was consistent with ordinary business care and prudence. The determination whether an expenditure is unreasonable shall depend upon the facts and circumstances of the particular case.

ANALYSIS

Issue 1

Whether the transfer of substantially all of M's net assets to you (the "Transfer") would adversely affect the status of either M or you as tax-exempt organizations described in § 501(c)(3).

Both M and you are currently recognized by the Service as organizations described in § 501(c)(3). Section 501(c)(3) describes organizations organized and operated exclusively for charitable,

educational, and other specified exempt purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in, any political campaign on behalf of (or in opposition to) any candidate for public office.

M's exempt purposes include the making of grants to QCRs, which M's trust instrument defines as organizations described in §§ 170(c)(1) and (2) that are entitled to exemption from tax under § 501(c)(3). Furthermore, Articles I.B and VI of M's trust instrument authorize the Trustees, in their discretion, to distribute up to the entire net income and principal of the Trust to such organizations in furtherance of your exempt purposes. You qualify as an organization described in § 170(c)(2) and are exempt from tax under § 501(c)(3). Therefore, you are a QCR and an eligible recipient of trust distributions under M's trust instrument, and the Transfer of all of M's remaining assets to an organization such as you is expressly permitted thereunder.

You are organized for charitable and educational purposes, including the provision of educational, vocational, social, psychological, and financial assistance to homeless individuals and families, and the making of distributions for such or similar purposes to organizations that qualify as exempt organizations under § 501(c)(3). Article IV, paragraph (a)(ii) of your Articles of Organization permits you to "receive contributions from any and all sources." Therefore, the receipt of the transferred funds from M is a permissible action by you under your governing instrument. You intend to utilize these funds in carrying out the activities which constitute the basis of your exempt purposes. No private inurement will result from the receipt of those funds. The founder, B, serves without compensation, and the only persons who will benefit from your activities will be those persons who fall within the charitable class that you were established to serve. Nor will the funds be used for legislative or political activities or for any other purpose that is not in conformity with your exempt purposes.

Since the Transfer is consistent with M's exempt purposes, and since the transferred funds will be used by you exclusively in furtherance of your exempt purposes, the Transfer will have no adverse effect on the qualification of either M or you as organizations described in § 501(c)(3).

Issue 2

Whether the Transfer would be a transfer described in § 507(b)(2).

I.R.C. § 507(b)(2) applies to the transfer of the assets of any private foundation to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization, or reorganization. Section 1.507-3(c)(1) provides that the terms "other adjustment, organization, or reorganization" shall include any partial liquidation or any other significant disposition of assets to one or more private foundations, other than transfers for full and adequate consideration. The term "significant disposition of assets to one or more private foundations" is defined by § 1.507-3(c)(2) as any disposition or series of dispositions where the aggregate value transferred is 25 percent or more of the fair market value of the foundation at the beginning of the taxable year.

M will transfer all of its net remaining assets to you after the payment of certain grants to unrelated QCR's and the payment of final taxes and expenses. After the Transfer is completed, the value of M's assets would be zero dollars (\$0.00). The assets transferred would constitute 100 percent of M's net assets remaining after the payment of its qualifying distributions, debts, expenses, and taxes, and not less than 93 percent of its total assets as of the beginning of the taxable year. Therefore, the Transfer would constitute a "significant disposition of assets" within the meaning of § 1.507-3(c)(2),

and, thus, would qualify as an “other adjustment, organization, or reorganization” within the meaning of § 1.507-3(c)(1). Accordingly, the Transfer would be a transfer described in § 507(b)(2).

Issues 3, 4, 5, and 6

Whether the Transfer would not terminate M’s private foundation status or cause it to incur any liability for the § 507(c) termination tax.

Whether, following the Transfer, M would be eligible to terminate its private foundation status by giving notice to the Service as provided in § 507(a)(1).

Whether, for purposes of calculating the termination tax under § 507(c), the date for determining the value of M’s assets is the date on which it gives the notice described in § 507(a)(1) (“Notice”).

Provided that Notice is given at least one day after the Transfer, and at a time when M’s net remaining assets are valued at Zero Dollars (\$0.00), whether the amount of termination tax due under § 507(c)(2) upon termination of M’s status as a private foundation would be Zero Dollars (\$0.00).

Section 1.507-1(b)(6) provides that when a foundation transfers all or part of its assets to one or more other private foundations pursuant to a transfer described in § 507(b)(2), such transferor foundation will not have terminated its private foundation status under § 507(a)(1). In addition, § 1.507-1(b)(7) provides that neither a transfer of all the assets of a private foundation nor a significant disposition of assets by a private foundation shall be deemed to result in a termination of the transferor private foundation under § 507(a) unless the transferor private foundation elects to terminate pursuant to § 507(a)(1). Furthermore § 1.507-3(d) provides that unless a private foundation voluntarily gives notice pursuant to § 507(a)(1), a transfer of assets described in § 507(b)(2) will not constitute termination of the transferor’s private foundation status under § 507(a)(1). Finally, § 1.507-4(b) provides that a private foundation that makes a transfer described in § 507(b)(2) is not subject to the tax imposed under § 507(c) with respect to such transfer unless the provisions of § 507(a) become applicable.

As discussed under Issue 2, above, the Transfer will constitute a significant distribution of assets described in § 507(b)(2). Further, you have represented that the Secretary has not notified M of any tax imposed by § 507(c) due to any willful or flagrant acts or failures to act. Consequently, the Transfer would not, of itself, terminate M’s private foundation status or subject it to the tax imposed under § 507(c).

Section 507(a)(1) provides that the status of an organization as a private foundation shall be terminated only if such organization notifies the Secretary of its intent to accomplish such termination and such organization pays the tax imposed by § 507(c). Furthermore, § 1.507-1(b)(1) provides that in order for a private foundation to terminate its private foundation status under § 507(a)(1) it must submit a statement to the Internal Revenue Service of its intent to terminate its private foundation status under § 507(a)(1). In M’s situation where there have been no willful repeated acts or failures to act, and no flagrant act or failure to act, which would give rise to taxes and penalties under Chapter 42, M may elect to terminate its private foundation status by notifying the Manager, Exempt Organizations Determinations (TE/GE), of its intent to accomplish such termination and paying any termination tax deemed to be due under § 507(c).

Section 507(c) imposes a tax on a terminating private foundation equal to the lesser of the aggregate tax benefit resulting from its § 501(c)(3) status and the value of its net assets. Section 507(e) and § 1.507-7(a) provide that, for purposes of § 507(c), the value of the net assets shall be determined at

whichever time such value is greater: (1) the first day on which the organization takes action which culminates in its ceasing to be a private foundation, or (2) the date on which it ceases to be a private foundation. Finally, § 1.507-7(b)(1) provides that in the case of a voluntary termination under § 507(a)(1), the date for determining the value of the foundation's assets for purposes of calculating the termination tax under § 507(c) shall be the date on which the foundation gives the notification described in § 507(a)(1). The date for determining the value of M's assets for purposes of calculating its termination tax is the date it gives Notice. If M gives Notice after the Transfer, the value of its assets on the date of the Notice would be Zero Dollars (\$0.00), and, thus, the amount of the § 507(c) termination tax imposed on M would be Zero Dollars (\$0.00).

Issues 7, 8, and 9

Whether, for purposes of §§ 507 through 509, you would be treated as a newly created organization as a result of the Transfer, pursuant to § 507(b)(2).

Whether you, as transferee of substantially all of M's net assets, would be treated as possessing those attributes and characteristics of M, the transferor, described in § 1.507-3(a)(2), (3), and (4).

Since M and you are both effectively controlled by the same persons within the meaning of §§ 1.482-1(a)(3) and 1.507-3(a)(9), whether, for purposes of Chapter 42 (§ 4940 et seq.) and §§ 507 through 509, you, the transferee, would be treated as though you were M, the transferor.

Section 1.507-3(a)(1) provides that in the case of a significant distribution of assets to one or more private foundations within the meaning of § 1.507-3(c) the transferee organization shall not be treated as a newly created organization. Rather, it shall be treated as possessing those attributes and characteristics of the transferor organization which are described in § 1.507-3(a)(2), (3), and (4). Since, as discussed under Issue 2, above, the Transfer would qualify as a "significant distribution of assets" within the meaning of § 1.507-3(c)(2), you would not be treated as a newly created organization as a result of the Transfer. Rather, you would be treated as possessing M's attributes and characteristics described in subparagraphs (2), (3), and (4) of § 1.507-3(a).

Treas. Reg. § 1.507-3(a)(9)(i) provides that if a private foundation transfers all of its net assets to one or more private foundations which are effectively controlled by the same persons which effectively controlled the transferor private foundation, for purposes of Chapter 42 (§ 4940 et seq.), the transferee foundation shall be treated as if it were the transferor. Since you have represented that B and C effectively control both M and you, for purposes of Chapter 42, you would be treated as if you were M.

Issues 10 and 11

Whether the Transfer would give rise to any gross investment income with respect to either M or you or will be subject to tax under § 4940(a).

Whether you, as transferee, may use any excess § 4940 tax paid by M to offset your § 4940 tax liability.

Section 4940(a) imposes an excise tax on a private foundation's net investment income for the taxable year. Rev. Rul. 2002-28 holds that when a private foundation transfers all of its assets to one or more private foundations in a transfer described in § 507(b)(2), the transfers do constitute investments of the transferor and, therefore, do not give rise to net investment income subject to tax under § 4940(a). Thus, the Transfer would not give rise to net investment income subject to tax under § 4940.

Furthermore, Rev. Rul. 2002-28 holds that if the transferor foundation transfers all of its assets to private foundations effectively controlled by the same persons that effectively control the transferor, any excess § 4940 tax paid by the transferor may be used by the transferee to offset its § 4940 tax liability. As you represent that the Foundations are effectively controlled by the same persons, any excess § 4940 tax paid by M may be used by you to offset your § 4940 tax liability.

Issues 12 and 13

Whether the Transfer would constitute an act of self-dealing within the meaning of § 4941(d), or would subject any disqualified person or foundation manager with respect to M or you to the tax imposed under § 4941(a).

Whether the provision by a law firm of reasonable and necessary legal services with respect to the Transfer, or the payment of reasonable compensation for such services by M or you, would constitute acts of self-dealing within the meaning of § 4941(d), notwithstanding the status of D, a disqualified person with respect to you, as a partner in that law firm.

Section 4941(a) imposes an excise tax on each act of self-dealing between a disqualified person and a private foundation. Section 4941 and § 1.507-3(a) determine whether the proposed Transfer of all of M's assets to you would constitute an act of self-dealing between a private foundation and its disqualified persons as defined in § 4946. Under § 53.4946-1(a)(8), a "disqualified person" does not include organizations that are exempt under § 501(c)(3). Therefore, the Transfer of M's assets to you would not be an act of self-dealing because you are recognized by the Service as an organization exempt from tax under § 501(c)(3).

Furthermore, while the payment of compensation, or the payment or reimbursement of expenses by a private foundation to a disqualified person is, generally, an act of self-dealing under § 4941(d)(1)(E), § 4941(d)(2)(E) and § 53.4941(d)-3(c)(1) provide that a payment or reimbursement to a disqualified person for personal services which are reasonable and necessary to carry out the exempt purposes of the private foundation is not an act of self-dealing provided the compensation, payment, or reimbursement is not excessive.

In this case, the law firm is not a disqualified person, so the payment to the law firm for legal services will not be a direct act of self-dealing. Under § 4946(a)(1)(F) a "disqualified person" includes a partnership in which disqualified persons hold more than 35 percent of the profits interests. D is a disqualified person and is a partner of the law firm but holds less than a 35 percent profits interest in the law firm.

The payment will not otherwise be treated as an indirect act of self-dealing benefitting D. Under § 53.4941(d)-1(b)(4) indirect self-dealing will not occur solely as a result of a transaction between a private foundation and an entity in which a disqualified person holds an interest where the entity is not a disqualified person by operation of § 4946(a)(1)(F). Moreover, as Example (1) of § 53.4941(d)-3(c)(2) demonstrates, the payment of compensation by a foundation for legal services does not constitute an act of self-dealing if the services performed are reasonable and necessary for carrying out of the foundation's exempt purposes and the amount paid for such services is not excessive, and you have represented that these requirements will be met.

Issue 14

Whether the Transfer will be a qualifying distribution by M under § 4942.

Whether you will assume M's "undistributed income" (if any) or succeed to M's excess distributions

(if any).

Section 4942(a) generally imposes a tax on the undistributed income of a private foundation (other than an operating foundation under § 4942(j)(3)) for any taxable year which has not been distributed before the first day of the second (or any succeeding) taxable year following such taxable year. Section 4942(c) defines “undistributed income” for any taxable year as the amount by which the distributable amount for such taxable year exceeds the qualifying distributions made out of such distributable amount for such taxable year. Section 4942(g)(1)(A) defines “qualifying distribution” generally as any amount (including that portion of reasonable and necessary administrative expenses) paid to accomplish one or more purposes described in § 170(c)(2)(B), but a qualifying distribution does not include a contribution to an organization controlled directly or indirectly by the foundation or by one or more disqualified persons with respect to the foundation

Section 1.507-3(a)(5) provides that, except as provided in section 1.507-3(a)(9), a private foundation making a transfer described in § 507(b)(2) must satisfy its distribution requirements under § 4942 for the taxable year in which the transfer is made. Section 1.507-3(a)(5) further provides that the transfer will count as a distribution in satisfaction of the transferor foundation’s distribution requirement under § 4942 subject to the provisions of § 4942(g). Section 4942(g) provides that a distribution from one private foundation to another private foundation, where both foundations are effectively controlled by the same persons, will not be treated as a qualifying distribution by the transferor foundation for the purposes of § 4942 except to the extent that the transferee foundation makes one or more distributions that would be qualifying distributions under § 4942(g) (other than a distribution to a controlled foundation) prior to the close of the transferee’s first tax year following the tax year in which it received the transfer and the distributions are treated as being made out of corpus (as if the transferee foundation were not an operating foundation).

Rev. Rul. 2002-28 holds that where, by reason of § 1.507-3(a)(9)(i), a transferee private foundation is treated as though it were the transferor for purposes of § 4942, a transfer to the transferee foundation is not treated as a qualifying distribution of the transferor foundation. Rather, the transferee foundation assumes all obligations with respect to the transferor’s “undistributed income” within the meaning of § 4942(c), if any, and reduces its own distributable amount under § 4942 by the transferor foundation’s excess qualifying distributions under § 4942(i). None of the three situations in Rev. Rul. 2002-28, however, involved an operating foundation.

As discussed under Issues 7, 8, and 9, above, by reason of § 1.507-3(a)(9)(i), you would be treated as if you were M for purposes of Chapter 42, including § 4942. Accordingly, the Transfer to you would not be treated as a qualifying distribution of M. Rather, you would assume M’s obligations with respect to its undistributed income within the meaning of § 4942(c), if any (after taking into account any excess qualifying distribution carryovers that M may have), and M would not be required to meet its qualifying distribution requirements under § 4942 for the taxable year of the Transfer prior to the Transfer. M must file a final Form 990-PF return for the short tax year of its termination. If M has undistributed income for such tax year, you will owe § 4942 tax if you fail, by the end of your tax year following the tax year in which you receive the Transfer, to make qualifying distributions of such amount that would be treated as out of corpus if you were a non-operating foundation. You should provide an attachment to your Form 990-PF showing how you have met this requirement.

If M has excess qualifying distributions that carry over to you, they will be forfeited if you are an operating foundation in the year of the Transfer. Section 53.4942(a)-3(e)(4) (Example (3)) explains that excess qualifying distributions carried forward lapse in their entirety in any year that the private foundation is treated as an operating foundation. Accordingly, if M has any unused excess qualifying distributions that it could have carried forward to a taxable year after the Transfer, and if you are an operating foundation in that year, M’s unused excess qualifying distributions will lapse

and will not be available for your use in any taxable year after the year of the Transfer if you were to cease to be an operating foundation.

Issue 15

Whether the Transfer would constitute a investment jeopardizing M's exempt purposes, or would be subject to tax under § 4944(a)(1).

Section 4944 imposes a tax on any investment that jeopardizes an exempt organization's charitable purposes. Rev. Rul. 2002-28 holds that where a private foundation transfers all of its assets and liabilities to another private foundation, the transfer does not constitute an investment for purposes of § 4944 and, therefore, the transfer does not constitute an investment jeopardizing the transferor foundation's exempt purposes and is not subject to tax under § 4944(a)(1). Therefore, the Transfer would not constitute a jeopardizing investment or subject M to tax under § 4944(a)(1).

Issues 16 and 17

Whether the Transfer would be a taxable expenditure within the meaning of § 4945(d) or would require the exercise of expenditure responsibility under § 4945(d)(4) or (h).

Whether the payment of the IRS fee for this private letter ruling would be treated as a taxable expenditure within the meaning of § 4945(d), or whether payment of reasonable legal fees to the attorneys for M and you to obtain this private letter ruling with respect to the Transfer would be treated a taxable expenditures within the meaning of § 4945(d)(5).

Section 4945 imposes a tax on any "taxable expenditure" made by a private foundation. Section 4945(d)(4) provides that the term "taxable expenditure" includes any amount paid or incurred as a grant to a private non-operating foundation unless the grantor foundation exercises expenditure responsibility with respect to such grant in accordance with § 4945(h).

Rev. Rul. 2002-28 holds that where, by reason of § 1.507-3(a)(9)(i), a transferee foundation is treated as though it were the transferor foundation for purposes of § 4945, the transferee foundation is not treated as the recipient of an expenditure responsibility grant, and no expenditure responsibility requirements must be exercise under § 4945(d)(4) or (h) with respect to the transfer to the transferee foundation.

As discussed under Issues 7, 8, and 9, above, by reason of § 1.507-3(a)(9)(i), you would be treated as if you were M for purposes of Chapter 42, including § 4945. Consequently, the Transfer would not be considered a taxable expenditure under § 4945, and there would be no expenditure responsibility requirements to be exercised under § 4945(d)(4) or (h) with respect to the Transfer.

Section 53.4945-6(b)(1)(v) provides that any payment which constitutes a qualifying distribution under § 4942(g) will not be treated as a taxable expenditure under § 4945(d)(5). Section 4942(g)(1)(A) and § 53.4942(a)-3(a)(2)(i) provide that a qualifying distribution under § 4942(g) includes reasonable and necessary administrative expenses paid to accomplish one or more purposes described in § 170(c)(1) or (2)(B). Administrative expenses incurred in obtaining a ruling from the Service or for legal fees relating to a foundation's exempt purposes are qualifying distributions. On the other hand, § 53.4945-6(b)(2) provides that expenditures for unreasonable administrative expenses, including consultant fees and other fees for services rendered, will ordinarily be taxable expenditures under § 4945(d)(5). The payment of legal fees to the attorneys for M or you and the payment of the IRS fee for this private letter ruling are administrative expenses necessary to the accomplishment of the Foundations' exempt purposes. So long as such payments

are reasonable, the legal fees paid to the attorneys for M and you to obtain a private letter ruling with respect to the Transfer, and the IRS fee paid for this private letter ruling, would not be treated as taxable expenditures within the meaning of § 4945(d)(5).

Issues 18 and 19

Whether the operation by you of state licensed postsecondary career training programs for a fee would adversely affect your tax exempt status under § 501(c)(3) or your status as an operating foundation under § 4942(j)(3).

Whether the fees received by you from the operation of the state licensed postsecondary career training programs would be considered gross income derived from an unrelated trade or business for purposes of § 512(a)(1).

Your exempt purposes, as described in your Articles of Organization, include “the provision of educational, vocational, social, psychological, and financial assistance to homeless individuals and families.” From your beginning, you have provided education and practical job-skills training to disadvantaged persons and those who have suffered displacement from economic upheavals so that they may be better equipped to obtain employment and to lead productive and satisfying lives. You now wish to provide training in software programs widely used by the business community to help displaced persons whose existing skills do not correspond to the current needs of the marketplace.

Providing such training is educational within the meaning of § 1.501(c)(3)-1(d)(3)(a), and contributes importantly to the accomplishment of your exempt purposes of providing educational and vocational assistance to homeless and displaced persons. Thus, such activities amount to a trade or business that is substantially related to the accomplishment of your exempt purposes within the meaning of § 1.513-1(d)(2), and are, therefore, not unrelated trade or business within the meaning of § 513(a). Insofar as the term “functionally related business” under § 4942(j)(4)(A) includes a trade or business which is not an unrelated trade or business, as defined in § 513, the providing of such state-licensed postsecondary career training programs by you would constitute a “functionally related business,” and deductible expenses related thereto in excess of the income from such business would constitute qualifying distributions made directly for the active conduct of activities constituting your exempt function for purposes of qualifying as a private operating foundation under § 4942(j)(3), as provided in § 53.4942(a)-2(d)(4) and § 53.4942(b)-1(b)(1). The operation of state licensed postsecondary career training programs for a fee will not adversely affect your status as an organization described in § 501(c)(3) or your status as a private operating foundation under § 4942(j)(3). Furthermore, since the income derived from such activities would constitute income from a related trade or business, such income would not constitute gross income derived from an unrelated trade or business for purposes of § 512(a)(1).

Issue 20

Whether, following the Transfer, if your qualifying distributions (within the meaning of § 4942(g)(1) or (2)) made directly for the active conduct of the activities constituting your exempt purpose or function were to exceed both your net investment income and your minimum investment return, you will continue to qualify as a private operating foundation within the meaning of § 4942(j)(3).

To qualify as a private operating foundation under § 4942(j)(3), an organization must meet the income test under § 4942(j)(3)(A) and any one of three alternative tests — the assets test under § 4942(j)(3)(B)(i), the endowment test under § 4942(j)(3)(B)(ii), or the support test under § 4942(j)(3)(B)(iii). The income test requires that the organization make qualifying distributions directly for the active conduct of the activities constituting the purpose or function for which it is

organized and operated equal to substantially all of the lesser of (i) its adjusted net income or (ii) its minimum investment return. The endowment test requires qualifying direct distributions of at least two-thirds of the foundation's minimum investment return.

You anticipate, and represent, that, notwithstanding an increase in your assets and income as a result of the Transfer, you will continue to make qualifying direct distributions in excess of both your minimum investment return and your adjusted net income. So long as your qualifying direct distributions continue to exceed both your net investment income and your minimum investment return, you would continue to qualify as a private operating foundation under § 4942(j)(3).

CONCLUSION

In light of the foregoing, we rule as follows:

1. The transfer of substantially all of M's net assets to you (the "Transfer") would not adversely affect the status of either M or you as organizations described in § 501(c)(3).
2. The Transfer would be a transfer described in § 507(b)(2).
3. The Transfer would not terminate M's private foundation status or cause M to incur any liability for the § 507(c) termination tax.
4. Following the Transfer, M would be eligible to terminate its private foundation status by giving notice to the Service as provided in § 507(a)(1).
5. For purposes of calculating the termination tax under § 507(c), the date for determining the value of M's assets would be the date on which it gives the notice described in § 507(a)(1) ("Notice").
6. Provided that Notice is given at least one day after the Transfer, and at a time when M's net remaining assets are valued at Zero Dollars (\$0.00), the amount of termination tax due under § 507(c)(2) upon termination of M's status as a private foundation would be Zero Dollars (\$0.00).
7. For purposes of §§ 507 through 509, you would be treated as a newly created organization as a result of the Transfer, pursuant to § 507(b)(2).
8. You, as transferee of substantially all of M's net assets, would be treated as possessing those attributes and characteristics of M described in § 1.507-3(a)(2), (3), and (4).
9. Since M and you are both effectively controlled by the same persons within the meaning of §§ 1.482-1(a)(3) and 1.507-3(a)(9), for purposes of Chapter 42 (§ 4940 et seq.) and §§ 507 through 509, you, the transferee, would be treated as though you were M, the transferor.
10. The Transfer would not give rise to net investment income and would not be subject to tax under § 4940(a).
11. You, as transferee, may use any excess § 4940 tax paid by M, the transferor, to offset your § 4940 tax liability.
12. The Transfer would not constitute an act of self-dealing within the meaning of § 4941(d), and would not subject any disqualified person or foundation manager with respect to M or you to the tax imposed under § 4941(a).
13. The provision by a law firm of reasonable and necessary legal services with respect to the

Transfer, and the payment of reasonable compensation for such services by M or you, would not constitute acts of self-dealing within the meaning of § 4941(d), notwithstanding the status of D, a disqualified person with respect to you, as a partner in that law firm.

14. The Transfer would not constitute a qualifying distribution by M under § 4942. You would assume M's undistributed income under § 4942 (if any) and be required to make qualifying distributions of such amount treated as distributed out of corpus by the end of your tax year after the tax year in which you receive the Transfer, but excess distributions by M (if any) will not carry over to you, but will lapse in the first year after the Transfer that you qualify as an operating foundation

15. The Transfer would not constitute an investment jeopardizing M's exempt purposes, and would not be subject to tax under § 4944(a)(1).

16. The Transfer would not be a taxable expenditure within the meaning of § 4945(d); consequently there would be no expenditure responsibility requirements to be exercised under § 4945(d)(4) or (h).

17. The payment of the IRS fee for this private letter ruling would not be treated as a taxable expenditure within the meaning of § 4945(d), and payments of reasonable legal fees to the attorneys for M and you to obtain this private letter ruling with respect to the Transfer would not be treated as taxable expenditures within the meaning of § 4945(d) so long as such payments were reasonable.

18. The operation by you of state licensed postsecondary career training programs for a fee would not adversely affect your tax-exempt status under § 501(c)(3) or your status as an operating foundation under § 4942(j)(3).

19. The fees received by you from the operation of state licensed postsecondary career training programs would not be considered gross income derived from an unrelated trade or business for purposes of § 512(a)(1).

20. Following the Transfer, if your qualifying distributions (within the meaning of § 4942(g)(1) or (2)) made directly for the active conduct of the activities constituting your exempt purpose or function were to exceed both your net investment income and your minimum investment return, you would continue to qualify as a private operating foundation under § 4942(j)(3).

This ruling will be made available for public inspection under § 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. I.R.C. § 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,

Peter A. Holiat

Acting Manager,

Exempt Organizations

Technical Group 1

LTR: Scholarship Awards Won't Be Taxable Expenditures.

Citations: LTR 201321029

The IRS ruled that awards made through a private foundation's employer-related scholarship program will not constitute taxable expenditures and will be excludable from the gross income of the recipients if the funds are used for qualified tuition and related expenses.

Contact person - ID number: * * *

Contact telephone number: * * *

UIL: 4945.04-04

Release Date: 5/24/2013

Date: February 27, 2013

Employer Identification Number: * * *

LEGEND:

B = Name

C = Company

D = Location

E = Location

F = Location

p = grade level

v = Number

w = Number range

x = Number

\$y = Dollar amount

Dear * * *:

You asked for advance approval of your employer-related scholarship grant procedures under Internal Revenue Code section 4945(g). This approval is required because you are a private foundation that is exempt from federal income tax. You requested approval of your scholarship program to fund the education of certain qualifying students.

OUR DETERMINATION

We approved your procedures for awarding employer-related scholarships. Based on the information you submitted, and assuming you will conduct your program as proposed, we determined that your procedures for awarding employer-related scholarships meet the requirements of Code section 4945(g)(1). As a result, expenditures you make under these procedures won't be taxable.

Also, awards made under these procedures are scholarship or fellowship grants and are not taxable to the recipients if they use them for qualified tuition and related expenses (subject to the limitations provided in Code section 117(b)).

DESCRIPTION OF YOUR REQUEST

Your letter indicates you will operate an employer-related scholarship program called B. The purpose of B is to provide scholarships for post-secondary education of undergraduate studies to students who are interested in obtaining an education focused on health and wellness related fields. Approximately v children will be eligible to apply and roughly w actual applications are to be received. You will award x non-renewable scholarships annually for \$y each to children of C employees and their subsidiaries. Scholarships will be offered for full-time study at an accredited college or vocational institution of the student's choice.

You will advertise your program by posting application information on your intranet and make annual announcements via company newsletters, e-mail, postings in employee cafeterias or on other bulletin boards to inform employees of the program and timing for the annual application process.

To be eligible, applicants must be graduating high school students or existing college students with a minimum GPA of 3.0 on a 4.0 scale, aged 25 and under and a dependent child of eligible full time employees with one year of employment who intends to attend a qualified post-secondary school. Students outside the United States must be in their final year of upper or higher secondary school or be current technical or university level students.

You define dependent children as biological, step, or legally adopted children living in the employee's household or primarily supported by the employee. Children of a) employees at or above a vice president or p level and above of C or subsidiaries, b) Directors of C, or c) Trustees of your foundation are not eligible to apply.

Interested students must complete the application in English, Spanish or French and mail it along with a copy of current and complete transcripts of grades and any other required documents to the qualified independent third party hired to manage your program. Online transcripts must display the student's name, school name, grade and credit hours earned for each course, and term in which each course was taken. Applicants will receive acknowledgement of receipt of their application. If an acknowledgement is not received within four weeks, applicants may contact the independent third party to verify that the application has been received.

Non-U.S. applicants currently or previously enrolled in an institute of higher education (university) must include their academic record (transcripts of grades) for all higher education course work completed and secondary school credential/diploma/certificate. Current secondary school students and students who have completed less than one year of higher education (university) must include their academic record (transcript of grades) for all secondary education course work completed during the past three years, and results of college entrance academic examinations.

All applicants are responsible for gathering and submitting all necessary information. Applications will be evaluated on the information supplied; therefore, answer all questions as completely as possible. Incomplete applications will not be evaluated. All information received will be considered confidential and is reviewed only by the independent third party management service hired.

Scholarship recipients are selected on the following basis: academic performance, demonstrated leadership and participation in school and community activities, work experience, a statement of career and educational goals and objectives, unusual school and community activities, work experience, unusual personal and family circumstances that have affected school or work achievements, and the applicant appraisal found on page two of the application. Academic evaluation of global applicants will include review of the grade/mark average based on the grading system used in the applicant's country and a review of the results of academic examinations.

Financial need is not considered. However, because sources of funding for higher education vary across the globe, you request applicants from countries outside the United States submit school cost and government subsidy information.

Provided there are qualified applicants, recipients will be selected in proportion to the number of employees in three primary C regions — D, E, and F. The goal is to grant at least one award per region.

The selection committee will be chosen from a qualified independent third party. No relatives of the independent selection committee, or children of C employees that are at a senior level position (Vice President, or equivalent, or above) are eligible to participate in the program. No children of C's board members or your foundation's trustees or disqualified persons will be eligible to participate. In no instance does any officer or employee of C or your foundation play a part in the selection. All applicants agree to accept the selection decisions as final. Applicants will be notified of selection decisions. Not all applicants to the program will be selected as recipients.

The independent third party will process scholarship payments on your behalf. Checks will be mailed to each recipient's home address and will be made payable to the student's school. The award checks will be issued in U.S. currency. If requested, award payments for recipients outside the United States and Canada may be made via wire transfer.

Recipients will have no obligation to you. They are, however, required to notify the independent third party of any changes in address, school enrollment, or other relevant information and to send complete official transcripts when requested. You reserve the right to review the conditions and procedures of this scholarship program and to make a change at any time including termination of the program.

You will (1) arrange to receive and review grantee reports annually and upon completion of the purpose for which the grant was awarded, (2) investigate diversion of funds from their intended purposes, and (3) take all reasonable and appropriate steps to recover the diverted funds, ensure other grant funds held by a grantee are used for their intended purposes, and withhold further payments to grantees until you obtain grantees' assurances that future diversions will not occur and

that grantees will take extraordinary precautions to prevent future diversion from occurring.

You will maintain all records relating to individual grants including information obtained to evaluate grantees, identify a grantee as a disqualified person, establish the amount and purpose of each grant, and establish that you undertook the supervision and investigation of grants described above.

BASIS FOR OUR DETERMINATION

The law imposes certain excise taxes on the taxable expenditures of private foundations (Code section 4945). A taxable expenditure is any amount a private foundation pays as a grant to an individual for travel, study, or other similar purposes. However, a grant that meets all of the following requirements of Code section 4945(g) is not a taxable expenditure.

The foundation awards the grant on an objective and nondiscriminatory basis.

The IRS approves in advance the procedure for awarding the grant.

The grant is a scholarship or fellowship subject to Code section 117(a).

The grant is to be used for study at an educational organization described in Code section 170(b)(1)(A)(ii).

Revenue Procedure 76-47, 1976-2 C.B. 670, provides guidelines to determine whether grants a private foundation makes under an employer-related program to employees or children of employees are scholarship or fellowship grants subject to the provisions of Code section 117(a). If the program satisfies the seven conditions in sections 4.01 through 4.07 of Revenue Procedure 76-47 and meets the applicable percentage tests described in section 4.08 of Revenue Procedure 76-47, we will assume the grants are subject to the provisions of Code section 117(a).

You represented that your grant program will meet the requirements of either the 25 percent or 10 percent percentage test in Revenue Procedure 76-47. These tests require that:

The number of grants awarded to employees' children in any year won't exceed 25 percent of the number of employees' children who were eligible for grants, were applicants for grants, and were considered by the selection committee for grants, or

The number of grants awarded to employees' children in any year won't exceed 10 percent of the number of employees' children who were eligible for grants (whether or not they submitted an application), or

The number of grants awarded to employees in any year won't exceed 10 percent of the number of employees who were eligible for grants, were applicants for grants, and were considered by the selection committee for grants.

You further represented that you will include only children who meet the eligibility standards described in Revenue Procedure 85-51, 1985-2 C.B. 717, when applying the 10 percent test applicable to employees' children.

In determining how many employee children are eligible for a scholarship under the 10 percent test, a private foundation may include only those children who submit a written statement or who meet the foundation's eligibility requirements. They must also satisfy certain enrollment conditions.

You represented that your procedures for awarding grants under this program will meet the

requirements of Revenue Procedure 76-47. In particular:

An independent selection committee whose members are separate from you, your creator, and the employer will select individual grant recipients.

You will not use grants to recruit employees nor will you end a grant if the employee leaves the employer.

You will not limit the recipient to a course of study that would particularly benefit you or the employer.

OTHER CONDITIONS THAT APPLY TO THIS DETERMINATION

This determination only covers the grant program described above. This approval will apply to succeeding grant programs only if their standards and procedures don't differ significantly from those described in your original request.

This determination is in effect as long as your procedures comply with sections 4.01 through 4.07 of Revenue Procedure 76-47 and with either of the percentage tests of section 4.08. If you establish another program covering the same individuals, that program must also meet the percentage test.

This determination applies only to you. It may not be cited as a precedent.

You cannot rely on the conclusions in this letter if the facts you provided have changed substantially. You must report any significant changes to your program to the Cincinnati Office of Exempt Organizations at::

Internal Revenue Service

Exempt Organizations Determinations

P.O. Box 2508

Cincinnati, OH 45201

You cannot award grants to your creators, officers, directors, trustees, foundation managers, or members of selection committees or their relatives.

All funds distributed to individuals must be made on a charitable basis and further the purposes of your organization. You cannot award grants for a purpose that is inconsistent with Code section 170(c)(2)(B).

You should keep adequate records and case histories so that you can substantiate your grant distributions with the IRS if necessary.

Please keep a copy of this letter in your records.

If you have questions, please contact the person listed at the top of this letter.

Sincerely,

Holly O. Paz

Director, Exempt Organizations

LTR: IRS Rules on Transfer of Assets Between Foundations.

Citations: LTR 201321024

The IRS ruled that the transfer of assets from one private foundation to another will not affect either foundation's tax-exempt status, will not give rise to termination taxes or net investment income taxes, will not be an act of self-dealing, and will not constitute a jeopardizing investment.

Contact Person: * * *

Identification Number: * * *

Telephone Number: * * *

Uniform Issues List Numbers: 501.03-00, 507.00-00, 507.05-00,
507.06-00, 507.09-00, 512.00-00, 4940.00-00, 4941.04-00, 4942.03-05,
4942.05-00, 4944.00-00, 4945.04-00

Release Date: 5/24/2013

Date: February 27, 2013

Employer Identification Number: * * *

LEGEND:

B = * * *

C = * * *

D = * * *

P = * * *

Dear * * *:

This responds to your letter dated May 31, 2012, in which you requested rulings on the application of Parts I and II of Subchapter F of Chapter 1, I.R.C. §§ 501-509, and Subchapter A of Chapter 42, Subtitle D, §§ 4940-4948, to the transaction described below.

FACTS

You are a trust organized exclusively for charitable purposes, and you have been recognized exempt from federal income taxation as an organization described in § 501(c)(3). You are classified as a private non-operating foundation within the meaning of § 509(a). You were created by, and originally funded with a contribution from, B. B and her husband, C, (jointly, the "Founders"), are your sole trustees. You stipulate that B is a substantial contributor to you within the meaning of § 507(d)(2)(A), that C is a substantial contributor to you within the meaning of § 507(d)(2)(B)(iii), that B and C are

your foundation managers within the meaning of § 4946(b), and, consequently, that B and C are disqualified persons with respect to you within the meaning of § 4946(a)(1)(A) and (B).

P is organized as a not-for-profit corporation under state law. P has been recognized exempt from federal income taxation as an organization described in § 501(c)(3), and is classified as a private operating foundation described in § 4942(j)(3). You and P do not share the same tax year. The officers and directors of P are B, C, and D. D is an unrelated person who has provided legal services to you, B, C, and P. You stipulate that B is a substantial contributor to P within the meaning of § 507(d)(2)(A), that C is a substantial contributor to P within the meaning of § 507(d)(2)(B)(iii), that B, C, and D are foundation managers of P within the meaning of § 4946(b), that B and C are disqualified persons with respect to P within the meaning of § 4946(a)(1)(A) and (B), and that D is a disqualified person with respect to P within the meaning of § 4946(a)(1)(B).

You represent that the Founders, as your sole Trustees and as two of the three directors of P, effectively control both you and P (collectively, "the Foundations") within the meaning of §§ 1.482-1(a)(3) and 1.507-3(a)(9)(i).

You represent that both of the Foundations have made timely tax filings on their respective Returns of Organizations Exempt from Income Tax, Forms 990-PF, for all applicable years, and that both have complied with all applicable state filing obligations throughout their respective terms of existence.

Neither of the Foundations has undertaken any activities that would be inconsistent with tax-exempt status as a § 501(c)(3) organization, nor made any changes to their respective governing documents since the filing of their Applications for Tax-Exempt Status, Form 1023. There have been no willful repeated acts (or failures to act), nor any willful and flagrant act (or failure to act), within the meaning of § 507(a)(2)(A), with respect to either of the Foundations that would give rise to liability for tax under Chapter 42 of the Code, and neither Foundation has received a notification from the Secretary of the Treasury described in § 507(a)(2)(B). Neither Foundation has previously terminated its status as a private foundation. You have made qualifying distributions in sufficient amount to avoid imposition of excise tax under § 4942. P has made qualifying distributions in connection with the conduct of its exempt mission to qualify as a private operating foundation under § 4942(j)(3).

You represent that all grants made, or to be made, by you prior to the transfer of your remaining assets to P, as described below, have been grants to public charities. P has not made grants to other organizations. Neither Foundation has incurred any "taxable expenditure" within the meaning of § 4945(d), and neither Foundation has previously made any grant or other disposition of funds that would require the exercise of expenditure responsibility within the meaning of § 4945(d)(4)(B).

Under the Declaration of Trust that serves as your governing instrument, your trustees are empowered to make distributions in their discretion from Trust income and principal to "Qualified Charitable Recipients" ("QCRs"). QCRs are defined as organizations described in § 170(c)(1) or (2) which are exempt from tax under § 501(c)(3). The Trust instrument makes reference to suggested types of QCR donees, but the Trustees are empowered to make distributions to any charitable organization qualifying as a QCR, without regard to its mission or purposes. P, as an organization described in §§ 170(c)(2) and 501(c)(3), is a QCR within the meaning of the Trust instrument, and, as such, is eligible under the Trust instrument to receive grants from you. Prior to, and except for, the transfer of its remaining assets to P as described below, all of your grants have been made or will have been made to unrelated grantees that are treated as public charities under the Code.

The corporate purposes of P are described in its Articles of Organization as including "the provision of educational, vocational, social, psychological, and financial assistance to homeless individuals and

families,” as well as making distributions to other § 501(c)(3) organizations. Since P was first organized, it has provided education and practical job-skills training to disadvantaged persons and those who have suffered displacement from recent economic upheavals with the objective of equipping them to survive in the current economy, to enter or re-enter the work-force, and to lead productive and satisfying lives. P has provided free career development services to unemployed and underemployed individuals, and has offered such individuals skill assessment, career planning, computer training, interview and resume help, financial planning, job search planning, and other assistance.

Over the past several years, the Founders have concluded that the services provided by P have been increasingly needed, in part because of the large number of people displaced by recent economic upheaval and recession. The population in need of such services has been underserved by other organizations and the need and demand for the services provided by P have increased. At the same time, economic circumstances have made fundraising from third parties more difficult. The Founders have determined that the exempt purposes of both Foundations will be best served by concentrating their efforts and charitable resources on the work and mission of P, and by eliminating the duplication and administrative burden of operating two separate private foundations.

Your only activities have consisted of grants made to unrelated QCRs, the missions of most of which are unrelated to P’s mission. The Trustees have determined that the best use of your remaining charitable funds, in furtherance of your exempt purpose, would be to provide assistance to P in carrying out the activities which form the basis of P’s exempt purposes. Therefore, the Founders, as your Trustees and as Directors of P, with the concurrence of P’s third director, have determined that it is in the best interests of both Foundations to contribute all of your remaining net funds to P, to discontinue any of your further activities or grants, and to continue to operate P in furtherance of its exempt purposes.

After making some final grants to unrelated public charities you will transfer all of your remaining assets to P. Your Trustees will reserve a final amount for estimated debts and expenses, including taxes due, if any, under § 4940, and, thereafter, transfer the balance of your remaining net assets to P (the “Transfer”). The Transfer will involve substantially all of your net assets, including all accumulated income and undistributed trust principal. Any amounts remaining after the final payment of taxes, expenses, and fees, will also be transferred to P. Following these transfers, you will retain no assets and will cease to operate.

You will file a Form 990-PF for the year of the disposition of your assets. No sooner than at least one day after the Transfer, your Trustees will provide notice pursuant to § 507(a)(1) to the Manager, Exempt Organizations Determinations, TE/GE, of your intent to terminate your private foundation status, in the form and manner prescribed by § 1.507-1(b) and other applicable regulations.

Following the Transfer, P will continue to operate as a private operating foundation engaged in the active conduct of activities in furtherance of its exempt purposes. It expects to use the transferred funds as well as its other assets exclusively in furtherance of its exempt purposes. The Founders expect that P’s qualifying distributions, substantially all in the form of expenditures incurred in carrying out its exempt activities, will continue to exceed its net income and minimum investment returns. P will also take responsibility for all liabilities, if any, under Chapter 42 that may be imposed or in effect with respect to either you or P after the Transfer date.

While P will continue to provide services free of charge, its management has determined that P’s exempt purposes can be further served by expanding its services to include fee-based training and certification programs in widely-used computer programs. These services have been identified as particularly valuable to the core mission of P, which is helping displaced and disadvantaged persons

acquire the skills needed to obtain meaningful and lasting employment. The fees paid for such services will help P recover the costs of those programs as well as provide a source of revenue to support P's ongoing operations and pro bono services.

The legal services with respect to the Transfer will be provided by a law firm in which D is a partner with a profits interest of less than 35%. D, as a director of P, is a disqualified person with respect to P. You represent that the law firm will charge reasonable fees for the legal services provided in connection with the Transfer, the termination of you and your status as a private foundation, and the application for a private letter ruling. The services provided by the law firm will be limited solely to such services as are reasonably necessary to carrying out the exempt purposes of the Foundations, and shall not be excessive.

RULINGS REQUESTED

You have requested the following rulings:

1. The transfer of substantially all of your net assets to P (the "Transfer") will not adversely affect the status of you or P as tax-exempt organizations described in § 501(c)(3).
2. The Transfer will be a transfer described in § 507(b)(2).
3. The Transfer will not terminate your private foundation status and will not cause you to incur any liability for the § 507(c) termination tax.
4. Following the Transfer, you will be eligible to terminate your private foundation status through the "voluntary termination" procedures of § 507(a)(1).
5. Pursuant to § 1.507-7(b)(1), the date for determining the value of your assets, for purposes of calculating the termination tax under § 507(c), shall be the date proper notification is given, in the manner prescribed in the regulations, of your intention voluntarily to terminate your private foundations status (hereinafter, "Notice").
6. Provided that such Notice is given at least one day after the Transfer, and at a time when your net remaining assets are valued at zero dollars (\$0.00), then the amount of termination tax due under § 507(c)(2) upon the termination of your status as a private foundation shall be zero dollars (\$0.00).
7. Pursuant to § 507(b)(2), P will not be treated as a newly created organization as a result of the Transfer.
8. P, as transferee of substantially all of your net assets, shall be treated as possessing those attributes and characteristics of yours described in subparagraphs (2), (3), and (4) of § 1.507-3(a).
9. The Founders, as the only Trustees of you, and as two of the three Directors of P, and as foundation managers and substantial contributors of both Foundations, effectively control both Foundations within the meaning of §§ 1.482-1(a)(3) and 1.507-3(a)(9). Accordingly, for purposes of Chapter 42, the transferee Foundation, P, will be treated as though it were you, the transferor Foundation.
10. The Transfer will not be a realization event for you, and will not give rise to any gross investment income or capital gain net income, within the meaning of § 4940, with respect to either you or P.
11. P, as transferee, may use any excess § 4940 tax paid by you, the transferor, to offset P's § 4940 tax liability.

12. The Transfer will not constitute self-dealing and will not subject either of the Foundations, or any of their respective officers, directors, or Trustees, as the case may be, to tax under § 4941.
13. The providing of reasonable and necessary legal services with respect to the Transfer by a law firm in which D is a partner, and the payment of reasonable compensation for such services by the Foundations, will not be an act of self-dealing within the meaning of § 4941(d), notwithstanding the status of D as a disqualified person with respect to P.
14. You will not be required to meet the qualifying distribution requirements of § 4942 for the taxable year of the Transfer provided that P's distributable amount for the year of the Transfer is increased by your distributable amount for the year of the Transfer, and your qualifying distributions made during the taxable year of the Transfer, if any, will be carried over to P, and may be used by P to meet its minimum distribution requirements under § 4942 for the year.
15. The Transfer will not constitute a jeopardizing investment within the meaning of § 4944.
16. The Transfer will not be a taxable expenditure within the meaning of § 4945(d), and there will be no expenditure responsibility requirements that must be exercised under § 4945(d)(4) or (h) with respect to the Transfer.
17. The payment of reasonable legal fees to the attorneys for you and P for services with respect to the Transfer, and the IRS fee for this Private Letter Ruling will not be treated as taxable expenditures within the meaning of § 4945(d)(5).
18. The operation by P of state licensed postsecondary career training programs for a fee will not adversely affect P's tax-exempt status under § 501(c)(3) or its status as a private operating foundation under § 4942(j)(3).
19. The fees received by P from payments by users for its certification classes will not be considered gross income derived from an unrelated trade or business for purposes of § 512(a)(1).
20. From and after the effective date of the Transfer, P will continue to exist as an organization that is exempt from taxation under § 501(c)(3) and which will qualify as a private operating foundation under § 4942(j)(3).

LAW

I.R.C. § 501(a) exempts from federal income taxation organizations described in § 501(c).

I.R.C. § 501(c)(3) describes organizations organized and operated exclusively for charitable, educational, and other designated exempt purposes.

Treas. Reg. § 1.501(c)(3)-1(d)(3)(i) provides that the term "educational," as used in § 501(c)(3), includes the instruction and training of the individual for the purpose of improving or developing his capabilities.

I.R.C. § 509(a) provides that an organization described in § 501(c)(3) is a private foundation unless it is described in § 509(a)(1), (2), (3), or (4).

I.R.C. § 507(a) provides that, except as provided in subsection (b), the status of any organization as a private foundation shall be terminated only if (1) it notifies the Secretary of its intent to accomplish such termination, or (2) with respect to such organization, 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, and the Secretary notifies such organization that it is liable for the tax imposed by subsection (c), and either such organization pays the tax (or any portion not abated under subsection (g)) or the entire amount of such tax is abated under subsection (g).

Treas. Reg. § 1.507-1(b)(1) provides that in order for a private foundation to terminate its private foundation status under § 507(a)(1), an organization must submit a statement to the Internal Revenue Service (“Service”) of its intent to terminate its private foundation status under § 507(a)(1). Such statement must set forth in detail the computation and amount of tax imposed under § 507(c). Unless the organization requests abatement of such tax pursuant to § 507(g), full payment of such tax must be made at the time the statement is filed under § 507(a)(1).

I.R.C. § 507(c) imposes an excise tax on each terminating private foundation equal to the lower of the aggregate tax benefit resulting from the § 501(c)(3) status of such foundation, or the value of the net assets of such foundation.

I.R.C. § 507(e) and Treas. Reg. § 1.507-7(a) provide that, for purposes of § 507(c), the value of the net assets shall be determined at whichever time such value is higher: (1) the first day on which action is taken by the organization which culminates in its ceasing to be a private foundation, or (2) the date on which it ceases to be a private foundation.

Treas. Reg. § 1.507-7(b)(1) provides that, in the case of a termination under § 507(a)(1), the date for determining the value of the foundation’s assets for purposes of calculating the termination tax under § 507(c) shall be the date on which the foundation gives the notification described in § 507(a)(1).

I.R.C. § 507(b)(2) provides that, in the case of a transfer of assets of a 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 a newly created organization.

Treas. Reg. § 1.507-3(c)(1) provides that, for purposes of § 507(b)(2), the terms “other adjustment, organization, or reorganization” shall include any partial liquidation or any other significant disposition of assets to one or more private foundations, other than transfers for full and adequate consideration or distributions out of current income.

Treas. Reg. § 1.507-3(c)(2) provides that the term “significant disposition of assets to one or more private foundations” includes any disposition (or series of related dispositions) by a private foundation to one or more private foundations of 25 percent or more of the fair market value of the net assets of the transferor foundation at the beginning of the taxable year in which the transfers occur.

Treas. Reg. § 1.507-1(b)(6) provides that when a foundation transfers all or part of its assets to one or more other private foundations pursuant to a transfer described in § 507(b)(2) and § 1.507-3(c), such transferor foundation will not have terminated its private foundation status under § 507(a)(1).

Treas. Reg. § 1.507-1(b)(7) provides that neither a transfer of all the assets of a private foundation nor a significant disposition of assets by a private foundation shall be deemed to result in a termination of the transferor private foundation under § 507(a) unless the transferor private foundation elects to terminate pursuant to § 507(a)(1) or § 507(a)(2) is applicable.

Treas. Reg. § 1.507-3(d) provides that unless a private foundation voluntarily gives notice pursuant to § 507(a)(1), a transfer of assets described in § 507(b)(2) will not constitute a termination of the

transferor's private foundation status under § 507(a)(1).

Treas. Reg. § 1.507-4(b) provides that private foundations which make transfers described in § 507(b)(2) are not subject to the tax imposed under § 507(c) with respect to such transfers unless the provisions of § 507(a) become applicable.

Treas. Reg. § 1.507-3(a)(1) provides that, in the case of a transfer of assets of a private foundation to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization, or reorganization, including a significant disposition of assets to one or more private foundations within the meaning of § 1.507-3(c), the transferee organization shall not be treated as a newly created organization. Rather, the transferee organization shall be treated as possessing those attributes and characteristics of the transferor organization which are described in subparagraphs (2), (3), and (4) of this paragraph.

Treas. Reg. § 1.507-3(a)(2)(i) provides that a transferee organization to which this § 1.507-3(a) applies shall succeed to the aggregate tax benefit of the transferor organization in an amount equal to the amount of such aggregate tax benefit 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 shall be determined at the time of the transfer.

Treas. Reg. § 1.507-3(a)(3) provides that, for purposes of § 507(d)(2), in the event of a transfer of assets described in § 507(b)(2), any person who is a "substantial contributor" (within the meaning of § 507(d)(2)) with respect to the transferor foundation shall be treated as a "substantial contributor" with respect to the transferee foundation, regardless of whether such person meets the \$5,000-two percent test with respect to the transferee organization at any time.

Treas. Reg. § 1.507-3(a)(4) provides that if a private foundation incurs liability for one or more of the taxes imposed under Chapter 42 (or any penalty resulting therefrom) prior to, or as a result of, making a transfer of assets described in § 507(b)(2) to one or more private foundations, in any case where transferee liability applies each transferee foundation shall be treated as receiving the transferred assets subject to such liability to the extent that the transferor foundation does not satisfy such liability.

Treas. Reg. § 1.507-3(a)(5) provides that, except as provided in subparagraph (9) of this paragraph, a private foundation is required to meet the distribution requirements of § 4942 for any taxable year in which it makes a § 507(b)(2) transfer of all or part of its net 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 § 4942(g). However, where the transferor has disposed of all of its assets, the recordkeeping requirements of § 4942(g)(3)(B) shall not apply during any period in which it has no assets. Such requirements are applicable for any taxable year other than a taxable year during which the transferor has no assets.

Treas. Reg. § 1.507-3(a)(9)(i) provides that if a private foundation transfers all of its net assets to one or more private foundations which are effectively controlled (within the meaning of § 1.482-1A(a)(3)), directly or indirectly, by the same person or persons who effectively control the transferor private foundation, for purposes of Chapter 42 (§ 4940 et seq.) and part II of Subchapter F of Chapter 1 of the Code (§§ 507 through 509), such a transferee private foundation shall be treated as if it were the transferor.

I.R.C. § 511(a)(1) imposes a tax for each taxable year on the unrelated business taxable income (as defined in § 512) of organizations described in § 501(c).

I.R.C. § 512(a)(1) provides that the term “unrelated business taxable income” means the gross income derived by any organization from any unrelated trade or business (as defined in § 513) regularly carried on by it less certain deductions and subject to certain modifications.

I.R.C. § 513(a) provides that the term “unrelated trade or business” means, in the case of an organization subject to the tax imposed by § 511, any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or functions constituting the basis for its exemption under § 501.

Treas. Reg. § 1.513-1(d)(2) provides that a trade or business is “related” to exempt purposes, in the relevant sense only where the conduct of the business activities bears a causal relationship to the achievement of exempt purposes (other than through the production of income); and the trade or business is “substantially related,” for purposes of § 513, only if the causal relationship is a substantial one. Thus, for the conduct of a trade or business from which a particular amount of gross income is derived to be substantially related to purposes for which exemption is granted, the production or distribution of the goods or the performance of the services from which the gross income is derived must contribute importantly to the accomplishment of those purposes. Whether activities productive of gross income contribute importantly to the accomplishment of any purpose for which an organization is granted exemption depends in each case upon the facts and circumstances involved.

I.R.C. § 4940(a) imposes on each private foundation which is exempt from taxation under § 501(a) for the taxable year a tax equal to 2 percent of the net investment income of such foundation for the taxable year.

Rev. Rul. 2002-28, 2002-1 C.B. 941, holds that when a private foundation transfers all of its assets to one or more private foundations in a transfer described in § 507(b)(2) the transfers do not give rise to net investment income and are not subject to tax under § 4940(a). The transferee foundations may use their proportionate share of any excess § 4940 tax paid by the transferor to offset their own § 4940 tax liability.

I.R.C. § 4941(a)(1) imposes a tax on each act of self-dealing between a disqualified person and a private foundation.

I.R.C. § 4946(a)(1) provides that the term “disqualified person,” with respect to a private foundation, includes a person who is —

(A) a substantial contributor to the foundation,

(B) a foundation manager (within the meaning of subsection (b)(1)),

(C) an owner of more than 20 percent of —

(i) the total combined voting power of a corporation,

(ii) the profits interest of a partnership, or

(iii) the beneficial interest of a trust or unincorporated enterprise, which is a substantial contributor to the foundation,

(D) a member of the family of any individual described in subparagraph (A), (B), or (C),

(E) a corporation of which persons described in subparagraph (A), (B), (C), or (D) own more than 35 percent of the combined voting power,

(F) a partnership in which persons described in subparagraph (A), (B), (C), or (D) own more than 35 percent of the profits interest, and

(G) a trust or estate in which persons described in subparagraph (A), (B), (C), or (D) hold more than 35 percent of the beneficial interest.

Treas. Reg. § 53.4946-1(a)(8) provides that, for purposes of § 4941, the term “disqualified person” shall not include any organization described in § 501(c)(3) other than an organization described in § 509(a)(4).

Treas. Reg. § 53.4941(d)-1(b)(4) provides that a transaction between a private foundation and an organization which is not controlled by the foundation (within the meaning of subparagraph (5) of this paragraph) and which is not described in § 4946(a)(1)(E), (F), or (G) because persons described in § 4946(a)(1)(A), (B), (C), or (D) own no more than 35 percent of the total combined voting power or profits or beneficial interest of such organization, shall not be treated as an indirect act of self-dealing between the foundation and such disqualified person solely because of the ownership interest of such persons in such organization.

I.R.C. § 4941(d)(1)(E) provides that the term “self-dealing” includes any direct or indirect payment of compensation (or payment or reimbursement of expenses) by a private foundation to a disqualified person.

I.R.C. § 4941(d)(2)(E) and Treas. Reg. § 53.4941(d)-3(c)(1) provide that the payment of compensation (and the payment or reimbursement of expenses) by a private foundation to a disqualified person for personal services which are reasonable and necessary to carrying out the exempt purpose of the private foundation shall not be an act of self-dealing if the compensation (or payment or reimbursement) is not excessive.

Treas. Reg. § 53.4941(d)-3(c)(2) provides examples illustrating the provisions of § 4941(d)(2)(E). In Example (1), M, a partnership, is a firm of 10 lawyers engaged in the practice of law. A and B, partners in M, serve as trustees to private foundation W and, therefore, are disqualified persons. In addition, A and B own more than 35 percent of the profits interest in M, thereby making M a disqualified person. M performs various legal services for W from time to time as such services are requested. It is concluded that the payment of compensation by W to M shall not constitute an act of self-dealing if the services performed are reasonable and necessary for the carrying out of W’s exempt purposes and the amount paid by W for such services is not excessive.

I.R.C. § 4942(a) imposes a tax on the undistributed income of a private foundation (other than an operating foundation under § 4942(j)(3)) for any taxable year which has not been distributed before the first day of the second (or any succeeding) taxable year following such taxable year.

I.R.C. § 4942(c) defines “undistributed income” for any taxable year as the amount by which the distributable amount for such taxable year exceeds the qualifying distributions made out of such distributable amount for such taxable year.

I.R.C. § 4942(d) defines “distributable amount” as the amount equal to the sum of the minimum investment return, plus certain other amounts, reduced by the sum of the taxes imposed on such private foundation for the taxable year under subtitle A and § 4940.

I.R.C. § 4942(g)(1)(A) provides that the term “qualifying distribution” means any amount (including

that portion of reasonable and necessary administrative expenses) paid to accomplish one or more purposes described in § 170(c)(2)(B), other than a contribution to (i) an organization controlled directly or indirectly by the foundation or by one or more disqualified persons with respect to the foundation, except as provided in paragraph (3), or (ii) a private foundation which is not an operating foundation under § 4942(j)(3), except as provided in paragraph (3).

I.R.C. § 4942(g)(3) provides that the term “qualifying distribution” includes a contribution to a § 501(c)(3) organization described in paragraph (1)(A)(i) or (ii) if —

(A) not later than the close of the first taxable year after its taxable year in which such contribution is received, such organization makes a distribution equal to the amount of such contribution and such distribution is a qualifying distribution (within the meaning of paragraph (1) or (2), without regard to this paragraph) which is treated under subsection (h) as a distribution out of corpus (or would be so treated if such § 501(c)(3) organization were a private foundation which is not an operating foundation), and

(B) the private foundation making the contribution obtains adequate records or other sufficient evidence from such organization showing that the qualifying distribution described in subparagraph (A) has been made by such organization.

I.R.C. § 4942(i) and Treas. Reg. § 53.4942(a)-3(e) provide for a carry-over of the amount by which qualifying distributions during the five preceding taxable years (other than amounts required to be distributed out of corpus under § 4942(g)(3)) have exceeded the distributable amounts for such years.

I.R.C. § 4942(j)(3) provides that, for purposes of § 4942, the term “operating foundation” means any organization —

A. which makes qualifying distributions (within the meaning of paragraph (1) and (2) of subsection (g)) directly for the active conduct of the activities constituting the purpose or function for which it is organized and operated equal to substantially all of the lesser of —

i. its adjusted net income (as defined in subsection (f), or

ii. its minimum investment return; (the “income test”) and

B.

i. substantially more than half of the assets of which are devoted directly to such activities or to functionally related businesses (as defined in paragraph (4)), or to both, or are stock of a corporation which is controlled by the foundation and substantially all of the assets of which are so devoted (the “assets test”),

ii. which normally makes qualifying distributions (within the meaning of paragraph (1) or (2) of subdivision (g)) directly for the active conduct of the activities constituting the purpose or function for which it is organized and operated in an amount not less than two-thirds of its minimum investment return (as defined in subsection (e)) (the “endowment test”), or

iii. substantially all of the support (other than gross investment income as defined in § 509(e)) of which is normally received from the general public and from 5 or more exempt organizations which are not described in § 4946(a)(1)(H) with respect to each other or the recipient foundation, not more than 25 percent of the support (other than gross investment income) of which is normally received from any one such exempt organization and not more than half of the support of which is normally

received from gross investment income (the “support test”).

Notwithstanding the provisions of subparagraph (A), if the qualifying distributions (within the meaning of paragraph (1) or (2) of subsection (g)) of an organization for the taxable year exceed the minimum investment return for the taxable year, clause (ii) of subparagraph (A) shall not apply unless substantially all of such qualifying distributions are made directly for the active conduct of the activities constituting the purpose or function for which it is organized and operated.

Treas. Reg. § 53.4942(b)-1(b)(1) provides, generally, that qualifying distributions are not made by a foundation “directly for the active conduct of activities constituting its charitable, educational, or other similar exempt purpose” unless such qualifying distributions are used by the foundation itself, rather than by or through one or more grantee organizations which receive such qualifying distributions directly or indirectly from such foundation. However, administrative expenses (such as staff salaries and traveling expenses) and other operating costs necessary to conduct the foundation’s exempt activities (regardless of whether they are “directly for the active conduct” of such activities) shall be treated as qualifying distributions expended directly for the active conduct of such exempt activities if such expenses and costs are reasonable in amount. Conversely, administrative expenses and operating costs which are not attributable to exempt activities, such as expenses in connection with the production of investment income, are not treated as qualifying distributions. Expenses attributable to both exempt and nonexempt activities shall be allocated to each such activity on a reasonable and consistently applied basis.

Treas. Reg. § 53.4942(a)-2(d)(4)(i) provides, in part, that where the deductions with respect to property used for a charitable, educational, or other similar exempt purpose exceed the income derived from such property, such excess shall not be allowed as a deduction, but may be treated as a qualifying distribution.

I.R.C. § 4942(j)(4)(A) provides that the term “functionally related business” includes a trade or business which is not an unrelated trade or business (as defined in § 513).

Rev. Rul. 2002-28, 2002-1 C.B. 941, provides that, when a private foundation transfers all of its assets to one or more private foundations in a transfer described in § 507(b)(2), the transfers do not constitute qualifying distributions for the transferor foundation under § 4942. The transferee foundations assume their proportionate share of the transferor foundation’s undistributed income under § 4942 and reduce their own distributable amount for purposes of § 4942 by their proportion share of the transferor’s excess qualifying distributions under § 4942(i).

I.R.C. § 4944(a)(1) imposes a tax on any amount invested by a private foundation in a manner that jeopardizes the carrying out of any of the foundation’s exempt purposes.

Rev. Rul. 2002-28, 2002-1 C.B. 941, holds that, when a private foundation transfers all of its assets to one or more private foundations in a transfer described in § 507(b)(2), the transfers do not constitute investments jeopardizing the transferor foundation’s exempt purposes and are not subject to tax under § 4944(a)(1).

I.R.C. § 4945(a)(1) imposes a tax on any “taxable expenditure” made by a private foundation.

I.R.C. § 4945(d)(4) provides that the term “taxable expenditure” includes any amount paid or incurred as a grant to a private non-operating foundation unless the grantor foundation exercises expenditure responsibility with respect to such grant in accordance with § 4945(h).

I.R.C. § 4945(d)(5) provides that the term “taxable expenditure” includes any amount paid or

incurred by a private foundation for any purpose other than one specified in § 170(c)(2)(B).

I.R.C. § 4945(h) provides that the expenditure responsibility referred to in § 4945(d)(4) means that a 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 it was made; (2) to obtain full and complete reports from the grantee on how the funds are spent; and (3) to make full and detailed reports with respect to such expenditures to the Secretary.

Rev. Rul. 2002-28, 2001-1 C.B. 941, provides that, when a private foundation transfers all of its assets to one or more private foundations effectively controlled by the same persons that effectively control the transferor, the transferee foundation is treated as the transferor foundation rather than as the recipient of an expenditure responsibility grant. Therefore, there are no expenditure responsibility requirements that must be exercised under § 4945(d)(4) or (h) with respect to the transfers to the transferee foundation. The transferor foundation is required to exercise expenditure responsibility over the transferor's outstanding grants until it disposes of all of its assets. Thereafter, during any period in which the transferor foundation has no assets, the transferor foundation is not required to exercise expenditure responsibility over any outstanding grants. However, the transferor foundation must still meet the § 4945(h) reporting requirements for the outstanding grants for the year in which the transfer was made.

Treas. Reg. § 53.4945-6(b)(1)(v) provides that any payment which constitutes a qualifying distribution under § 4942(g) ordinarily will not be treated as taxable expenditures under § 4945(d)(5).

Treas. Reg. § 53.4945-6(b)(2) provides that any expenditures for unreasonable administrative expenses, including compensation, consultant fees, and other fees for services rendered will ordinarily be taxable expenditures under § 4945(d)(5) unless the foundation can demonstrate that such expenses were paid or incurred in the good faith belief that they were reasonable and that the payment or incurrence of such expenses in such amounts was consistent with ordinary business care and prudence.

The determination whether an expenditure is unreasonable shall depend upon the facts and circumstances of the particular case.

ANALYSIS

Issue 1

Whether the transfer of substantially all of your net assets to P (the "Transfer") would adversely affect the status of either you or P as tax-exempt organizations described in § 501(c)(3).

Both you and P are currently recognized by the Service as organizations described in § 501(c)(3). Section 501(c)(3) describes organizations organized and operated exclusively for charitable, educational, and other specified exempt purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in, any political campaign on behalf of (or in opposition to) any candidate for public office.

Your exempt purposes include the making of grants to QCRs, which your trust instrument defines as organizations described in §§ 170(c)(1) and (2) that are entitled to exemption from tax under § 501(c)(3). Furthermore, Articles I.B and VI of your trust instrument authorize the Trustees, in their

discretion, to distribute up to the entire net income and principal of the Trust to such organizations in furtherance of your exempt purposes. P qualifies as an organization described in § 170(c)(2) and is exempt from tax under § 501(c)(3). Therefore, P is a QCR and an eligible recipient of trust distributions under your trust instrument, and the Transfer of all your remaining assets to such an organization is expressly permitted thereunder.

P is organized for charitable and educational purposes, including the provision of educational, vocational, social, psychological, and financial assistance to homeless individuals and families, and the making of distributions for such or similar purposes to organizations that qualify as exempt organizations under § 501(c)(3). Article IV, paragraph (a)(ii) of P's Articles of Organization permits P to "receive contributions from any and all sources." Therefore, the receipt of the transferred funds from you is a permissible action by P under its governing instrument. P's intention is to utilize these funds in carrying out the activities which constitute the basis of its exempt purposes. No private inurement will result from the receipt of those funds. The founder, B, serves without compensation, and the only persons who will benefit from P's activities will be those persons who fall within the charitable class that P was established to serve. Nor will the funds be used for legislative or political activities or for any other purpose that is not in conformity with P's exempt purposes.

Since the Transfer is consistent with your exempt purposes, and since the transferred funds will be used by P exclusively in furtherance of its exempt purposes, the Transfer will have no adverse effect on the qualification of either you or P as organizations described in § 501(c)(3).

Issue 2

Whether the Transfer would be a transfer described in § 507(b)(2).

I.R.C. § 507(b)(2) applies to the transfer of the assets of any private foundation to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization, or reorganization. Section 1.507-3(c)(1) provides that the terms "other adjustment, organization, or reorganization" shall include any partial liquidation or any other significant disposition of assets to one or more private foundations, other than transfers for full and adequate consideration. The term "significant disposition of assets to one or more private foundations" is defined by § 1.507-3(c)(2) as any disposition or series of dispositions where the aggregate value transferred is 25 percent or more of the fair market value of the foundation at the beginning of the taxable year.

You will transfer all of your net remaining assets to P after the payment of certain grants to unrelated QCR's and the payment of final taxes and expenses. After the Transfer is completed, the value of your assets would be zero dollars (\$0.00). The assets transferred would constitute 100 percent of your net assets remaining after the payment of your qualifying distributions, debts, expenses, and taxes, and not less than 93 percent of your total assets as of the beginning of the taxable year. Therefore, the Transfer would constitute a "significant disposition of assets" within the meaning of § 1.507-3(c)(2), and, thus, would qualify as an "other adjustment, organization, or reorganization" within the meaning of § 1.507-3(c)(1). Accordingly, the Transfer would be a transfer described in § 507(b)(2).

Issues 3, 4, 5, and 6

Whether the Transfer would not terminate your private foundation status or cause you to incur any liability for the § 507(c) termination tax.

Whether, following the Transfer, you would be eligible to terminate your private foundation status

by giving notice to the Service as provided in § 507(a)(1).

Whether, for purposes of calculating the termination tax under § 507(c), the date for determining the value of your assets is the date on which you give the notice described in § 507(a)(1) ("Notice").

Provided that Notice is given at least one day after the Transfer, and at a time when your net remaining assets are valued at Zero Dollars (\$0.00), whether the amount of termination tax due under § 507(c)(2) upon termination of your status as a private foundation would be Zero Dollars (\$0.00).

Section 1.507-1(b)(6) provides that when a foundation transfers all or part of its assets to one or more other private foundations pursuant to a transfer described in § 507(b)(2), such transferor foundation will not have terminated its private foundation status under § 507(a)(1). In addition, § 1.507-1(b)(7) provides that neither a transfer of all the assets of a private foundation nor a significant disposition of assets by a private foundation shall be deemed to result in a termination of the transferor private foundation under § 507(a) unless the transferor private foundation elects to terminate pursuant to § 507(a)(1). Furthermore § 1.507-3(d) provides that unless a private foundation voluntarily gives notice pursuant to § 507(a)(1), a transfer of assets described in § 507(b)(2) will not constitute termination of the transferor's private foundation status under § 507(a)(1). Finally, § 1.507-4(b) provides that a private foundation that makes a transfer described in § 507(b)(2) is not subject to the tax imposed under § 507(c) with respect to such transfer unless the provisions of § 507(a) become applicable.

As discussed under Issue 2, above, the Transfer will constitute a significant distribution of assets described in § 507(b)(2). Further, you have represented that the Secretary has not notified you of any tax imposed by § 507(c) due to any willful or flagrant acts or failures to act. Consequently, the Transfer would not, of itself, terminate your private foundation status or subject you to the tax imposed under § 507(c).

Section 507(a)(1) provides that the status of an organization as a private foundation shall be terminated only if such organization notifies the Secretary of its intent to accomplish such termination and such organization pays the tax imposed by § 507(c). Furthermore, § 1.507-1(b)(1) provides that in order for a private foundation to terminate its private foundation status under § 507(a)(1) it must submit a statement to the Internal Revenue Service of its intent to terminate its private foundation status under § 507(a)(1). In your situation where there have been no willful repeated acts or failures to act, and no flagrant act or failure to act, which would give rise to taxes and penalties under Chapter 42, you may elect to terminate your private foundation status by notifying the Manager, Exempt Organizations Determinations (TE/GE), of your intent to accomplish such termination and paying any termination tax deemed to be due under § 507(c).

Section 507(c) imposes a tax on a terminating private foundation equal to the lesser of the aggregate tax benefit resulting from its § 501(c)(3) status and the value of its net assets. Section 507(e) and § 1.507-7(a) provide that, for purposes of § 507(c), the value of the net assets shall be determined at whichever time such value is greater: (1) the first day on which the organization takes action which culminates in its ceasing to be a private foundation, or (2) the date on which it ceases to be a private foundation. Finally, § 1.507-7(b)(1) provides that in the case of a voluntary termination under § 507(a)(1), the date for determining the value of the foundation's assets for purposes of calculating the termination tax under § 507(c) shall be the date on which the foundation gives the notification described in § 507(a)(1). The date for determining the value of your assets for purposes of calculating your termination tax is the date you give Notice. If you give Notice after the Transfer, the value of your assets on the date of the Notice would be Zero Dollars (\$0.00), and, thus, the amount of the § 507(c) termination tax imposed on you would be Zero Dollars (\$0.00).

Issues 7, 8, and 9

Whether, for purposes of §§ 507 through 509, P would be treated as a newly created organization as a result of the Transfer, pursuant to § 507(b)(2).

Whether P, as transferee of substantially all of your net assets, would be treated as possessing those attributes and characteristics of you, the transferor, described in § 1.507-3(a)(2), (3), and (4).

Since you and P are both effectively controlled by the same persons within the meaning of §§ 1.482-1(a)(3) and 1.507-3(a)(9), whether, for purposes of Chapter 42 (§ 4940 et seq.) and §§ 507 through 509, P, the transferee, would be treated as though it were you, the transferor.

Section 1.507-3(a)(1) provides that in the case of a significant distribution of assets to one or more private foundations within the meaning of § 1.507-3(c) the transferee organization shall not be treated as a newly created organization. Rather, it shall be treated as possessing those attributes and characteristics of the transferor organization which are described in § 1.507-3(a)(2), (3), and (4). Since, as discussed under Issue 2, above, the Transfer would qualify as a “significant distribution of assets” within the meaning of § 1.507-3(c)(2), P would not be treated as a newly created organization as a result of the Transfer. Rather, P would be treated as possessing your attributes and characteristics described in subparagraphs (2), (3), and (4) of § 1.507-3(a).

Treas. Reg. § 1.507-3(a)(9)(i) provides that if a private foundation transfers all of its net assets to one or more private foundations which are effectively controlled by the same persons which effectively controlled the transferor private foundation, for purposes of Chapter 42 (§ 4940 et seq.), the transferee foundation shall be treated as if it were the transferor. Since you have represented that B and C effectively control both you and P, for purposes of Chapter 42, P would be treated as if it were you.

Issues 10 and 11

Whether the Transfer would give rise to any gross investment income with respect to either you or P or will be subject to tax under § 4940(a).

Whether P, as transferee, may use any excess § 4940 tax paid by you to offset P’s § 4940 tax liability.

Section 4940(a) imposes an excise tax on a private foundation’s net investment income for the taxable year. Rev. Rul. 2002-28 holds that when a private foundation transfers all of its assets to one or more private foundations in a transfer described in § 507(b)(2), the transfers do constitute investments of the transferor and, therefore, do not give rise to net investment income subject to tax under § 4940(a). Thus, the Transfer would not give rise to net investment income subject to tax under § 4940.

Furthermore, Rev. Rul. 2002-28 holds that if the transferor foundation transfers all of its assets to private foundations effectively controlled by the same persons that effectively control the transferor, any excess § 4940 tax paid by the transferor may be used by the transferee to offset its § 4940 tax liability. As you represent that the Foundations are effectively controlled by the same persons, any excess § 4940 tax paid by you may be used by P to offset P’s § 4940 tax liability.

Issues 12 and 13

Whether the Transfer would constitute an act of self-dealing within the meaning of § 4941(d), or would subject any disqualified person or foundation manager with respect to you or P to the tax imposed under § 4941(a).

Whether the provision by a law firm of reasonable and necessary legal services with respect to the Transfer, or the payment of reasonable compensation for such services by you or P, would constitute acts of self-dealing within the meaning of § 4941(d), notwithstanding the status of D, a disqualified person with respect to P, as a partner in that law firm.

Section 4941(a) imposes an excise tax on each act of self-dealing between a disqualified person and a private foundation. Section 4941 and § 1.507-3(a) determine whether the proposed Transfer of all of your assets to P would constitute an act of self-dealing between a private foundation and its disqualified persons as defined in § 4946. Under § 53.4946-1(a)(8), a “disqualified person” does not include organizations that are exempt under § 501(c)(3). Therefore, the Transfer of your assets to P would not be an act of self-dealing because P is recognized by the Service as an organization exempt from tax under § 501(c)(3).

Furthermore, while the payment of compensation, or the payment or reimbursement of expenses by a private foundation to a disqualified person is, generally, an act of self-dealing under § 4941(d)(1)(E), § 4941(d)(2)(E) and § 53.4941(d)-3(c)(1) provide that a payment or reimbursement to a disqualified person for personal services which are reasonable and necessary to carry out the exempt purposes of the private foundation is not an act of self-dealing provided the compensation, payment, or reimbursement is not excessive.

In this case, the law firm is not a disqualified person, so the payment to the law firm for legal services will not be a direct act of self-dealing. Under § 4946(a)(1)(F) a “disqualified person” includes a partnership in which disqualified persons hold more than 35 percent of the profits interests. D is a disqualified person and is a partner of the law firm but holds less than a 35 percent profits interest in the law firm.

The payment will not otherwise be treated as an indirect act of self-dealing benefitting D. Under § 53.4941(d)-1(b)(4) indirect self-dealing will not occur solely as a result of a transaction between a private foundation and an entity in which a disqualified person holds an interest where the entity is not a disqualified person by operation of § 4946(a)(1)(F). Moreover, as Example (1) of § 53.4941(d)-3(c)(2) demonstrates, the payment of compensation by a foundation for legal services does not constitute an act of self-dealing if the services performed are reasonable and necessary for carrying out of the foundation’s exempt purposes and the amount paid for such services is not excessive, and you have represented that these requirements will be met.

Issue 14

Whether the Transfer will be a qualifying distribution by you under § 4942.

Whether P will assume your “undistributed income” (if any) or succeed to your excess distributions (if any).

Section 4942(a) generally imposes a tax on the undistributed income of a private foundation (other than an operating foundation under § 4942(j)(3)) for any taxable year which has not been distributed before the first day of the second (or any succeeding) taxable year following such taxable year. Section 4942(c) defines “undistributed income” for any taxable year as the amount by which the distributable amount for such taxable year exceeds the qualifying distributions made out of such distributable amount for such taxable year. Section 4942(g)(1)(A) defines “qualifying distribution” generally as any amount (including that portion of reasonable and necessary administrative expenses) paid to accomplish one or more purposes described in § 170(c)(2)(B), but a qualifying distribution does not include a contribution to an organization controlled directly or indirectly by the foundation or by one or more disqualified persons with respect to the foundation

Section 1.507-3(a)(5) provides that, except as provided in section 1.507-3(a)(9), a private foundation making a transfer described in § 507(b)(2) must satisfy its distribution requirements under § 4942 for the taxable year in which the transfer is made. Section 1.507-3(a)(5) further provides that the transfer will count as a distribution in satisfaction of the transferor foundation's distribution requirement under § 4942 subject to the provisions of § 4942(g). Section 4942(g) provides that a distribution from one private foundation to another private foundation, where both foundations are effectively controlled by the same persons, will not be treated as a qualifying distribution by the transferor foundation for the purposes of § 4942 except to the extent that the transferee foundation makes one or more distributions that would be qualifying distributions under § 4942(g) (other than a distribution to a controlled foundation) prior to the close of the transferee's first tax year following the tax year in which it received the transfer and the distributions are treated as being made out of corpus (as if the transferee foundation were not an operating foundation).

Rev. Rul. 2002-28 holds that where, by reason of § 1.507-3(a)(9)(i), a transferee private foundation is treated as though it were the transferor for purposes of § 4942, a transfer to the transferee foundation is not treated as a qualifying distribution of the transferor foundation. Rather, the transferee foundation assumes all obligations with respect to the transferor's "undistributed income" within the meaning of § 4942(c), if any, and reduces its own distributable amount under § 4942 by the transferor foundation's excess qualifying distributions under § 4942(i). None of the three situations in Rev. Rul. 2002-28, however, involved an operating foundation.

As discussed under Issues 7, 8, and 9, above, by reason of § 1.507-3(a)(9)(i), P would be treated as if it were you for purposes of Chapter 42, including § 4942. Accordingly, the Transfer to P would not be treated as a qualifying distribution of yours. Rather, P would assume your obligations with respect to your undistributed income within the meaning of § 4942(c), if any (after taking into account any excess qualifying distribution carryovers that you may have), and you would not be required to meet your qualifying distribution requirements under § 4942 for the taxable year of the Transfer prior to the Transfer. You must file a final Form 990-PF return for the short tax year of your termination. If you have undistributed income for such tax year, P will owe § 4942 tax if P fails, by the end of P's tax year following the tax year in which P receives the Transfer, to make qualifying distributions of such amount that would be treated as out of corpus if P were a non-operating foundation. P should provide an attachment to its Form 990-PF showing how it has met this requirement.

If you have excess qualifying distributions that carry over to P, they will be forfeited if P is an operating foundation in the year of the Transfer. Section 53.4942(a)-3(e)(4) (Example (3)) explains that excess qualifying distributions carried forward lapse in their entirety in any year that the private foundation is treated as an operating foundation. Accordingly, if you have any unused excess qualifying distributions that you could have carried forward to a taxable year after the Transfer, and if P is an operating foundation in that year, your unused excess qualifying distributions will lapse and will not be available for P's use in any taxable year after the year of the Transfer if P were to cease to be an operating foundation.

Whether the Transfer would constitute a investment jeopardizing your exempt purposes, or would be subject to tax under § 4944(a)(1).

Section 4944 imposes a tax on any investment that jeopardizes an exempt organization's charitable purposes. Rev. Rul. 2002-28 holds that where a private foundation transfers all of its assets and liabilities to another private foundation, the transfer does not constitute an investment for purposes of § 4944 and, therefore, the transfer does not constitute an investment jeopardizing the transferor foundation's exempt purposes and is not subject to tax under § 4944(a)(1). Therefore, the Transfer would not constitute a jeopardizing investment or subject you to tax under § 4944(a)(1).

Issues 16 and 17

Whether the Transfer would be a taxable expenditure within the meaning of § 4945(d) or would require the exercise of expenditure responsibility under § 4945(d)(4) or (h).

Whether the payment of the IRS fee for this private letter ruling would be treated as a taxable expenditure within the meaning of § 4945(d), or whether payment of reasonable legal fees to the attorneys for you and P to obtain this private letter ruling with respect to the Transfer would be treated a taxable expenditures within the meaning of § 4945(d)(5).

Section 4945 imposes a tax on any "taxable expenditure" made by a private foundation. Section 4945(d)(4) provides that the term "taxable expenditure" includes any amount paid or incurred as a grant to a private non-operating foundation unless the grantor foundation exercises expenditure responsibility with respect to such grant in accordance with § 4945(h).

Rev. Rul. 2002-28 holds that where, by reason of § 1.507-3(a)(9)(i), a transferee foundation is treated as though it were the transferor foundation for purposes of § 4945, the transferee foundation is not treated as the recipient of an expenditure responsibility grant, and no expenditure responsibility requirements must be exercise under § 4945(d)(4) or (h) with respect to the transfer to the transferee foundation.

As discussed under Issues 7, 8, and 9, above, by reason of § 1.507-3(a)(9)(i), P would be treated as if it were you for purposes of Chapter 42, including § 4945. Consequently, the Transfer would not be considered a taxable expenditure under § 4945, and there would be no expenditure responsibility requirements to be exercised under § 4945(d)(4) or (h) with respect to the Transfer.

Section 53.4945-6(b)(1)(v) provides that any payment which constitutes a qualifying distribution under § 4942(g) will not be treated as a taxable expenditure under § 4945(d)(5). Section 4942(g)(1)(A) and § 53.4942(a)-3(a)(2)(i) provide that a qualifying distribution under § 4942(g) includes reasonable and necessary administrative expenses paid to accomplish one or more purposes described in § 170(c)(1) or (2)(B). Administrative expenses incurred in obtaining a ruling from the Service or for legal fees relating to a foundation's exempt purposes are qualifying distributions. On the other hand, § 53.4945-6(b)(2) provides that expenditures for unreasonable administrative expenses, including consultant fees and other fees for services rendered, will ordinarily be taxable expenditures under § 4945(d)(5). The payment of legal fees to the attorneys for you or P and the payment of the IRS fee for this private letter ruling are administrative expenses necessary to the accomplishment of the Foundations' exempt purposes. So long as such payments are reasonable, the legal fees paid to the attorneys for you and P to obtain a private letter ruling

with respect to the Transfer, and the IRS fee paid for this private letter ruling, would not be treated as taxable expenditures within the meaning of § 4945(d)(5).

Issues 18 and 19

Whether the operation by P of state licensed postsecondary career training programs for a fee would adversely affect P's tax exempt status under § 501(c)(3) or its status as an operating foundation under § 4942(j)(3).

Whether the fees received by P from the operation of the state licensed postsecondary career training programs would be considered gross income derived from an unrelated trade or business for purposes of § 512(a)(1).

The exempt purposes of P, as described in its Articles of Organization, include "the provision of educational, vocational, social, psychological, and financial assistance to homeless individuals and families." From its beginning, P has provided education and practical job-skills training to disadvantaged persons and those who have suffered displacement from economic upheavals so that they may be better equipped to obtain employment and to lead productive and satisfying lives. P now wishes to provide training in software programs widely used by the business community to help displaced persons whose existing skills do not correspond to the current needs of the marketplace.

Providing such training is educational within the meaning of § 1.501(c)(3)-1(d)(3)(a), and contributes importantly to the accomplishment of P's exempt purposes of providing educational and vocational assistance to homeless and displaced persons. Thus, such activities amount to a trade or business that is substantially related to the accomplishment of P's exempt purposes within the meaning of § 1.513-1(d)(2), and are, therefore, not unrelated trade or business within the meaning of § 513(a). Insofar as the term "functionally related business" under § 4942(j)(4)(A) includes a trade or business which is not an unrelated trade or business, as defined in § 513, the providing of such state-licensed postsecondary career training programs by P would constitute a "functionally related business," and deductible expenses related thereto in excess of the income from such business would constitute qualifying distributions made directly for the active conduct of activities constituting P's exempt function for purposes of qualifying as a private operating foundation under § 4942(j)(3), as provided in § 53.4942(a)-2(d)(4) and § 53.4942(b)-1(b)(1). The operation of state licensed postsecondary career training programs for a fee will not adversely affect P's status as an organization described in § 501(c)(3) or its status as a private operating foundation under § 4942(j)(3). Furthermore, since the income derived from such activities would constitute income from a related trade or business, such income would not constitute gross income derived from an unrelated trade or business for purposes of § 512(a)(1).

Issue 20

Whether, following the Transfer, if P's qualifying distributions (within the meaning of § 4942(g)(1) or (2)) made directly for the active conduct of the activities constituting its exempt purpose or function were to exceed both its net investment income and its minimum investment return, P will continue to qualify as a private operating foundation within the meaning of § 4942(j)(3).

To qualify as a private operating foundation under § 4942(j)(3), an organization must meet the income test under § 4942(j)(3)(A) and any one of three alternative tests — the assets test under § 4942(j)(3)(B)(i), the endowment test under § 4942(j)(3)(B)(ii), or the support test under § 4942(j)(3)(B)(iii). The income test requires that the organization make qualifying distributions directly for the active conduct of the activities constituting the purpose or function for which it is organized and operated equal to substantially all of the lesser of (i) its adjusted net income or (ii) its

minimum investment return. The endowment test requires qualifying direct distributions of at least two-thirds of the foundation's minimum investment return.

P anticipates, and represents, that, notwithstanding an increase in its assets and income as a result of the Transfer, P will continue to make qualifying direct distributions in excess of both its minimum investment return and its adjusted net income. So long as P's qualifying direct distributions continue to exceed both its net investment income and its minimum investment return, P would continue to qualify as a private operating foundation under § 4942(j)(3).

CONCLUSION

In light of the foregoing, we rule as follows:

1. The transfer of substantially all of your net assets to P (the "Transfer") would not adversely affect the status of either you or P as organizations described in § 501(c)(3).
2. The Transfer would be a transfer described in § 507(b)(2).
3. The Transfer would not terminate your private foundation status or cause you to incur any liability for the § 507(c) termination tax.
4. Following the Transfer, you would be eligible to terminate your private foundation status by giving notice to the Service as provided in § 507(a)(1).
5. For purposes of calculating the termination tax under § 507(c), the date for determining the value of your assets would be the date on which you give the notice described in § 507(a)(1) ("Notice").
6. Provided that Notice is given at least one day after the Transfer, and at a time when your net remaining assets are valued at Zero Dollars (\$0.00), the amount of termination tax due under § 507(c)(2) upon termination of your status as a private foundation would be Zero Dollars (\$0.00).
7. For purposes of §§ 507 through 509, P would be treated as a newly created organization as a result of the Transfer, pursuant to § 507(b)(2).
8. P, as transferee of substantially all of your net assets, would be treated as possessing those attributes and characteristics of yours described in § 1.507-3(a)(2), (3), and (4).
9. Since you and P are both effectively controlled by the same persons within the meaning of §§ 1.482-1(a)(3) and 1.507-3(a)(9), for purposes of Chapter 42 (§ 4940 et seq.) and §§ 507 through 509, P, the transferee, would be treated as though it were you, the transferor.
10. The Transfer would not give rise to net investment income and would not be subject to tax under § 4940(a).
11. P, as transferee, may use any excess § 4940 tax paid by you, the transferor, to offset P's § 4940 tax liability.
12. The Transfer would not constitute an act of self-dealing within the meaning of § 4941(d), and would not subject any disqualified person or foundation manager with respect to you or P to the tax imposed under § 4941(a).
13. The provision by a law firm of reasonable and necessary legal services with respect to the Transfer, and the payment of reasonable compensation for such services by you or P, would not

constitute acts of self-dealing within the meaning of § 4941(d), notwithstanding the status of D, a disqualified person with respect to P, as a partner in that law firm.

14. The Transfer would not constitute a qualifying distribution by you under § 4942. P would assume your undistributed income under § 4942 (if any) and be required to make qualifying distributions of such amount treated as distributed out of corpus by the end of P's tax year after the tax year in which P receives the Transfer, but excess distributions by you (if any) will not carry over to P, but will lapse in the first year after the Transfer that P qualifies as an operating foundation

15. The Transfer would not constitute an investment jeopardizing your exempt purposes, and would not be subject to tax under § 4944(a)(1).

16. The Transfer would not be a taxable expenditure within the meaning of § 4945(d); consequently there would be no expenditure responsibility requirements to be exercised under § 4945(d)(4) or (h).

17. The payment of the IRS fee for this private letter ruling would not be treated as a taxable expenditure within the meaning of § 4945(d), and payments of reasonable legal fees to the attorneys for you and P to obtain this private letter ruling with respect to the Transfer would not be treated as taxable expenditures within the meaning of § 4945(d) so long as such payments were reasonable.

18. The operation by P of state licensed postsecondary career training programs for a fee would not adversely affect P's tax-exempt status under § 501(c)(3) or its status as an operating foundation under § 4942(j)(3).

19. The fees received by P from the operation of state licensed postsecondary career training programs would not be considered gross income derived from an unrelated trade or business for purposes of § 512(a)(1).

20. Following the Transfer, if P's qualifying distributions (within the meaning of § 4942(g)(1) or (2)) made directly for the active conduct of the activities constituting its exempt purpose or function were to exceed both its net investment income and its minimum investment return, P would continue to qualify as a private operating foundation under § 4942(j)(3).

This ruling will be made available for public inspection under § 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. I.R.C. § 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,

Peter A. Holiat

Acting Manager,

Exempt Organizations

Technical Group 1

[Insurance Company Seeks Discounted Health Plan Fee for Tax-Exempt, Nonprofit Hospitals.](#)

James Fritz of Bluegrass Family Health has urged Treasury to classify health plans owned by nonprofit, tax-exempt hospitals or hospital systems in the same category as other nonprofit, tax-exempt health plans, which would give the hospital plans a 50 percent discount on the insurance plan fee required under the Affordable Care Act.

May 16, 2013

The Honorable Jacob Lew

Secretary of the Treasury

United States Department of the Treasury

1500 Pennsylvania Avenue, NW, Room 3330

Washington, DC 20220

RE: REG-118315-12: Health Insurance Providers Fee

Dear Secretary Lew:

We write on a matter of concern to a number of federally taxable regional health insurance plans owned by tax-exempt hospitals and health care systems. These hospital-owned health plans (HHPs) are unique because they are entirely owned and controlled by parents that are tax-exempt under section 501(a) of the Internal Revenue Code (IRC) and are further described in section 501(c). Despite paying taxes under the IRC, HHPs function more similarly to nonprofit entities because they must reinvest whatever marginal profits they produce each year into the hospital parent's charitable mission. HHPs were originally created as taxable entities due to the prevailing physician ownership model at the time of their founding. However, as the ownership model moved away from physician ownership, HHPs found it nearly impossible to convert to nonprofit status due to the evolving interpretation of section 501(m) of the IRC. As a result, HHPs will be assessed at unsustainable levels under REG-118315-12: Health Insurance Providers Fee ("the insurer fee") and will likely be forced to significantly limit services or exit the market altogether. Either outcome will negatively affect the communities that HHPs serve by impacting the charitable activities of their parent hospitals.

The recently released rules implementing Section 9010 of the Patient Protection and Affordable Care Act (ACA) failed to curtail the implementation of the insurer fee on this specific group of health

plans. In § 57.4(a)(4)(iii) of the insurer fee, the ACA is interpreted as granting partial reductions for certain exempt activities to health insurers that are exempt from Federal income tax and meet section 501(c) requirements. We believe HHPs should be included in this category of health plans that receive partial reductions because, like other nonprofit health plans, HHP premiums are attributable to the exempt activities of their parent nonprofit, tax-exempt hospitals and health systems. We urge you to provide relief to these plans from the insurer fee, consistent with the treatment of other tax exempt providers.

We are concerned that these taxable health plans owned entirely by nonprofit, tax-exempt hospitals or health systems appear to be included in a group of health plans that receive no exemptions from the insurer fee, while other nonprofit insurance providers receive either a partial or full exemption. We believe HHPs should receive a 50 percent exemption from the insurer fee because they are an essential part of the communities they serve.

HHPs operate differently than traditional for-profit health plans and should be treated accordingly. The parent hospitals and health systems, exempt under Internal Revenue Code Section 501(c)(3) and Section 501(c)(4), are required to hold and use all of their assets and earnings for tax-exempt, charitable purposes. This requirement extends to the equity and earnings of wholly owned/controlled taxable subsidiaries, such as HHPs. Therefore, the cost of the insurer fee that a HHP will be required to pay under the proposed regulation will ultimately reduce the resources of the parent hospital or health system to fulfill their charitable missions. The imposition of the fee on these hospitals and health systems will detract from the organization's mission and the vital community services they provide. To impose the insurer fee on these community-based providers is not sustainable and will have a damaging effect on the communities that these plans serve.

We believe that if no relief is granted to these hospital-owned health plans in the final regulations, these types of health plans will be assessed approximately \$200 million in fees in 2014 under the insurer fee. This will make it impossible for these plans to continue to offer quality, locally-based compassionate health care. The imposition of the full insurer fee on these providers may drive HHPs from the marketplace, thus limiting the choices available in these areas.

Classifying these 28 health plans with other non-profit tax-exempt health insurers appears to be in alignment with the federal government's tax exempt policies. These plans share the same charitable mission-driven agendas of their parent nonprofit health systems and should be treated in the same manner as other tax-exempt entities. Adding these plans to the 50 percent tax exempt category would increase the fees of the health plans remaining in the non-exempt category by only about 1.8 percent, resulting in a de minimis impact on the health insurance marketplace.

We greatly appreciate your willingness to continue refining your approach and hope you will grant these hospital-owned health plans a 50 percent exemption from the Health Insurance Providers Fee.

Sincerely,

James S. Fritz

President & CEO

Bluegrass Family Health

Lexington, KY

Minnesota Lawmaker Requests Guidance on Historic Rehabilitation Tax Credit.

Rep. Betty McCollum, D-Minn., has written to Treasury to request guidance on the future of the historic rehabilitation tax credit program, which she says has been disrupted by a recent court ruling and subsequent IRS memorandum that have created uncertainty and effectively halted investment in rehabilitation projects.

May 10th, 2013

The Honorable Jack Lew

Secretary

U.S. Department of the Treasury

1500 Pennsylvania Avenue N.W.

Washington, D.C. 20220

Dear Mr. Secretary:

I recently met with local nonprofit and development leaders in my Congressional District who have participated in many successful projects to rehabilitate historic properties during the past forty years, due in large part to the Historic Rehabilitation Tax Credit program (HTC). These leaders voiced concerns about the result of a recent court ruling and subsequent Internal Revenue Service (IRS) memorandum and uncertainty that has effectively halted investment in these projects, and which they believe could jeopardize the future of the HTC program. Therefore, I respectfully request your assistance in providing clear guidance from the IRS that allows the HTC to be utilized again within the next 60 days.

Nationally and in Minnesota, the HTC enjoys strong bipartisan support. HTC is a critical tool for urban renewal, facilitating the creation of jobs through the rehabilitation of historic buildings. Since its creation in the 1970s, it has helped to create 2.3 million jobs, rehabilitated more than 38,000 buildings, and spurred more than \$106 billion in private investment. This record of success and the litany of examples of community revitalization in every state in the nation have made this a popular and effective tool for economic resurgence.

Through my conversations with Minnesota leaders in urban revitalization and historic preservation, I have learned that several recent or current local projects likely would not have been possible or will not be possible without the HTC. The successful redevelopment of the landmark Saint Paul Pioneer and Endicott buildings into mixed use and residential units is helping to spur energy investment in the heart of the city's downtown, and could not have occurred without the HTC according the project's developer. More urgently, a nonprofit partnership to save rapidly deteriorating buildings at the former frontier military outpost Fort Snelling and convert them for use as housing for homeless veterans is in jeopardy. Similarly, a project to rehabilitate the former Saint Paul Post Office Building for mixed use and residential development is at risk, due to the current impasse with the HTC.

In communities like mine with a large urban core and many historic and endangered properties, HTC is a catalyst and lynchpin for redevelopment and renewal as our economy recovers from the great recession. This story is similar across the country. By one national estimate, loss of the HTC

for a year would mean that 55,000 jobs will not be created, 1,000 structures will not be rehabilitated, and more than \$3 billion in private funding will not be invested in strategic historic property rehabilitation. Given the pressing need to have businesses grow and create more jobs in the economy, an immediate resolution of this matter would allow this investment to continue.

It is my understanding that within the last week, senior IRS officials have indicated that more clarity will be provided to the public within the coming days or weeks. This is a welcome development, and I respectfully request your assistance to make sure this commitment is kept.

Residents of my Congressional District are proud of our success at protecting and investing in our historic properties by utilizing the HTC. It would be an honor to host you for a tour of some of these dynamic projects should your schedule allow it in the coming months.

Thank you for your support in finding an expeditious path forward that assures that the HTC is functioning again and the economic benefits it makes available to communities across the nation are once again flowing.

Sincerely,

Betty McCollum

Member of Congress

[Udall Announces Bill to Lower Excise Tax on Beer.](#)

The Brewers Excise and Economic Relief (BEER) Act of 2013 would reduce the per-barrel federal excise tax on beer and eliminate excise taxes for most small brewers, Sen. Mark Udall, D-Colo., said in a May 15 release announcing the bill's introduction.

[IRS Official Explains Approach in Power Generation Revenue Procedure.](#)

The IRS chose to use a definitional safe harbor in the long-awaited power generation revenue procedure (Rev. Proc. 2013-24, 2013-21 IRB 1) because of the difficulties raised by a percentage safe harbor, Douglas E. Toney, utilities technical specialist, IRS Large Business and International Division, said during a May 16 webcast.

Issued April 30, the Service's latest industry issue resolution guidance provides safe harbor definitions for unit of property and major component that taxpayers may use when applying the disposition rules in the repair regulations (T.D. 9564) to power generation property, according to Carol Conjura of KPMG LLP, whose firm sponsored the webcast.

Conjura noted that the revenue procedure for electric transmission and distribution property (Rev. Proc. 2011-43, 2011-37 IRB 1) uses a percentage safe harbor for expensing.

"A percentage approach would have presented more challenges to implement. These are very different assets than electric and transmission distribution assets," Toney said. "The approach of defining units of property and major components is more administrable and easier to follow than a percentage approach would have been."

Conjura suggested that anticipated guidance on gas transmission property may be more likely to use a percentage safe harbor, given that gas transmission property, unlike power generation property but like electric transmission property, is considered network property.

Toney said the definitions in Rev. Proc. 2013-24 were intended to “reflect the application of the concepts in the regs to these particular and specific types of plant assets used in the generation of steam or electricity.” He added that although that approach “wasn’t driven by the accounting records . . . it will be easier for the power generation companies to identify these major components and units of property because of their accounting records.”

Practitioner Questions

Conjura asked why the guidance didn’t allow for a four-year adjustment period for a positive section 481 adjustment. According to the revenue procedure, “A taxpayer must take the entire net section 481(a) adjustment into account (whether positive or negative) in computing taxable income in the year of change.”

By pushing all of the effects of section 481 into one tax year, all taxpayers will receive the same treatment, regardless of their initial positions, Toney replied.

Peter Baltmanis of KPMG LLP asked whether in the context of the guidance the definitions of different service levels contained in a taxpayer’s long-term service agreement would help determine whether an expense should be capitalized or deducted. Taxpayers in the power generation industry enter into long-term service agreements that may cover the costs connected with the replacement of a major component in connection with an outage.

Although broad generalizations are difficult to make, “the long-term service agreements most likely would be one step removed from a determination of the actual work done. I don’t know that they’d be helpful,” Toney said. “The scope of the work done is probably more clearly reflected in the individual work orders.” He added that an analysis would depend on the facts and circumstances.

Acceptable extrapolation methods are contained in appendix B of the revenue procedure. Baltmanis asked about statistical sampling and whether the procedures in Rev. Proc. 2013-24 differ from those in Rev. Proc. 2011-43.

The basic principles are the same, Toney said, but “the formula was tweaked a little bit to eliminate some unintended results.” The most significant difference is that the initial calculation under Rev. Proc. 2013-24 is performed on a gross basis, not a net basis, he said.

[IRS Publishes Proposed Regs on Community Health Needs Assessment Requirement for Tax-Exempt Hospitals.](#)

The IRS has published proposed regulations (REG-106499-12) that provide guidance to charitable hospital organizations on the community health needs assessment (CHNA) requirements and related excise tax and reporting obligations. The regs also clarify the consequences for failing to meet these and other requirements for charitable hospital organizations.

Comments and requests for a public hearing must be received by July 5. The regs are proposed to be effective for returns filed on or after the date they are published in the Federal Register as final or temporary regulations.

Section 501(r)(1) imposes four additional requirements that organizations described as hospital organizations must satisfy to be tax exempt under section 501(c)(3), one of which is to conduct a CHNA every three years. In July 2011 Treasury and the IRS issued guidance (Notice 2011-52) on the anticipated regulatory provisions.

As a general rule, the proposed regs provide that a hospital organization operates a hospital facility if it is a partner in a joint venture, limited liability company, or other entity treated as a partnership for federal income tax purposes that operates the hospital facility. A hospital organization also operates a hospital facility under the proposed regs if it does so through a wholly owned entity that is disregarded as separate from the hospital organization for federal tax purposes. A hospital organization is not required, however, to meet the requirements of section 501(r) for any activities unrelated to the operation of a hospital facility.

The proposed regs provide that a hospital organization meets the requirements of section 501(r)(3) in any tax year for a hospital facility it operates only if the hospital facility has conducted a CHNA in that tax year or in either of the two immediately preceding tax years. Also, an authorized body of the hospital facility is required to have adopted an implementation strategy to meet the community health needs identified through the CHNA by the end of the tax year in which the hospital facility conducts the CHNA. The regs include extensive rules for conducting a CHNA and developing implementation strategies.

Under the proposed regs, a hospital facility's omission of required information from a policy or report described in reg. section 1.501(r)-3 or 1.501(r)-4 or error regarding the implementation or operational requirements described in reg. section 1.501(r)-3 through 1.501(r)-6 will not be considered a failure to meet a requirement of section 501(r) if the omission or error was minor, inadvertent, and due to reasonable cause and the hospital facility corrects the omission or error as promptly after discovery as is reasonable given the nature of the omission or error. Also, the IRS will consider for purposes of determining whether revocation of section 501(c)(3) status is warranted the relative size, scope, nature, and significance of any failures to meet the section 501(r) requirements as well as the reasons for the failures and whether the same type of failures have previously occurred. The proposed regs include rules that apply if one hospital facility within a hospital organization fails to meet a section 501(r) requirement during a tax year, even though the hospital organization as a whole continues to be recognized as a section 501(c)(3) organization.

Citations: REG-106499-12; 2013-21 IRB 1111; 78 F.R. 20523-20544

IRS: Fraternal Society's Sale of Insurance Policies to Nonmember Spouses Is Unrelated Trade or Business.

In technical advice, the IRS concluded that an entity's sale of life insurance policies to nonmember widows of deceased insured members, under which the widow can name as a beneficiary someone other than a dependent of the member, isn't substantially related to the entity's exempt fraternal purposes.

The parent entity of a fraternal beneficiary society that operates under the lodge system sells individual life insurance contracts to its members. Membership is limited to men. The parent entity and its subordinate chapters have a group exemption under section 501(c)(8). The parent entity was formed to provide aid and assistance to its members and their families and beneficiaries. Within a year following the death of a member who was insured by the parent entity, the nonmember widow

could request insurance coverage under which the widow could name someone other than a dependent of the member as a beneficiary.

The parent entity derives income from frequent and regular sales of insurance contracts to the widows of deceased members. Unless those sales are substantially related to the entity's performance of its exempt fraternal functions, the revenue derived from those sales is includable in the entity's unrelated business taxable income. To determine whether the sales constitute an unrelated trade or business, the IRS examined the relationship between the sales and the furtherance of the entity's fraternal purposes.

The IRS determined that the sale of insurance to a widow is no different than an ordinary contractual relationship between a policyholder and an insurance company: The nonmember spouse is ineligible for membership and, thus, lacks any fraternal relationship or mutuality of interest with the entity's members; the insurance coverage that is offered to the widow after the member's death is not a continuation of the member's policy; the widow may apply for different coverage from that held by the member; and the widow isn't guaranteed coverage. Further, section 501(c)(8) requires that a fraternal beneficiary society provide benefits to the society's members and their dependents but a widow may designate a beneficiary other than a dependent of a member.

Thus, the IRS determined that the sale of insurance policies to nonmember widows of deceased insured members doesn't contribute importantly to the society's exempt fraternal purpose and, thus, isn't substantially related to the entity's exempt fraternal purposes. The IRS concluded that the sale of commercial-type insurance to nonmembers constitutes an unrelated trade or business.

Citations: TAM 201320023

Rules Governing Nonprofits and Political Activity: A Brief Overview.

If you've read the news at all this week, you've likely read about the escalating controversy regarding the IRS' seemingly selective scrutiny of certain organizations, including Tea Party organizations. Without delving into the motivations behind the IRS' actions, the central question they were attempting to answer is whether the groups were operating in a manner consistent with the rules governing the activity of 501(c)(4) nonprofit organizations, the tax status for which they had applied (and were all ultimately granted, to the best of our knowledge). Given the increased attention on the topic, below is a brief overview of the permissible activities and characteristics of nonprofits that engage in political activities.

This is meant to be a basic overview, and there is a tremendous amount of nuance and detail not included here. If you need more detailed information, please see the references at the end and/or consult a specialist in nonprofit or political law. That said, there are three basic types of organizations that engage with the political system:

501(c)(3) Organizations – Public Charities

There are two types of 501(c)(3) organizations: Public Charities and Private Foundations. This section focuses exclusively on Public Charities, which are allowed to participate in the civic sphere in ways that are in line with their charitable mission.

Permitted activities: Voter education, voter registration, policy analysis, issue education, and related nonpartisan activities. Allowed to conduct limited lobbying (defined as "insubstantial") activities.

Organizations have the option to choose an official test (501H election) that sets a concrete limit on lobbying expenditures.

Advantages: Greater fundraising capacity through charity status. Can accept contributions of any size from individuals, corporations, and other nonprofits. Not required to disclose donors to the public, although the information is shared with the IRS on Forms 990.

Disadvantages: Restrictions on allowable political activities. Cannot directly engage in elections. Cannot be involved in lobbying as a primary organization activity.

Examples: League of Women Voters, The Urban Institute

501(c)(4) – Social Welfare Organizations; 501(c)(5) – Labor Unions; 501(c)(6) – Business Leagues

While many, if not most, 501(c)(4) organizations do not engage heavily in lobbying or political activity, the ones that do are supposed to exist in order to “promote the social welfare.” 501(c)(5) and 501(c)(6) organizations are membership-based associations capturing labor/agricultural entities and business entities, respectively.

Permitted activities: Nonpartisan issue and legislative advocacy, lobbying, endorsement of specific legislation.

Advantages: Not required to disclose donors to the public, although shared with the IRS on Forms 990. Can accept contributions of any size; the Citizens United decision allowed for unlimited corporate contributions. Can engage in nonpartisan election campaign-related activity, but that must not be the primary purpose of organization. Can endorse candidates in communication with members, although not with public.

Disadvantages: Must be nonpartisan. Cannot publicly (outside of membership) endorse or overtly support or oppose political candidates. No contributions to 501(c)(4) organizations for lobbying or political activity are tax-deductible, by individuals or businesses. In 501(c)(6) organizations, the portion of membership dues used for lobbying and political expenditures cannot be claimed by members as a business expense and deducted from tax liability.

Examples: AARP (c4), Crossroads GPS (c4), Tea Party Patriots (c4), SEIU (c5), Chamber of Commerce (c6)

527 Organizations – Political Action Committees

Section 527 of the tax code encompasses all forms of organizations engaged directly in electoral politics, including candidate and political party committees. This section focuses on independent Political Action Committees that are predominantly-though not exclusively-organized under Section 527, both “traditional” PACs and the newer SuperPACs that emerged following the 2010 Citizens United decision. There is another notable type of independent spending committee known informally as the “527” that can raise and spend money on elections in unlimited amounts without endorsing specific candidates, but these organizations are now significantly less prevalent and influential than they were around a decade ago.

Permitted activities: Partisan-oriented activities to influence elections. Explicit support of or opposition to individual candidates.

Advantages: “Traditional” PACs can engage in direct political activity and endorse candidates. SuperPACs can raise money in unlimited amounts from individuals or corporate/organizational

donors.

Disadvantages: Required to disclose donors to the public through the Federal Election Commission. "Traditional" PACs have \$5000 contribution limits. SuperPACs are not allowed to coordinate with candidate committees. Lobbying activities are not necessarily tax-exempt.

Examples: EMILY's List (PAC), American Crossroads (SuperPAC)

Each structure serves a specific function within the political sphere, but reviewing applications of all politically oriented organizations to ascertain whether the proposed activities fit into the allowable activities of the organization type they have chosen seems prudent. However, many of the lines between these organizational types are blurry. Of particular relevance to the current controversy, 501(c)(4) social welfare organizations in practice run issue-based attack ads that look a lot like attempts to influence the outcome of an election. With little guidance from Congress, the IRS is left with the unenviable task of sorting out whether organizations engaged in such activities are merely toeing that blurry line or outright crossing it in some objective way.

If you want to learn more, here are some resources:

Chapter 10 of the 2006 book *Nonprofits and Government: Collaboration and Conflict*, published by Urban Institute Press, is devoted to permissible activities for politically active nonprofits.

The Alliance for Justice offers details about the permissible political activities of 501(c)(4) organizations.

The National Center for Charitable Statistics website has more general information about 501(c)(4), c5, and c6 organizations.

The IRS offered detailed guidance on the "Political Campaign and Lobbying Activities of IRC 501(c)(4), (c)(5), and (c)(6) Organizations" in 2003.

The Congressional Research Service released a more recent study looking at the role of SuperPACs in federal elections and their relation to other types of political organizations.

The IRS 2012 Data Book has details on the number of 501c organizations by type, including those applying for tax exemption and how many were reviewed more closely and ultimately rejected. See the tables on pages 55 and 56.

Author: Jeremy Koulish

[Comments Sought on Exempt Organization E-File Form.](#)

The IRS, as part of a paperwork reduction effort, has asked for public comment on Form 8453-EO, "Exempt Organization Declaration and Signature for Electronic Filing"; comments are due by July 15, 2013.

[Tea Party Flap Highlights the Road to Exemption.](#)

The uproar surrounding the revelation that the IRS gave extra scrutiny to the exemption applications of conservative groups, resulting in delays in the applications' processing, may have people wondering how the process is supposed to work.

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That possibility may have been on the minds of IRS officials on May 15 when they released a Q&A explaining the exemption application process, including how the IRS handles applications of organizations that may engage in political or advocacy activities. Detailed information is also available at <http://www.irs.gov/eo>.

Numerous Tea Party groups and other conservative entities sought to qualify as tax-exempt organizations described in section 501(c)(4). To qualify, an organization must operate primarily to further the common good and general welfare of the people of the community, according to the IRS. Civic leagues, homeowners associations, and volunteer fire companies can qualify as social welfare organizations.

An organization that believes it meets the qualifications for exemption must decide whether to declare itself exempt or apply to the IRS for exemption. Rosemary E. Fei of Adler & Colvin said most of her firm's clients apply for exemption because they want the IRS to bless their proposed activities in writing and because potential donors may want to see a favorable determination letter. (Contributions to a section 501(c)(4) organization are not deductible, however.) A favorable determination letter also grants the organization advantageous postage rates and exemption from some state taxes.

To apply for exemption under section 501(c)(4), an organization must file a Form 1024, "Application for Recognition of Exemption Under Section 501(a)," which is more than 25 pages and asks about the organization's activities, revenues and expenses, assets and liabilities, and other issues. Organizations seeking exemption as a charity under section 501(c)(3) instead file a Form 1023, "Application for Recognition of Exemption Under Section 501(c)(3)."

Using Form 1024 requires a user fee of \$400 for organizations with annual gross receipts of \$10,000 or less during the preceding four years, or of \$850 for organizations with annual gross receipts exceeding \$10,000 for the preceding four years.

An organization also must have an employer identification number, even if it has no employees. The EIN can be obtained by filing Form SS-4, "Application for Employer Identification Number."

Exemption applications are sent to the IRS determinations center in Cincinnati. If the application is complete, the IRS will send the organization a letter of acknowledgement; incomplete applications will be returned. If the IRS needs more information to determine whether the organization qualifies for exemption, it will ask the applicant for the information by a specified date.

Applicants will be informed if their applications are forwarded to IRS headquarters for review. In its Q&A, the IRS said the Cincinnati office may consult with tax law specialists in Washington on how the law applies to a particular case.

Fei said that if an application is in a category singled out for special attention, it will be assigned to a dedicated group of agents. In that case, the applicant can expect a significantly longer wait for one of those few agents to become available, she said. The applicant may also be asked questions that do

not seem directly relevant to the application or that have already been answered, she added.

The applicant will normally receive a determination letter after the IRS gets all the information it needs, Fei said. An organization whose application is denied will receive a letter explaining why the IRS believes it does not qualify for exempt status, and it has 30 days to protest. If the IRS does not receive a protest within that time frame, the proposed denial becomes final. Organizations seeking exemption under section 501(c)(3) may petition the Tax Court, the Court of Federal Claims, or the D.C. district court for declaratory judgment that they qualify, but the IRS's determination is final for section 501(c)(4).

The Tea Party controversy may have arisen because the IRS decided to form a dedicated group to handle the applications of social welfare organizations with possible political or advocacy agendas, "since they certainly would present legal issues that would require more knowledge to review than typical applications," Fei said. The group would have had to identify indications that applications needed specialized review, and it may have occurred to someone in the group that having "Tea Party" in an organization's name might point to a political focus that warranted careful scrutiny, she said.

"It was stupid because of the appearance of bias, but in terms of efficient use of limited IRS resources, not unreasonable," Fei said.

by Fred Stokeld

Guidance Planned for Intermediate Violations of Community Needs Assessment Rules.

The IRS is developing guidance on correction and disclosure of section 501(r) violations that are more than minor or inadvertent but less than egregious or willful, a Treasury Department official said May 15.

The guidance is likely to take the form of a revenue procedure and will provide hospitals with more details on remedying failures to comply with section 501(r) requirements, of which community health needs assessments (CHNAs) are one, and a way to keep those details fresh, Ruth Madrigal, attorney-adviser in the Treasury Office of Tax Legislative Counsel, said during a luncheon program sponsored by the District of Columbia Bar Taxation Section's Exempt Organizations Committee.

The intermediate violations comprise "a large range, but I think we gave the outlines of it in the proposed regs that there would be a mechanism for disclosure and correction," Madrigal said after the luncheon, referring to REG-106499-12. "And so I think we need to put some meat on those bones," she said, adding that officials hope to release the new guidance before the final regs.

The proposed regs say Treasury and the IRS plan to publish guidance to help hospital facilities correct failures to meet CHNA requirements and other rules under section 501(r) and to inform them how to disclose the corrections.

Revocation of a hospital's exemption is possible but won't be a knee-jerk response, Madrigal said. The proposed regs lay out several factors the IRS will consider when deciding whether to revoke exempt status, including the size and scope of the failures. Madrigal said she believes the factors would be applied when the failure was known, which would typically be during an audit. But she said hospitals she's spoken with and those who regularly counsel hospitals are working hard to avoid all

failures, so a willful or egregious failure would be rare.

Minor and inadvertent failures won't be considered failures if corrected reasonably promptly after they're found, Madrigal said, giving the example of a hospital failing to widely publicize its policy for a few days because its posted financial assistance policy fell under a sofa and the website hosting the policy crashed due to malware.

"The things that are truly minor, foot faults, they don't need to be discussed," Madrigal said.

Schedule H

Alexander L. Reid of Morgan, Lewis & Bockius LLP said there are discrepancies between the instructions on Schedule H of the Form 990, "Return of Organization Exempt from Income Tax," and the proposed regs under section 501(r). For example, the definition of a hospital is broader in the instructions than in the proposed regs, raising the question of which should be relied on, Reid said. Typically after a statutory change makes an IRS form obsolete, the IRS has attached a cover sheet with instructions on how to proceed, but that hasn't happened yet, he said.

"It would be premature to change the form until we do have final regulations in place," said Amy Giuliano, attorney-adviser in the IRS Office of Associate Chief Counsel (Tax-Exempt and Government Entities). "We're planning to change [Schedule] H when the regulations are finalized."

by David van den Berg

Cardin Bill Would Clarify Church Pension Plan Treatment.

The Church Plan Clarification Act of 2013 (S. 952), introduced by Senate Finance Committee member Benjamin L. Cardin, D-Md., would make code changes for religious institution pension plans to provide clarity and to bring them more in line with other qualified plans.

Citations: S. 952; Church Plan Clarification Act of 2013

Travel Reimbursement Policies: What you need to know!

In keeping with the IRS mission of providing America's taxpayers with top-quality service by helping you understand and meet your tax responsibilities, the office of Federal, State and Local Governments will host a phone forum on May 28th to assist you in determining the proper tax treatment of various allowances and reimbursement payments.

To learn more, we cordially invite you to attend the "Travel Reimbursement Policies: What you need to know!" Phone Forum. This forum is tailored for federal, state and local government board members and employers, payroll and benefits administrators.

- During this 60-minute presentation we will cover:
- Accountable plan rules
- Payment not covered under an accountable plan
- Board member payments or stipends
- Car allowance payment policy

- Meal allowances
- Fringes benefits

You can register at Travel Reimbursement Policies Phone Forum. Please register as soon as possible because space is limited.

If you have any travel reimbursement or allowance payments questions, please e-mail them to: te.ge.fslg.outreach@irs.gov by May 21, 2013, and we will try to answer them during the phone forum. Please use the subject line: Travel Reimbursement Policies.

We look forward to the opportunity to serve you on May 28th.

Register at:

<http://apps.irs.gov/app/scripts/exit.jsp?dest=http://ems.intellor.com/index.cgi?p=204699&t=71&do=register&s=&rID=418&edID=305>

[IRS: Many Tax-Exempt Organizations Must File with IRS By May 15 to Preserve Tax-Exempt Status.](#)

A key deadline of May 15 is facing many tax-exempt organizations that are required by law to file annual reports with the Internal Revenue Service. Organizations will see their federal tax exemptions automatically revoked if they have not filed reports for three consecutive years.

The Pension Protection Act of 2006 mandates that most tax-exempt organizations file annual Form 990-series informational returns or notices with the IRS. Under this law, organizations that fail to file reports for three consecutive years automatically lose their federal tax-exempt status. The law, which went into effect at the beginning of 2007, also imposed a new annual filing requirement on small organizations. Churches and church-related organizations are not required to file annual reports.

Form 990-series information returns and notices are due on the 15th day of the fifth month after an organization's fiscal year ends. Organizations that need additional time to file may obtain an extension.

Many organizations use the calendar year as their fiscal year, which makes May 15 the deadline for them. Organizations that fail to file annual reports for three consecutive years will see their tax exemptions automatically revoked as of the due date of the third required filing.

Small tax-exempt organizations with average annual receipts of \$50,000 or less may file an electronic notice called a Form 990-N (e-Postcard), which asks organizations for a few basic pieces of information. Tax-exempt organizations with average annual receipts above \$50,000 must file a Form 990 or 990-EZ, depending on their receipts and assets. Private foundations file a Form 990-PF.

The IRS began to publish the names of organizations identified as having automatically lost their tax-exempt status for failing to file annual reports for three consecutive years. Organizations that have had their exemptions automatically revoked and wish to have that status reinstated must file an application for exemption and pay the appropriate user fee.

The IRS offers an online search tool, Exempt Organizations Select Check, to help users more easily

find key information about the federal tax status and filings of certain tax-exempt organizations, including whether organizations have had their federal tax exemptions automatically revoked.

JCT Releases Tax Reform Working Group Report.

A May 6 report by the Joint Committee on Taxation prepared for the House Ways and Means Committee summarizes current tax law, selected tax reform proposals, and suggestions submitted to the committee's tax reform working groups.

[http://services.taxanalysts.com/taxbase/eps_pdf2013.nsf/DocNoLookup/11003/\\$FILE/2013-11003-1.pdf](http://services.taxanalysts.com/taxbase/eps_pdf2013.nsf/DocNoLookup/11003/$FILE/2013-11003-1.pdf)

IRS Spells Out Policy on E-Mail Searches During Investigations.

The IRS will obtain a search warrant in all cases when seeking the content of stored e-mail communications from internet service providers, the IRS announced in a May 3, 2013, policy statement, adding that it will not seek e-mails from an ISP in civil administrative proceedings.

[http://services.taxanalysts.com/taxbase/eps_pdf2013.nsf/DocNoLookup/11183/\\$FILE/2013-11183-1.pdf](http://services.taxanalysts.com/taxbase/eps_pdf2013.nsf/DocNoLookup/11183/$FILE/2013-11183-1.pdf)

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Urban Institute Reviews Charitable Contributions Deduction.

This paper attempts to better understand rhetoric over the charitable contributions deduction, arguing that debate surrounding the deduction is ultimately a projection of more fundamental debates relating to the theme of government versus charity. The phrase “government versus charity” can mean government as opposed to charity or government in opposition to charity. The first sense contemplates the need to choose which of government versus charity should supply a given good or service. The second sense contemplates the ideal regulatory posture of government in relation to charity. Competing views over the charitable contributions deduction often reduce to competing views over these two issues.

The full paper is available at:

<http://www.urban.org/UploadedPDF/412818-The-Charitable-Contributions-Deduction.pdf>

IRS: Restriction on Use of Property Affects Its Fair Market Value.

In a legal memorandum, the IRS concluded that a restriction on the use of donated property within the boundaries of a national park affects the fair market value of the property under section 170.

A taxpayer claimed a charitable deduction for a donation to the National Park Service of land and mineral rights located in a national park. Before the donation, mining was phased out in the park after Congress passed the Mining in the National Parks Act of 1976. Mining was then resumed on a limited basis for years until the last of the mines in the park was closed.

Under section 170, the fair market value of a property determines the amount of the contribution and is calculated as the price at which the property would change hands between a buyer and a seller.

The IRS said examiners should determine if the donated property’s highest and best use is for mining and whether existing legal restrictions on mining are likely to be removed for a potential owner. The IRS also said examiners should consider whether the property became worthless in the year that mining operations in the park were closed.

Citations: ILM 201319010

IRS Looks to Build on College and University Project.

After releasing the almost complete results of more than 30 examinations of colleges and universities on their compensation and unrelated business income last month, the IRS plans to gather more information from across the exempt sector, an agency official told a congressional subcommittee May 8.

Speaking at a hearing of the House Ways and Means Oversight Subcommittee, Lois Lerner, exempt organizations director in the IRS Tax-Exempt and Government Entities Division, said the agency has “already started a second unrelated business income project.”

“We are looking at organizations that are reporting unrelated business activity on their 990s but they’re not filing a [Form] 990-T,” Lerner said. “We think that’s problematic.”

That project started in the current fiscal year, Lerner said, adding that she couldn’t predict when the examinations would be completed.

In response to a question from Ways and Means member Diane Black, R-Tenn., Lerner said plans are in the works to review multiple types of exempt organizations. “I think that it is very important to broaden this out and see what kind of activities are going on in other tax-exempt organizations, because this was a homogeneous group,” she said. “We want to look farther, and we are developing a project for our next year’s workplan that will do just that.”

Other colleges and universities may be included in the larger study, Lerner said.

Lerner was the lone witness at the hearing about the IRS’s colleges and universities compliance project final report released in April. The report provided findings of more than 30 examinations of colleges and universities on compensation and unrelated business income. With more than 90 percent of the exams finished, the IRS said they resulted in more than 180 adjustments to unrelated business taxable income amounts. The report also revealed that about 20 percent of the private colleges and universities examined failed to meet the rebuttable presumption standard for compensation. (Prior coverage .)

Subcommittee Chair Charles W. Boustany Jr., R-La., asked about the report, noting that colleges and universities and their advisers were frequently wrong about the classification of activities and allocation of expenses related to activities.

“What we did not see was organizations that didn’t seem to have a thought out reason for classifying things the way they classified them,” Lerner said. “But it is very factual related and there were disagreements between the IRS and the organizations, and I think by putting this report out and doing some other work around the issue that we can probably benefit the college and university sector as well as the exempt sector in general.”

“This investigation is notable for what you uncovered,” said Ways and Means member Joseph Crowley, D-N.Y. “And I think we’re all disturbed by what you have discovered in terms of abuse within college and university systems.”

Boustany noted that discussions about tax reform are taking place and said the report contains some troubling details about tax-exempt organizations and how they report unrelated business income and determine executive compensation. He asked Lerner if the report suggested the presence of structural problems within the tax-exempt sector, or if more targeted changes were needed.

"I think that it's really important for us to get more information than [on] just these 34 organizations, because they were selected because of potential noncompliant activity," Lerner responded. "I would like to gather more information more broadly to see where the real issues are that could be addressed before changes were made."

Lerner, in response to questioning from Oversight Subcommittee ranking minority member John Lewis, D-Ga., said that the examinations do not represent a statistically valid sample and that the results apply only to the 34 examined organizations. Four hundred questionnaires that were sent to randomly selected colleges and universities and were completed before the examinations, however, do represent a statistically valid sample and can be considered generally representative of how colleges and universities act, she said.

Lewis also asked whether anything was learned from the examinations that could be useful in investigating other areas of the exempt sector. Lerner said there was.

"This is the first time that we've actually looked beyond the fact that the organizations were using comparables to see whether the comparables were really in fact comparable," she said. "And when I speak to groups about this, what I caution the board members and the executive directors about is, don't just accept the report from a compensation consultant — you need to ask them questions about this. Because it can be done correctly, and obviously the organizations are trying to do it correctly."

Boustany Cites High Noncompliance by Colleges on UBIT.

An IRS review of exempt colleges found "almost universal noncompliance by some of the most sophisticated organizations in the tax-exempt sector," particularly in their calculation of unrelated business income taxes, House Ways and Means Oversight Subcommittee Chair Charles W. Boustany Jr., R-La., said at a May 8 hearing.

[http://services.taxanalysts.com/taxbase/eps_pdf2013.nsf/DocNoLookup/11266/\\$FILE/2013-11266-1.pdf](http://services.taxanalysts.com/taxbase/eps_pdf2013.nsf/DocNoLookup/11266/$FILE/2013-11266-1.pdf)

Elected Constables Are Employees for Tax Purposes; County Is Employer.

In partially redacted field attorney advice, the IRS concluded that a state's elected constables aren't subject to self-employment tax, are employees for FICA and income tax withholding purposes, and that the county is the statutory employer for employment tax purposes because it controls payment to the constables.

This memorandum responds to your request for advice dated June 13, 2012, regarding the above taxpayer. This advice may not be used or cited as precedent in other cases. This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as the attorney-client privilege. If disclosure becomes necessary, please contact this office for our views.

ISSUES

1. Are the elected constables serving * * * ("constables") covered under a section 218 agreement?

2. Are the constables considered fee-based public officials for purposes of I.R.C. § 1402(c)(1) and therefore subject to self-employment tax?
3. Are the constables employees for the purposes of the Federal Insurance Contributions Act ("FICA")?
4. Are the constables employees for the purposes of federal income tax withholding ("ITW") requirements?
5. If constables are employees, who is the employer for federal employment tax purposes?

SUMMARY CONCLUSIONS

1. The constables are covered by a section 218 agreement, as established by the letter you received from the Social Security Administration. * * *
2. The constables are not solely fee-based as required by section 1402(c)(1), and therefore they are not fee-based public officials. The constables are not subject to self-employment tax.
3. The constables are employees based on the common law employee analysis and are therefore employees for purposes of FICA.
4. The constables are employees for the purposes of ITW pursuant to I.R.C. § 3401(c) because they are elected officials.
5. The employer of the constables for employment tax purposes is the County. The County controls the payment to the constables and is therefore the statutory employer under I.R.C. § 3401(d)(1).

FACTS

Background

Both the State and the County have section 218 agreements¹. In order to determine whether the constables are covered under the State or County 218 agreements, you requested a determination from the Social Security Administration ("SSA") regarding whether the constables were covered under either 218 agreement. * * *, you received a letter from SSA which stated that the constable position is covered under the State 218 agreement. * * *

The County made payments to approximately * * * constables totaling approximately \$* * * during the years at issue. The constables perform various services such as prisoner transport, service of summonses and warrants, court protection within the Magisterial Courts of Pennsylvania, and services relating to landlord/tenant disputes and resolutions.

Constables are elected officials within a local government in the State. The constables are required to take an oath of office and undergo a background check. They must also receive State-provided training and certification prior to performing services as a constable. Constables must provide proof to the clerk of courts that they hold professional liability insurance in amounts set by statute in order to maintain certification. Once constables are certified by the State, they have statewide authority and jurisdiction enabling him to perform services throughout the state, not just in the local area in which they were elected. Therefore, the constables may perform services for and receive payment from multiple counties. In some counties, constables serve as the primary means of law enforcement.

Constables are covered by quasi-judicial immunity. See e.g. *Berg v. Allegheny County*, 219 F.3d 261 (3d Cir. 2000). However, upon election, a constable must post a bond between \$500 and \$3000 as directed by the court to be held in trust for the use and benefit of persons who may sustain injury by reason of neglect of duty. 44 Pa C.S.A. § 7114(c).

Enacted in October of 2009, Part IV of Title 44 of the Pennsylvania Code, titled “Other Officers,” sets out the provisions of State statute relating to constables. Part IV contains one chapter, Chapter 71 titled “Constables.” Chapter 71 includes subchapters outlining election, appointment, conflicts, training, powers and duties, compensation, and penalties and remedies.² A constable is elected for a term of six years. 44 Pa. C.S.A. § 7111 (2009). Constables can be re-elected for an unlimited number of terms. Per your interviews, many constables have a continuing and ongoing relationship with the County. Some of the constables in the County have held office for between 20 and 30 years. When a constable vacancy occurs, the court of common pleas for the county where there is a vacancy must appoint an individual to serve as a constable for the remainder of the term. Id. § 7121. The constable has sole power to appoint deputy constables, subject to approval of the court of common pleas. Id. § 7122.

State statute provides “[w]hile a constable or deputy constable is performing duties other than judicial duties, regardless of whether or not he is certified under this subchapter, he shall not in any manner hold himself out to be active as an agent, employee, or representative of any court, magisterial district judge or judge.” Id. § 7142(f) (emphasis added). Prior to 2009, State statute provided that a constable was an independent contractor and not an employee of the Commonwealth, the judiciary, the township, or the county in which he works. This provision appears to follow a ruling of the Supreme Court of Pennsylvania which held unconstitutional as a violation of separation of powers a provision attempting to make constables employees of the State judiciary because constables perform functions of the executive branch. In re Act 147 of 1990, 528 A.2d 985, 990. (Pa. 1991).

Constable Training and Certification

State statute provides for the establishment of a board responsible for establishing, implementing and administering a constable education and training program. 44 Pa. C.S.A. § 7144 (2009). The board also certifies constables and deputy constables who have completed training requirements. Id. The constables must complete a total of 80 hours of initial training and comply with a mandatory continuing education program which may include no more than 40 required hours per year. Id. §§ 7145, 7146. Constables interviewed stated they must also attend an additional 40 hours of training for required firearms certification. The mandatory curriculum for the training consists of topics including: role of the constable in the justice system; professional development; civil law process; criminal law process; mechanics of arrest; prisoner transport and custody; and court security. State statute establishes an account to provide funds for the constable training program; the account is funded by a surcharge collected by constables as a court cost and turned over to the Department of Revenue. Id. § 7149.

Constable Powers and Duties

State statute also sets out the powers and duties of the constables. Constables are required to serve at all elections by preserving the peace at polling places. Id. § 7152. The statute directs constables to arrest individuals without a warrant for various offenses. Id. § 7158. Constables may serve as coroner; collect taxes under a warrant issued by the tax collector; and arrest a person trespassing upon any forest. Id. §§ 7154-7156.

Constables must impound trespassing livestock and notify owner to collect livestock and pay the

constable for the cost of damage, care and fee for the constable. Id. § 7159. If the owner fails to pay, the livestock shall be sold at a public sale and the all money realized from the sale will be turned over to the magisterial district judge. Id. § 7159.1. The magisterial district judge then distributes payment to the landowner for damages and the constable for his services. Id.

Some other duties which constables may perform include, but are not limited to, the following: transporting defendants to arraignments and hearings; carrying out sales and ejectments in landlord-tenant disputes; serving complaints, summonses and notices; providing courtroom security; executing warrants of arrest; serving notice of election to township or borough officers; seizing registration plates and drivers' licenses. Id. §§ 7161, 7165. Criminal subpoenas can be served by police officers or constables. Sheriff's deputies are also permitted to transport prisoners.

Constables generally set their own hours of work. The magisterial district judges assign work to the constables. The constables interviewed indicated that they can turn down work but do so at the risk of not getting future assignments from that judge. The constables interviewed stated that the judges are the bosses and make the rules. A constable must be present in the courtroom when a magisterial district judge is present in court. Therefore the magisterial district courts cannot function without the services of the constable. The constables view themselves as "officers of the court." Police officers in the county do not provide courtroom or courthouse security. Sheriff's deputies perform courtroom security for the "major" courts.

Constables must provide some of the supplies necessary for the performance of their duties. For example, they must provide their own vehicles for prisoner transport, clothing, guns, ammunition and handcuffs. Some judges require a constable to be in uniform when providing courtroom security, while others simply require the constables dress professionally. There is no state-mandated uniform for constables. The court provides metal detectors and wands. Some courts also provide constables with desk space or an office. The State issues the constables ID badges with the title "PA State Constable."

***. Constables are not prohibited from performing services for private entities, ***. Constables must carry an additional liability insurance policy if he performs private work.

Constable Guidelines and Discipline

***. ***. A State constable handbook is in the process of being drafted ***. During the required constable training, the constables must abide by a State-issued classroom code of conduct. The constables you interviewed stated that the State regulates how they do their job.

State statute provides for discipline of constables through Subchapter H, Penalties and Remedies. A court of common pleas may inquire into the official conduct of the constable and remove the constable from office if it determines the constable is incompetent. Id. § 7172. A constable's compensation may be withheld if he defaults on remittance of collected tax. Id. § 7173. A constable may also be subject to fines and criminal penalties for neglecting or refusing to perform duties. Id. §§ 7175, 7178. As public officials, constables are required to file Statements of Financial Interests annually with the State Ethics Commission.

Constable Payment

Constables are paid according to schedules set by statute. Where the constable is performing a service on behalf of a litigant, for example, the litigant is required to pay the constable fees in advance to the court for services desired to be performed. Id. § 7161(d). According to State statute, the court is to turn the fees over to the constable as soon as possible. Id. § 7161(e). In criminal

cases, the constable fees are charged to the defendant; however, if the defendant is discharged or indigent, the fee is assessed to the county. Id. § 7161(g)(16). * * *.

Constables are reimbursed for actual mileage traveled. Id. § 7161. In certain cases when transporting prisoners, the constable may, at his discretion, be accompanied by a second constable or deputy constable; in these cases each constable shall receive payment for the transportation. Id. For services performed relating to elections, constable compensation is paid by the county. Id. § 7163. The Department of Motor Vehicles pays the constables for seizing registrations and drivers' licenses. Id. § 7165.

Constables are permitted by statute to collect monies from the public for certain items, including outstanding fines and constable fees and surcharges. Amounts collected by the constable must be turned over entirely to the court within time frames set by statute. The court then distributes payment to the constables. * * *.

* * *. Payments for election day services are paid from a separate fund by the Board of Elections.

LAW AND ANALYSIS

1. Coverage Under a Section 218 Agreement

The SSA determines whether the workers are employees within the meaning of section 210(j) of the Social Security Act, which applies the common law rules. If the SSA determines that an individual worker is covered under the section 218 agreement, the Service then has jurisdiction over the liability for FICA taxes with respect to wages paid to such individual. See I.R.C. section 3121(d)(4).

The determination of who is covered under the terms of a section 218 agreement is under the jurisdiction of the SSA. See Sec 3 (page 3) of the attached 2002 IRS-SSA MOU. The final determination of federal tax liability is under the jurisdiction of the Service. The enforcement mechanism with respect to section 218 agreements is also with the Service because the payments under the agreements are treated as FICA taxes.

The SSA (Regional Office III, Philadelphia) has determined that the constables are covered under the State 218 agreement. * * *.

2. Fee-Based Public Officials Subject to Self-Employment Tax

Before we apply the common law employee analysis, we must determine whether the constables are fee-based public officials for the purposes of the Self-Employment Contributions Act ("SECA"). If the constables are fee-based public officials, they are subject to SECA rather than FICA ("fee-based public official exception"). SECA is imposed on the self-employment income derived by an individual from any trade or business carried on by such individual. I.R.C. §§ 1401, 1402(a).

The general rule is that the performance of the functions of a public office does not constitute a trade or business. I.R.C. § 1402(c)(1), Treas. Reg. § 1.1402(c)-2(a). However, when those functions are compensated solely on a fee basis, the performance of those functions does constitute a trade or business. I.R.C. § 1402(c)(1).

The statute provides that a trade or business does not include "the performance of the functions of a public office, other than the functions of a public office or of a State or political subdivision thereof with respect to fees received in any period in which the functions are performed in a position compensated solely on a fee basis". I.R.C. § 1402(c)(1). Treas. Reg. § 1.1402(c)-2(a)(2) provides:

If an individual receives fees after 1967 for the performance of the functions of a public office of a State or a political subdivision thereof for which he is compensated solely on a fee basis, and if the service performed in such office is eligible for (but is not made the subject of) an agreement between the State and the Secretary of Health, Education, and Welfare pursuant to section 218 of the Social Security Act to extend social security coverage thereto, the service for which such fees are received constitutes a trade or business within the meaning of section 1402(c) and § 1.1402(c)-1. If an individual performs service for a State or a political subdivision thereof in any period in more than one position, each position is treated separately for purposes of the preceding sentence.

Therefore, “fee-based public officials” are public officials — (1) who receive fees; (2) whose positions are compensated solely on a fee basis; and (3) who are not subject to a 218 agreement. Fee-based public officials are subject to SECA rather than FICA. A public office includes any elective or appointive office of a State or its political subdivision. Treas. Reg. § 1.1402(c)-2(b). Examples include a county commissioner, a judge, a marshal, a sheriff, a constable or a notary public. *Id.* The constables in the County are elected and are therefore public officials.

Next we must determine whether the constables are compensated solely on a fee basis. The IRS position on what constitutes a fee is clarified in Revenue Ruling 74-608. In Rev. Rul. 74-608, State statute required an elected tax collector to account for and turn over all tax collections to the treasurer of each taxing authority. State statute also authorized the taxing authority to set a salary, wage, or commission, not to exceed 5% of the tax collected, as remuneration for the tax collector. His remuneration for his term in office was a fixed percentage of the amounts collected and turned over for each taxing authority; specifically, 3 percent from the county, 4 percent from the township and 2.8 percent from the school district. The revenue ruling finds that the tax collector is not a fee-based public official because his remuneration was a salary from a government fund rather than fees collected directly from the public. Rev. Rul. 74-608 provides.

When a public official receives his remuneration in the form of fees directly from the members of the public with whom he does business, such remuneration is ‘fees’ within the meaning of section 1402(c)(1) of the Act. When, however, a public official receives his remuneration or salary from a government fund and no portion of the monies collected by him belongs to or can be retained by him as compensation, the remuneration is not ‘fees’ under section 1402(c)(1).

In Rev. Rul. 74-608, not only was the tax collector turning over what he collected from the public to the taxing authority, but also the taxing authority had the authority to determine what his remuneration would be and paid with general government funds.

For some of their duties, the constables serving this County collect monies from the public and turn them over to the County. The County then pays then constables an amount set by statute. Often the amount collected is equal to the amount due to the constable by statute. The constables also receive other payments for their services that do not come directly from the public. For example, they receive payments directly from the County for their services on Election Day. In addition, they receive a payment directly from the judge for the sale of livestock. Therefore, the constables are not solely fee-based for the purposes of SECA, as required by the clear statutory language of section 1402(c)(1).

In addition, as noted above, according to SSA, the constables are covered under the State 218 agreement. Coverage under a 218 agreement also removes the constables from the provisions of SECA pursuant to section 1402(c)(1). Therefore, the constables do not qualify for the fee-based public official exception.

3. Employees for the Purposes of FICA

The definition of employee for purposes of FICA includes “any individual who, under the usual common law rules applicable in determining the employer-employee relationship, has the status of an employee” and “any individual who performs services that are included in an agreement entered into pursuant to section 218 of the Social Security Act.” I.R.C. § 3121(d). Since SSA has determined that constables are included in the State’s section 218 agreement, they must be treated as employees for purposes of FICA. * * *.Whether an employer-employee relationship exists in a particular situation is a factual question to which common law principles apply. See *Weber v. Commissioner*, 103 T.C. 378, 386, aff’d. 60 F.3d 1104 (4th Cir. 1995); *Nationwide Mutual Ins. Co. v. Darden*, 503 U.S. 318, 323 (1992). Factors which are considered include: (1) the degree of control exercised by the principal; (2) which party invests in work facilities used by the individual; (3) the opportunity of the individual for profit or loss; (4) whether the principal can discharge the individual; (5) whether the work is part of the principal’s regular business; (6) the permanency of the relationship; and (7) the relationship the parties believed they are creating. *Weber v. Commissioner* at 387. See also, *Avis Rent A Car System v. United States*, 503 F.2d 423 (2d Cir. 1974); *Ewens & Miller, Inc. v. Commissioner*, 117 T.C. 263, 270 (2001).

The Treasury Regulations also offer guidance in making a determination as to whether workers are employees or independent contractors:

Generally such relationship exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished. That is, an employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done. In this connection, it is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if he has the right to do so. The right to discharge is also an important factor indicating that the person possessing that right is an employer. Other factors characteristic of an employer, but not necessarily present in every case, are the furnishing of tools and the furnishing of a place to work, to the individual who performs the services. In general, if an individual is subject to the control or direction of another merely as to the result to be accomplished by the work and not as to the means and methods for accomplishing the result, he is an independent contractor. An individual performing services as an independent contractor is not as to such services an employee under the usual common law rules. Individuals such as physicians, lawyers, dentists, veterinarians, construction contractors, public stenographers, and auctioneers, engaged in the pursuit of an independent trade, business, or profession, in which they offer their services to the public, are independent contractors and not employees.

Treas. Reg. § 31.3121(d)-1(c)(2).

Additionally, Rev. Rul. 87-41 identifies twenty factors, based on an examination of cases and rulings, which indicate whether sufficient control is present to establish an employer-employee relationship. These twenty factors are to be used as a guide in determining employment status; however, special scrutiny may be required to ensure that formalistic aspects of an arrangement do not obscure its substance. The factors are (1) instructions, (2) training, (3) integration (whether the worker’s services are so integrated into business operations that success of continuation of business depend upon those services), (4) services rendered personally, (5) hiring, supervising and paying assistants, (6) continuing relationship, (7) set hours of work, (8) full time required, (9) doing work on employer’s premises, (10) order or sequence set (worker must perform services in the order or sequence determined by the person for whom services are performed), (11) oral or written reports, (12) payment by hour, week, month, (13) payment of business and/or travel expenses, (14) furnishing of tools and materials, (15) significant investment (if worker invests in facilities, this is an

indication of independent contractor status; however, if there is a lack of investment on the part of the worker, it indicates a status of employee), (16) realization of profit or loss (if worker can realize a profit or loss, it indicates independent contractor status), (17) working for more than one firm at a time, (18) making service available to the general public, (19) right to discharge, and (20) right to terminate.

More recently the Service considers the issue under three primary categories of evidence — behavioral control, financial control, and relationship of the parties. Refer to IRM 4.23.5-1 and Independent Contractor or Employee? Training Materials, Training 3320-102 (10-96). Facts that illustrate behavioral control, or whether there is a right to direct or control how the worker performs the specific task for which he or she is hired, are (1) instructions and (2) training. Facts that illustrate financial control, or whether there is a right to direct or control how the business aspects of the worker's activities are conducted, are (1) significant investment, (2) unreimbursed expenses, (3) services available to the public, (4) method of payment, and (5) opportunity for profit or loss. Facts that illustrate the relationship of the parties are (1) employee benefits, (2) intent of parties/written contracts, (3) permanency, (4) discharge/termination, and (5) regular business activity.

The facts regarding behavioral control indicate that the constables are employees. The constables must undergo 80 hours of initial training plus up to 80 hours of additional training each year. * * *. These facts indicate that the State and/or the County have control over how the constables perform their duties.

The facts regarding financial control are mixed. The constables must turn over all monies collected to the County and then only receive payment if they properly submit forms according to the County's procedures and a judge signs off on those forms. This indicates control over the finances at the County and State level. The constables are reimbursed for their mileage and are provided some tools (metal detectors, desk). However, the constables must provide some of the tools needed themselves (cars, guns, ammunition, etc.). The constables also make an investment by posting a bond upon election. However, the constables have a minimized financial loss because in some cases they are able to collect payment regardless of whether they are successful in their services or not. While it is legally possible for constables to provide services for the public, according to your interviews, it is rare.

The facts regarding the relationship of the parties are also mixed. The County has been treating the constables as independent contractors and reporting payments made to them on Forms 1099. In addition, they do not provide any employee benefits to the constables. However, the constables have an ongoing relationship with the County as some of them have served for more than 20 years. In addition, the constables are completely integrated into the County business; the magisterial district court cannot function without them and the County relies on them to serve notices and execute warrants because they do not have enough police officers or sheriffs to do so. The constables can be terminated by a judge for failure to perform their duties pursuant to the statute.

As in most worker classification cases, the facts are not all indicative of an employee or an independent contractor. However, on balance, it appears that the constables are employees. The State's ability to control how the constables perform their services through state statute, required training and the * * * constable handbook is an especially strong factor that indicates they are employees subject to the control of an employer.

The County maintains that the constables are not its employees. It relies, in part, on State case law which holds that the constables are independent contractors and not employees. For example, the Supreme Court of Pennsylvania held that legislation designed to bring constables within the control

and direction of the judiciary was in violation of the State's constitution because it attempted to place constables, whose central functions and activities consist of exercising executive powers, within the supervisory authority of the judicial branch, thereby violating the doctrine of separation of powers. In re Act 147 of 1990, 528 A.2d 985, 990. (Pa. 1991). The court cited an earlier case that held a constable is not an employee of the Commonwealth, the judiciary, the township, or the county in which he works. *Id.* at 986, citing *Rosenwald v. Barbieri*, 462 A.2d 644 (Pa. 1983). State case law is not binding for federal income tax purposes. In addition, the court in these cases did not apply the common law employee analysis used to determine coverage under FICA. Finally, there do not appear to be any cases classifying the constables as independent contractors since the enactment of Chapter 71 to the Pennsylvania Code in 2009, discussed above. These amendments and consolidation appear to make significant changes to the law regarding constables and may change the analysis under state law. Thus, the County's reliance on state case law is unfounded.

4. Employees for the Purposes of Income Tax Withholding

I.R.C. § 3402 obligates any employer making a payment of wages to deduct and withhold tax as prescribed by the Secretary. I.R.C. § 3401(a) defines wages as all remuneration (other than fees paid to a public official) for services performed by an employee for his employer. I.R.C. § 3401(c) provides that for the purposes of income tax withholding ("ITW") requirements, an employee includes "an officer, employee, or elected official of the United States, a State or any political subdivision thereof . . ." Because the constables are elected officials of the County, they are employees for the purpose of ITW.

5. Who is the Employer?

Section 3401(d)(1) provides, that for purposes of income tax withholding, the term employer means the person for whom an individual performs or performed any service, of whatever nature, as the employee of such person, except that if the person for whom the individual performs or performed the services does not have control of the payment of the wages for such services, the term "employer" (except for purposes of the definition of wages) means the person having control of the payment of such wages. Neither FICA nor FUTA contains a definition of employer similar to the definition contained in section 3401(d)(1), relating to income tax withholding. However, *Otte v. U.S.*, 419 U.S. 43 (1974), holds that a person who is an employer under section 3401(d)(1), relating to income tax withholding, is also an employer for purposes of FICA withholding under section 3102. *Otte* involved a trustee in bankruptcy who was an employer under section 3401(d)(1) by virtue of having control over the payment of wages owed by the bankrupt. The Court stated, "The fact that the FICA withholding provisions of the Code do not define 'employer' is of no significance, for that term is not to be given a narrower construction for FICA withholding than for income tax withholding." *Otte*, 419 U.S. at 51. The *Otte* decision has been extended to provide that the person having control of the payment of wages is also an employer for purposes of section 3111, which imposes the FICA tax on employers, and for purposes of section 3301, which imposes the FUTA tax on employers.³ In re *Armadillo Corp.*, 410 F. Supp. 407 (D. Col. 1976), *aff'd*, 561 F.2d 1382 (10th Cir. 1977), In re *Laub Baking Co.*, 642 F.2d 196 (6th Cir. 1981), and *STA of Baltimore — ILA Container Royalty Fund v. U.S.*, 621 F. Supp. 1567 (D.C. Md. 1985), *aff'd*, 804 F.2d 296 (4th Cir. 1986) reached similar conclusions.

The constables primarily perform services for the courts, which are part of the State judiciary system. They also perform various services the County by serving on election day, executing warrants, and impounding livestock. They also perform services for private litigants, including carrying out ejectments in landlord-tenant disputes. However, the constables' payment for all of these services is controlled by the County, as the funds come from County checking accounts and the County Manager of Constable Services verifies all submissions for payments. Even if the County

is not the common law employer, the County is the employer for purposes of ITW and FICA because it controls the payments.

CONCLUSION

Based on the facts you have gathered, we agree that the constables are employees under the common law standard. Further, SSA has determined that the constables are covered under the State's 218 agreement. Finally, we believe the County is liable for employment taxes for the constables.

Please call * * * if you have any further questions.

Joseph W. Spires

Area Counsel

(Tax Exempt & Government Entities)

IRS Reminder: Calendar Year Form 990 Series Returns Due by May 15.

May 15 is the filing deadline for exempt organizations whose tax year ends on December 31, unless the organization submitted Form 8868, Application for Extension of Time To File an Exempt Organization Return. Remember an organization that fails to file for three consecutive years automatically loses its federal tax-exempt status.

Foundation's Grantmaking Expenditures Not Taxable.

The IRS ruled that expenditures made through a private foundation's grantmaking program through which American art will be brought to international audiences will not be taxable.

Dear * * *

You asked for advance approval of your educational grant procedures under Internal Revenue Code section 4945(g)(3). This approval is required because you are a private foundation that is exempt from federal income tax.

OUR DETERMINATION

We approved your procedures for awarding educational grants. Based on the information you submitted, and assuming you will conduct your program as proposed, we determined that your procedures for awarding educational grants meet the requirements of Code section 4945(g)(3). As a result, expenditures you make under these procedures won't be taxable.

DESCRIPTION OF YOUR REQUEST

You are dedicated to fostering exploration, understanding, and enjoyment of the visual arts of the United States for national and international audiences. You are committed to supporting projects designed to engage audiences around the globe in an enriched dialogue on American art. Through

grants and initiatives, you have made it a priority to bring American art, interpretation, and research resources to international audiences, and have a particular interest in fostering multi-national perspectives.

In furtherance of this international perspective, you will initiate a grant making program called B. The B will further your mission of internationalizing the field of American art by supporting scholars worldwide who share your goals of excellence and originality. In addition to encouraging international scholarship, B will enrich the field through the introduction of new approaches to American art research and will enable scholars outside the United States greater access to American art scholarship. It also will allow them to publish on this topic in their home countries.

Awards under B generally will be made to qualified publishers of selected works. Such grants will be treated as grants to organizations. In limited circumstances described below, however, certain grants will be made directly to individual authors and volume editors and/or contributors. The grants to individuals is the reason you are requesting advance approval under section 4945(g)(3).

B will support scholarly publications that (1) offer translations of key texts on American art, (2) encourage international scholarship on American art, or (3) present focused theses exploring American art in an international context. B is designed to determine the nature of the proposed publication, the professional qualifications of the publisher, the professional qualifications of the author, the commitment and capacity of the author and his or her publisher, and the expected outcomes of publication.

You initially intend to operate B with a three-year budget of x dollars. Grants to support the publication of a book generally will not exceed y dollars, and grants to support the publication of an article generally will not exceed z dollars, although you may vary the size of the grants based on the quality of the applications received and the amount requested. Funds awarded under B will be used for direct costs of publishing the particular work, including translation costs and image rights of black-and-white or full-color illustrations.

You will promote the grants through an extensive list of academic and museum contacts. Grant announcements will be posted on your website and distributed to various relevant associations worldwide. Additionally, information about the grants will be disseminated to individuals through your general e-newsletter, as well as international curators, publishers, and scholars through targeted e-blasts. Posters and postcards are also distributed to major universities and museums to increase the visibility of your grant program.

Each application must be for a scholarly book or article in print or digital format that focuses on historical American art (circa 1500 to 1980), that has an international dimension, and that is under contract for publication. You will strongly encourage applications for:

Translations of books and articles originally written or published in English.

English-language translations of books and articles originally written or published in another language.

Books and articles for publication outside the United States.

Internationally collaborative projects.

Books and articles examining American art in an international context.

Neither new exhibition catalogues nor collection catalogues are eligible for grants under your

program; however, translations or reprints of exhibition catalogues that were originally published prior to 2005 may be considered if they contain substantial scholarship.

In reviewing applications, your review committees will consider objective criteria regarding each application. The criteria you will consider include:

The publication's significant contribution to the field of American art as well as its place in the current literature on the topic.

The publisher's history, mission, and art list.

The distribution and marketing plan for the publication.

The author's curriculum vitae.

A partial (in the case of a book) or full (in the case of an article) manuscript, including sample book chapters in both languages if the project involves translation or a detailed English abstract if the article is in a language other than English.

Two or more recent peer reviews of the full manuscript.

The publisher's endorsement of the manuscript.

Your organization will review applications using internal and external review committees. The external review committee will be comprised of three or more international scholars in the field of American art, each with extensive subject matter knowledge and experience. All external review committee members will be asked to provide a list of potential personal and/or financial conflicts, and will be asked to recuse themselves should any conflicts arise. External review committee members shall remain anonymous to the public and to applicants during their term on the committee. No external review committee member may benefit personally or professionally from the selection of any particular application for the grant.

The internal review committee will consist of your staff including scholars of American art. Your staff will process and review applications received, with a focus on accomplishing your goal of international exposure for American art. Your internal review committee will collect the recommendations of the external review committee and combine these results with your internal review committee. The internal review committee will make the final decision regarding the recipients. No internal review committee member may benefit personally or professionally from the selection of any particular application for a grant.

B awards generally will be paid to the qualified publisher to be used only for the approved publication; however, grants will be made directly to authors in certain circumstances.

Each grant will be made pursuant to a written grant agreement with the publisher or author. The grant agreement will limit the use of the funds to those enumerated in the approved application. Grant recipients will be required to submit periodic reports to you, and a schedule of deadlines for these reports will be outlined in the grant agreement. If required reports are delinquent or there are other indications of a possible diversion of funds, follow-up requests will be submitted. If satisfactory reports are not received after a reasonable time, you will attempt to recover the funds. While conducting an investigation, you will withhold future payments (if any) until the delinquent reports have been submitted. If a diversion is determined to have occurred, no future payments will be made to the recipient and appropriate steps will be taken to recover the grant funds. You will maintain appropriate records regarding the amount of the grant, grant recipient, information sufficient to

insure that the recipient was not a “disqualified person” under Code Section 4946 with respect to you for the purposes of the self-dealing rules set forth in Code Section 4941, the purpose of the grant, the grant agreement and final report, and all follow-up information regarding progress reports, any suspension of grants, and any investigations of possible diversion of grant funds.

BASIS FOR OUR DETERMINATION

The law imposes certain excise taxes on the taxable expenditures of private foundations (Code section 4945). A taxable expenditure is any amount a private foundation pays as a grant to an individual for travel, study, or other similar purposes. However, a grant that meets all of the following requirements of Code section 4945(g) is not a taxable expenditure.

The foundation awards the grant on an objective and nondiscriminatory basis.

The IRS approves in advance the procedure for awarding the grant.

The grant is:

A scholarship or fellowship subject to section 117(a) and is to be used for study at an educational organization described in section 170(b)(1)(A)(ii); or

A prize or award subject to the provisions of section 74(b), if the recipient of the prize or award is selected from the general public; or

To achieve a specific objective; produce a report or similar product; or improve or enhance a literary, artistic, musical, scientific, teaching, or other similar skill or talent of the recipient.

To receive approval of its educational grant procedures, Treasury Regulations section 53.4945-4(c)(1) requires that a private foundation show:

The grant procedure includes an objective and nondiscriminatory selection process.

The grant procedure results in the recipients performing the activities the grants were intended to finance.

The foundation plans to obtain reports to determine whether the recipients have performed the activities that the grants were intended to finance.

OTHER CONDITIONS THAT APPLY TO THIS DETERMINATION

This determination covers only the grant program described above. This approval will apply to succeeding grant programs only if their standards and procedures don’t differ significantly from those described in your original request.

This determination applies only to you. It may not be cited as precedent.

You cannot rely on the conclusions in this letter if the facts you provided have changed substantially. You must report any significant changes in your program to the Cincinnati Office of Exempt Organizations at:

* * *

You cannot make grants to your creators, officers, directors, trustees, foundation managers, or members of selection committees or their relatives.

All funds distributed to individuals must be made on a charitable basis and must further the purposes of your organization. You cannot award grants for a purpose that is inconsistent with Code section 170(c)(2)(B).

You should keep adequate records and case histories so that you can substantiate your grant distributions with the IRS if necessary.

We've sent a copy of this letter to your representative as indicated in your power of attorney.

Please keep a copy of this letter in your records.

If you have any questions, please contact the person listed at the top of this letter.

Sincerely,

Holly O. Paz

Director, Exempt Organizations

Rulings and Agreements

Citations: LTR 201318008

IRS: Religious Organization's Benefits Plans Are Church Plans.

The IRS ruled that a tax-exempt religious organization's defined benefit pension plans are church plans within the meaning of section 414(e), retroactive to specified dates.

Date: February 6, 2013

Dear * * *

This letter is in response to your request dated May 13, 2005, as supplemented by correspondence dated March 5, 2012, submitted on your behalf by your authorized representative regarding the church plan status of Plan X, Plan Y and Plan Z within the meaning of section 414(e) of the Internal Revenue Code (Code).

The following facts and representations have been submitted under penalties of perjury on your behalf:

Taxpayer A was established in 19* * * by Order B, a Church C religious order based in Country G, which operates hospitals and health care facilities in three locations in the United States. Taxpayer A is a not-for-profit corporation organized under the laws of State E. Taxpayer A is listed in Directory S, and accordingly, is exempt from Federal income tax under section 501(c) of the Code. Order B is listed in Directory S as being represented in Entity I by virtue of its presence at Taxpayer A. The current president and chief executive officer of Taxpayer A is a member of Order B.

Taxpayer A's by-laws contain the stated purpose to establish and operate a Church C hospital for the purposes of providing hospitalization and care of the sick and injured, necessary facilities for the treatment of disease, and for scientific purposes; and to establish and operate schools and educational institutions in the hospital, nursing and related fields. Any applicant for appointment to

Taxpayer A's medical staff must, as part of the application, agree to be bound by the Ethical and Religious Directives of Church C Healthcare Services as promulgated by Entity J.

Under Article III of Taxpayer's by-laws, the sole member of Taxpayer A's corporation is Network D. Also under the by-laws, Network D has the right to ensure that Taxpayer A is conducting its business and affairs consistently with and in furtherance of the objectives and philosophy of Order B.

Network D is a corporation organized under the Statute N. Among its corporate purposes is to conduct the business affairs of the corporation in a manner consistent with the objectives and philosophy of Order B. Prior to September ***, 20***, members of Network D were from the Provincial Council of Order B, and those members of Entity F Executive were appointed by the Provincial Council. The Provincial Council of Order B is comprised of the local Provincial Superior of Order B and the local Provincial Superior of Order B's councilors. The Entity F Executive is comprised of Order B members who have been appointed by the Provincial Council to serve on the Entity F Executive.

Effective September ***, 20***, Network D's by-laws were amended to provide that Network D's members shall be comprised of seven members appointed by the General Council of Order B, at least four of whom must at all times be members of Order B. As a result, you represent that Taxpayer A is under the control of Network D, a majority of whose members must be members of Order B. If at any time Network D ceases to exist, Taxpayer A's by-laws provide that the Provincial Council may elect a new corporate member.

Prior to the adoption of Taxpayer A's current by-laws on October ***, 20***, Taxpayer A's members were members of Order B's Provincial Council and members of the Entity F Executive. Since its founding in 19***, Taxpayer A has been controlled either directly, or through Network D, by Order B.

Taxpayer A's board of trustees is responsible for the oversight of Taxpayer A, the appointment of its officers and medical staff, the assessment of its programs, the preparation and recommendation to Network D of Taxpayer A's capital and operating budget, and certain additional oversight responsibilities set forth in Taxpayer A's by-laws. The board of trustees is comprised of not less than 12, nor more than 18 members, including three members of Order B or their representatives, appointed by Entity F, at least five members appointed by Network D, two members of Taxpayer A's medical staff, and any additional trustees (up to 18) appointed by Network D.

Entity F is a corporation which is incorporated under the laws of Country G. Under its by-laws, its membership is limited to members of Order B. The members of Entity F consist of the members of the Provincial Council of Order B and selected members of the Entity F Executive. Any member of the board of trustees of Taxpayer A may be removed by Network D with or without cause. As a result, through its power to appoint Taxpayer A's trustees, either through Entity F or through Network D, and its power through Network D to remove the trustees with or without cause, you represent that Order B controls the board of trustees..

In 19***, Taxpayer A adopted Plan X for the benefit of the employees of Taxpayer A. Plan X is a defined benefit pension plan. Plan X is a new plan, not a successor plan, and meets the requirements of section 401(a) of the Code. Effective September ***, 19***, Plan X's benefit formula was incorporated into the plan document for Plan Y. Accruals under Plan X were frozen by an amendment to Plan X effective November ***, 19***, which is incorporated into the current plan by an individually designed amendment.

Plan Y is a defined contribution money purchase pension plan adopted by Taxpayer A on September

, 19, solely for the benefit of its employees. Plan Y is intended to be qualified under section 401(a) of the Code.

The combined plan document for Plan X and Plan Y was amended and restated periodically, and the most recent favorable determination letter for the combined plan document is dated April ***, 20***. Participation in Plan X and Plan Y has been limited to employees of Taxpayer A at all times.

Plan Z was originally adopted by Taxpayer A effective January ***, 19***, solely for the benefit of its employees. Plan Z is intended by Taxpayer A to be a tax deferred annuity arrangement under section 403(b) of the Code. Participation in Plan Z has been limited to employees of Taxpayer A at all times.

None of the eligible participants in Plan X, Plan Y or Plan Z are, were, or can be considered to be employed in connection with one or more unrelated trades or businesses within the meaning of section 513 of the Code. The plans do not include as participants employees of for-profit entities.

By resolutions dated December ***, 20***, Taxpayer A established Committee H. Committee H's sole purpose and function is to administer Plan X, Plan Y and Plan Z. Under the resolutions, the initial members of Committee H were the president and chief executive officer of Taxpayer A, and the executive vice president of Taxpayer A. If Taxpayer A's president is a member of Order B, the president is an ex officio member of Committee H and has the authority to appoint and discharge up to six Committee H members at any time. Under Taxpayer A's by-laws, the President of Taxpayer A is appointed (and can be removed) by Network D.

You represent that the establishing resolutions for Committee H provide that if the president is not or ceases to be a member of Order B, Network D shall assume the authority to appoint and discharge up to seven Committee H members, so that Committee H continues to constitute an organization that is controlled by or associated with Order B. As established by Taxpayer A, Committee H has all such powers as may be necessary or helpful to discharge its duties as administrator of the plans.

By resolutions dated December ***, 20***, Taxpayer A amended Plan X, Plan Y and Plan Z to name Committee H as the administrator under each of the Plans.

Taxpayer A has not made the election under section 410(d) of the Code with respect to Plan X, Plan Y, or Plan Z. However, it has in the past voluntarily operated Plan Y in compliance with the standards of the Employee Retirement Security Act of 1974 (ERISA) to include filing Form 5500, and paying premiums to the Pension Benefit Guaranty Corporation.

In accordance with Revenue Procedure 2011-44, Notice to Employees with reference to Plan X was provided on March ***, 20***. This notice explained to participants of Plan X, Plan Y and Plan Z the consequences of church plan status.

Based on the foregoing, you request a ruling that Plan X and Plan Y are church plans within the meaning of section 414(e) of the Code effective as of January 1, 1974; and that Plan Z is a church plan within the meaning of section 414(e) of the Code effective as of January 1, 1987.

Section 414(e) was added to the Code by section 1015 of ERISA. Section 1017(e) of ERISA provided that section 414(e) of the Code applied as of the date of ERISA's enactment. However, section 414(e) of the Code was subsequently amended by section 407(b) of the Multiemployer Pension Plan Amendments Act of 1980, Pub. Law 96-364, to provide that section 414(e) of the Code was effective as of January 1, 1974.

Section 414(e)(1) of the Code generally defines a church plan as a plan established and maintained for its employees (or their beneficiaries) by a church or a convention or association of churches which is exempt from taxation under section 501 of the Code.

Section 414(e)(2) of the Code provides, in part, that the term “church plan” does not include a plan that is established and maintained primarily for the benefit of employees (or their beneficiaries) of such church or convention or association of churches who are employed in connection with one or more unrelated trades or businesses (within the meaning of section 513 of the Code); or if less than substantially all of the individuals included in the plan are individuals described in section 414(e)(1) of the Code or section 414(e)(3)(B) of the Code (or their beneficiaries).

Section 414(e)(3)(A) of the Code provides that a plan established and maintained for its employees (or their beneficiaries) by a church or by a convention or association of churches includes a plan maintained by an organization, whether a civil law corporation or otherwise, the principal purpose or function of which is the administration or funding of a plan or program for the provision of retirement benefits or welfare benefits, or both, for the employees of a church or a convention or association of churches, if such organization is controlled by or associated with a church or a convention or association of churches.

Section 414(e)(3)(B) of the Code defines “employee” of a church or a convention or association of churches to include a duly ordained, commissioned, or licensed minister of a church in the exercise of his or her ministry, regardless of the source of his or her compensation, and an employee of an organization, whether a civil law corporation or otherwise, which is exempt from tax under section 501 of the Code, and which is controlled by or associated with a church or a convention or association of churches.

Section 414(e)(3)(C) of the Code provides that a church or a convention or association of churches which is exempt from tax under section 501 of the Code shall be deemed the employer of any individual included as an employee under subparagraph (B).

Section 414(e)(3)(D) of the Code provides that an organization, whether a civil law corporation or otherwise, is associated with a church or a convention or association of churches if the organization shares common religious bonds and convictions with that church or convention or association of churches.

Section 414(e)(4)(A) of the Code provides that if a plan, intended to be a church plan, fails to meet one or more of the church plan requirements and corrects its failure within the correction period, then that plan shall be deemed to meet the requirements of this subsection for the year in which the correction was made and for all prior years. Section 414(e)(4)(C)(i) of the Code provides, in pertinent part, that the term “correction period” means the period ending 270 days after the date of mailing by the Secretary of a notice of default with respect to the plan’s failure to meet one or more of the church plan requirements.

Revenue Procedure 2011-44, 2011-39 I.R.B. 446, supplements the procedures for requesting a letter ruling under section 414(e) of the Code relating to church plans. The revenue procedure: (1) requires that plan participants and other interested persons receive a notice in connection with a letter ruling request under section 414(e) of the Code for a qualified plan; (2) requires that a copy of the notice be submitted to the Internal Revenue Service (IRS) as part of the ruling request; and (3) provides procedures for the IRS to receive and consider comments relating to the ruling request from interested persons.

In order for an organization that is not itself a church or convention or association of churches to

have a qualified church plan, it must establish that its employees are employees or deemed employees of a church or convention or association of churches under section 414(e)(3)(B) of the Code by virtue of the organization's control by or affiliation with a church or convention or association of churches. Employees of any organization maintaining a plan are considered to be church employees if the organization: 1) is exempt from tax under section 501 of the Code; and, 2) is controlled by or associated with a church or convention or association of churches. In addition, in order to be a church plan, the plan must be administered or funded (or both) by an organization described in section 414(e)(3)(A) of the Code. To be described in section 414(e)(3)(A) of the Code, an organization must have as its principal purpose the administration or funding of the plan and must also be controlled by or associated with a church or convention or association of churches.

In this case, Taxpayer A is a not-for-profit corporation which is exempt from federal income tax under section 501(a) of the Code as an organization described in section 501(c)(3) of the Code. In view of the common religious bonds between Church C and Taxpayer A, the inclusion of Order B in Directory S, and the indirect control of Taxpayer A by Church C through Order B, we conclude that Taxpayer A is associated with a church or a convention or association of churches within the meaning of section 414(e)(3)(D) of the Code, that the employees of Taxpayer A meet the definition of employee under section 414(e)(3)(B) of the Code and that they are deemed to be employees of a church or a convention or association of churches by virtue of being employees of an organization which is exempt from tax under section 501 of the Code and which is controlled by or associated with a church or a convention or association of churches.

Effective December ***, 20**, with Taxpayer A's establishment of Committee H and Committee H becoming administrator of Plan X, Plan Y and Plan Z, the plans are each maintained by an organization whose sole purpose and function is the administration of the plans. Under the establishing resolutions for Committee H, if Taxpayer A's president is a member of Order B, the president is an ex officio member of Committee H, and has the authority to appoint and discharge up to seven additional Committee H members. The establishing resolutions for Committee H provide that if the president is not or ceases to be a member of Order B, Network D has the authority to appoint and discharge Committee H members. Accordingly, Committee H is an organization that is controlled by or associated with Order B which is a Church C religious order. As a result, the plans are administered by an organization that is controlled by or associated with a church or an association of churches within the meaning of section 414(e)(3)(A) of the Code.

Also, as provided under section 414(e)(4)(A) of the Code, where a plan fails to meet one or more of the church plan requirements and corrects its failure within the correction period, then that plan shall be deemed to meet the requirements of section 414(e) for the year in which the correction is made and for all prior years. Committee H was established to administer Plan X, Plan Y and Plan Z on December 1**, 20**, which is within the correction period for Plan X, Plan Y and Plan Z.

Based on the foregoing facts and representations, we conclude that Plan X and Plan Y are church plans within the meaning of section 414(e) of the Code, and have been church plans within the meaning of section 414(e) of the Code retroactive to January **, 19**. We conclude that Plan Z is a church plan within the meaning of section 414(e) of the Code, and has been a church plan within the meaning of section 414(e) of the Code retroactive to January **, 19**.

This letter expresses no opinion as to whether Plan X and Plan Y satisfy the requirements for qualification under section 401(a) or whether Plan Z satisfies the requirements of section 403(b) of the Code.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

A copy of this letter is being sent to your authorized representative pursuant to a Power of Attorney on file in this office.

If you have any questions regarding this letter, please contact * * * at * * *. Please refer all correspondence to SE:T:EP:RA:T3.

Sincerely yours,

Laura B. Warshawsky, Manager

Employee Plans Technical Group 3

Citations: LTR 201318030

IRS Rules on Donation of Depreciated Property.

The IRS ruled that if a taxpayer donates fully depreciated property to one or more charities, the resulting charitable deduction will not be reduced by 20 percent of the accumulated depreciation of the property.

Re: Request for Private Letter Ruling under

Sections 170, 291, and 1250

Dear * * *:

This letter responds to a letter dated July 27, 2012, and supplemental correspondence, submitted by Taxpayer requesting a letter ruling that, if certain section 1250 property is contributed to one or more tax-exempt organizations, the charitable deduction attributable to the value of that contribution will not be reduced by twenty percent of the accumulated depreciation of this section 1250 property under section 291(a)(1) of the Internal Revenue Code.

FACTS

Taxpayer represents that the facts are as follows:

Taxpayer is a State1 corporation with a principal place of business in City1, State1. Taxpayer is a wholly-owned subsidiary of A and joins in the consolidated Federal income tax return filed for the affiliated group headed by A. A files its consolidated Federal income tax return on a calendar year basis.

Taxpayer owns certain improved real property located at Taxpayer's B plant in City1, State1 (the "B property"). The B property contains certain depreciable real property that is section 1250 property. Most of this section 1250 property has been fully depreciated. Hereinafter, the fully depreciated B property that is section 1250 property will be referred to as "the Property."

Taxpayer intends to contribute some or all of the Property to one or more organizations that are exempt from Federal income tax under section 501(c)(3) as a charitable contribution under section 170. Moreover, Taxpayer intends to claim a charitable deduction under section 170 with respect to its contribution of the Property to one or more section 501(c)(3) tax-exempt organizations.

Taxpayer represents that these section 501(c)(3) tax-exempt organizations will have the same basis in the Property as Taxpayer will have at the time of the transfer pursuant to section 1015(a).

RULING REQUESTED

Taxpayer requests the following ruling:

If the Property is contributed to one or more section 501(c)(3) tax-exempt organizations, the charitable deduction attributable to the value of the contribution will not be reduced by twenty percent of the accumulated depreciation of the Property pursuant to section 291(a)(1).

LAW AND ANALYSIS

Section 170 generally allows a deduction, subject to certain limitations, for charitable contributions made during the taxable year to or for the use of organizations described in section 170(c), including section 501(c)(3) organizations.

Section 170A-1(c)(1) of the Income Tax Regulations provides that 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) and section 1.170A-4(a), or section 170(e)(3) and section 1.170A-4A(c).

Section 170(e)(1) provides that the amount of any charitable contribution of property otherwise taken into account under section 170 shall be reduced by, among other amounts, the amount of gain that would not have been long-term capital gain (determined without regard to section 1221(b)(3)) if the property contributed had been sold by the taxpayer at its fair market value (determined at the time of such contribution).

Section 1.170A-4(a)(1) provides that in the case of a contribution by an individual or by a corporation of ordinary income property, as defined in section 1.170A-4(b)(1), the amount of the charitable contribution that would be taken into account under section 170(a) without regard to section 170(e) shall be reduced before applying the percentage limitations under section 170(b) by the amount of gain that would have been recognized as gain that is not long-term capital gain if the property 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(b)(1) defines the term "ordinary income property" as meaning property any portion of the gain on which would not have been long-term capital gain if the property had been sold by the donor at its fair market value at the time of its contribution to the charitable organization.

Section 291(a)(1) provides that in a case where a corporation disposes of section 1250 property, an amount equal to twenty percent of the excess, if any, of (A) the amount that would be treated as ordinary income if such property was section 1245 property, over (B) the amount treated as ordinary income under section 1250 (determined without regard to section 291(a)(1)), shall be treated as gain which is ordinary income under section 1250 and shall be recognized notwithstanding any other provision of Subtitle A of the Code. Section 291(a)(1) further provides that under regulations prescribed by the Secretary, the provisions of section 291(a)(1) will not apply to the disposition of any property to the extent that section 1250(a) does not apply to such disposition by reason of section 1250(d).

If section 1245 property is disposed of, section 1245(a)(1) generally provides that the amount by which the lower of (A) the recomputed basis of the property, or (B) the amount realized (in the case of a sale, exchange, or involuntary conversion) or the fair market value of such property (in the case

of any other disposition), exceeds the adjusted basis of such property is treated as ordinary income. Such gain is recognized notwithstanding any other provision of Subtitle A of the Code.

Section 1245(a)(2) defines the term “recomputed basis” with respect to any property as meaning, generally, its adjusted basis recomputed by adding thereto all adjustments reflected in such adjusted basis on account of deductions (whether in respect of the same or other property) allowed or allowable to the taxpayer or to any other person for depreciation or amortization.

If section 1250 property is disposed of after December 31, 1975, section 1250(a)(1)(A) generally provides that 100 percent of the lower of (i) that portion of the additional depreciation attributable to periods after December 31, 1975, in respect of such property, or (ii) the excess of the amount realized (in the case of a sale, exchange, or involuntary conversion), or the fair market value of such property (in the case of any other disposition), over the adjusted basis of such property, is treated as gain that is ordinary income. Such gain is recognized notwithstanding any other provision of Subtitle A of the Code.

Section 1250(b)(1) defines the term “additional depreciation” as meaning, in the case of any property, the depreciation adjustments in respect of such property; except that, in the case of property held more than one year, it means such adjustments only to the extent that they exceed the amount of the depreciation adjustments that would have resulted if such adjustments had been determined for each taxable year under the straight-line method of depreciation.

Section 1250(d)(1) provides that section 1250(a) shall not apply to a disposition by gift.

Section 1.1250-3(a)(1) provides that, for purposes of section 1250(d)(1), the term “gift” shall have the same meaning as in section 1.1245-4(a).

Section 1.1245-4(a) provides that the term “gift” means, generally, a transfer of property which, in the hands of the transferee, has a basis determined under the provisions of section 1015(a) or (d) (relating to basis of property acquired by gifts).

If section 1250 property is disposed of by gift (as defined in sections 1.1250-3(a)(1) and 1.1245-4(a)), section 1250(d)(1) provides that section 1250(a) does not apply to such disposition. Consequently, section 291(a)(1) would not apply to a gift (as defined in sections 1.1250-3(a)(1) and 1.1245-4(a)) of section 1250 property.

In this case, Taxpayer represents that it intends to contribute the Property to one or more organizations that are section 501(c)(3) tax-exempt organizations, that this intended contribution will be a valid charitable contribution that meets the requirements of section 170, and that these section 501(c)(3) tax-exempt organizations will have a basis in the Property equal to Taxpayer’s basis in the Property at the time of transfer pursuant to section 1015(a). These are material representations. Because the basis of the Property in the hands of the section 501(c)(3) tax-exempt organizations will be the same as Taxpayer’s basis in the Property at the time of the transfer pursuant to section 1015(a), the contribution of the Property by Taxpayer to the section 501(c)(3) organizations is a gift for purposes of sections 1250(d)(1) and 1.1250-3(a)(1). Accordingly, the provisions of section 291(a)(1) will not apply to Taxpayer’s disposition of the Property to the section 501(c)(3) tax-exempt organizations.

CONCLUSION

Based solely on Taxpayer’s representations and the relevant law and analysis set forth above, we conclude that if the Property is contributed to one or more section 501(c)(3) tax-exempt

organizations, the charitable deduction attributable to the value of the contribution will not be reduced by twenty percent of the accumulated depreciation of the Property pursuant to section 291(a)(1).

Except as specifically set forth above, no opinion is expressed or implied concerning the tax consequences of the facts described above under any other provisions of the Code. Specifically, this letter ruling is based upon Taxpayer's description of the proposed contribution of property to certain section 501(c)(3) organizations. This letter ruling does not address whether the proposed contribution is a valid charitable contribution that meets the requirements of section 170. Further, the amount of the deduction for the proposed contribution is outside the scope of this letter ruling, and no approval of the amount should be inferred from this letter ruling. Moreover, no opinion is expressed or implied on (i) whether any of the property located at B is section 1250 property, and (ii) the propriety of Taxpayer's methods of depreciating the property located at B.

This letter ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

In accordance with the power of attorney, we are sending a copy of this letter to Taxpayer's authorized representatives. We are also sending a copy of this letter to the appropriate operating division director.

Sincerely,

Kathleen Reed

Chief, Branch 7

Office of Associate Chief Counsel

(Income Tax and Accounting)

Citations: LTR 201318003

IRS: Colleges and Universities Compliance Project Final Report - Revised.

The IRS has released a revised version of its Colleges and Universities Compliance Project Final Report.

The revised report can be found at:

http://www.irs.gov/pub/irs-tege/CUCP_FinalRpt_042513.pdf

IRS Declines to Limit Retroactive Effect of Organization's Revocation.

In technical advice, the IRS declined to limit the retroactive effect of its revocation of a credit counseling organization's tax-exempt status.

The IRS initially denied the organization's exemption application partly because of the organization's

close connection to a for-profit company owned by the president of the organization. After the organization said it would educate the public on money management and provide credit counseling, the IRS granted exemption. But a subsequent IRS examination showed the organization, six years after obtaining exemption, had contracted with the same for-profit entity and was operating as a trade or business. The IRS also discovered that the organization was primarily engaged in enrolling people in debt management plans instead of providing counseling. Further, the organization had not told the IRS about its change in operations.

The IRS concluded that the revocation may be retroactive to the year under examination, when the IRS determined the organization had made material changes in its operations.

IRS: Foundation's Expenditures for Mentorship Program Aren't Taxable.

The IRS ruled that expenditures made through a private foundation's mentorship program for disadvantaged youth will not be taxable.

Dear * * *:

You asked for advance approval of your educational grant procedures under Internal Revenue Code section 4945(g)(3). This approval is required because you are a private foundation that is exempt from federal income tax.

OUR DETERMINATION

We approved your procedures for awarding educational grants. Based on the information you submitted, and assuming you will conduct your program as proposed, we determined that your procedures for awarding educational grants meet the requirements of Code section 4945(g)(3). As a result, expenditures you make under these procedures won't be taxable.

DESCRIPTION OF YOUR REQUEST

Your letter indicates that you will operate a mentorship program.

The program will provide greater opportunities for disadvantaged youth around the world to realize their full potential and attain mentorships by introducing young adults to leading entrepreneurs, artists, and academics, by sponsoring visa applications, and by covering expenses related to the pursuit of their goals whether in the fields of science, arts, sports, academia, or otherwise.

You intend to both publicize your program on your website, and through foreign and international websites that have the potential of drawing a wide audience from around the world.

You will have application forms completed by both a nominating organization and the potential protégé. In the future you intend to allow applicants to self-nominate.

You aim to support young adults, ages 18 to 30, who have faced, or are facing, significant adversity in life. You do not define what specifically constitutes adversity. It is up to the applicants to demonstrate how their ability to develop in their chosen fields has been stifled by individual circumstances. You will consider individuals who have not had the economic means to pursue their goals, as well as individuals living under oppressive regimes, or in repressive communities. These are just a few examples of the kind of adversity that might qualify a candidate for the mentorship

program.

Specific criteria for selection will be based on the following factors:

Age: Applicants should be between the ages of 18 and 30.

Talent: Applicants must demonstrate talent, potential, and perseverance in their chosen fields.

Need: Applicants must demonstrate that they have faced significant adversity, as defined by each applicant's individual circumstances.

Professional Development Potential: Applicants should demonstrate that the foundation can significantly impact his or her ability to realize his or her full potential.

Leadership Potential: Applicants must demonstrate a genuine desire to give back to their communities in a meaningful and realistic way. Specifically, in accordance with W, protégés must work to bring about positive change in one of the following categories: alleviation of poverty and hunger, improvement of education for all, elimination of discrimination, environmental sustainability, improvement of global health, improvement of global economy, or attainment of world peace.

Substantial contributors, foundation managers, officers, directors, and employees of the foundation, as well as their family members, are ineligible to participate in the mentorship program.

You currently plan to run between two and six mentorships each year. You hope to scale up to ten to twelve mentorships in the future depending on the availability of funding, the particular needs of each recipient, and the overall success of your programs.

You envision providing support to protégés of up to \$z per recipient over the course of a year or, some cases, more than a year. The support will be used to cover the expenses of travel, conference participation, art exhibits, supplies, courses, and other expenses related to each protégés particular field of interest, as well as in some cases a cash stipend.

You have adopted the following mandatory procedure in order to ensure continuing compliance with the post-9/11 Executive Orders and with Office of Foreign Assets Control, OFAC, requirements:

You will operate in compliance with all statutes, Executive Orders, and regulations restricting or prohibiting U.S. persons from engaging in transactions and dealings with countries, entities, or individuals subject to economic sanctions administered by OFAC.

You will check the OFAC List of Specially Designated Nationals, SDN, and Blocked Persons before dealing with persons including individuals, organizations and entities and specifically avoid dealing with any persons on the list.

You will not enter into a relationship with a grantee where doubts exist about the grantees' ability to ensure safe delivery of charitable resources independent of influence by or association with any terrorist organization.

You will not engage in trade or transaction activities that violate the regulation behind OFAC's country-based sanctions programs or engage in trade or transaction activities with sanctions targets named on OFAC's SDN list.

You will acquire from OFAC the appropriate license and registration where necessary.

The selection committee varies per protégé. The President and Executive Director, together field applications to select the most promising candidates. The candidates will then be presented to an individualized selection committee made up of experts and luminaries in the applicant's field, in order to assess the relevance of the stated goals and the potential of the applicant. Once a protégé has been selected, the Board of Directors of the foundation will approve the chosen recipients.

The following are criteria you use for grant renewal.

Recipients must:

Participate actively in their fields, including maintaining frequent contact with you and with their mentors, and participate in conferences, exhibits, or roundtables, as pertinent.

Provide receipts and other documentation showing the use of all grant monies awarded.

Spend the majority of their time in the communities from which they came, and seek to improve the conditions of their particular communities beyond the length of the program. The goal of each protégé should be to one day mentor other youths in his or her chosen field and to bring about positive change in his or her own community.

You will maintain records of your mentorship participants, including the names and addresses of its protégés and mentors, as well as accounts of their activities and any expenses paid to facilitate the mentorship. Records will also include information obtained to evaluate protégés, confirmation that the protégé is not a disqualified person to the foundation, the amount and purpose of any assets spent, how the mentorship was supervised and how any possible diversion of funds was investigated and addressed.

You closely monitor and evaluate the expenditure of funds and the progress made by each recipient. A representative from the foundation will attend conferences and exhibitions at which protégés are participating, and will also continue to maintain frequent contact with all of the participants of the program, including the mentors. Much of the support is provided in the form of in-kind support (such as hotel rooms), or in the reimbursement of specific expenses documented by the protégé. While mentors provide guidance, support, and networking opportunities, the foundation acts as a kind of sub-mentor by monitoring the protégés' progress, finding adequate housing and other necessary facilities, recording all expenses, and sponsoring foreign individuals for visa or other purposes. To the extent the support is distributed in the form of a stipend/grant to a protégé, the protégé will be required to sign a letter or agreement committing to how the funds will be used, and agreeing to oversight by the foundation and to fulfilling any reporting requirements. Upon completion of each mentorship, the foundation and the protégé will work together to produce a summary report describing the goals achieved, the work produced, and the protégé's use of resources. If the mentorship goes beyond one year in duration, the foundation will require annual interim reports.

Any possible diversion of grant funds will be promptly investigated. If the foundation discovers that funds have been misused, it will take all reasonable and appropriate steps to recover diverted funds, and will make no further distributions to that recipient, unless it is able to obtain assurances that future diversion will not occur and protégé will take extraordinary precautions to prevent future diversion from occurring.

BASIS FOR OUR DETERMINATION

The law imposes certain excise taxes on the taxable expenditures of private foundations (Code section 4945). A taxable expenditure is any amount a private foundation pays as a grant to an

individual for travel, study, or other similar purposes.

However, a grant that meets all of the following requirements of Code section 4945(g) is not a taxable expenditure.

The foundation awards the grant on an objective and nondiscriminatory basis.

The IRS approves in advance the procedure for awarding the grant.

The grant is:

A scholarship or fellowship subject to section 117(a) and is to be used for study at an educational organization described in section 170(b)(1)(A)(ii); or

A prize or award subject to the provisions of section 74(b), if the recipient of the prize or award is selected from the general public; or

To achieve a specific objective; produce a report or similar product; or improve or enhance a literary, artistic, musical, scientific, teaching, or other similar skill or talent of the recipient.

To receive approval of its grant procedures, Treasury Regulations section 53.4945-4(c)(1) requires that a private foundation demonstrate that:

The grant procedure includes an objective and nondiscriminatory selection process.

The grant procedure results in the recipients performing the activities the grants were intended to finance.

The foundation plans to obtain reports to determine whether the recipients have performed the activities that the grants were intended to finance.

OTHER CONDITIONS THAT APPLY TO THIS DETERMINATION

This determination covers only the grant program described above. This approval will apply to succeeding grant programs only if their standards and procedures don't differ significantly from those described in your original request.

This determination applies only to you. It may not be cited as precedent.

You cannot rely on the conclusions in this letter if the facts you provided have changed substantially.

You must report any significant changes in your program to the Cincinnati Office of Exempt Organizations at:

Internal Revenue Service

Exempt Organizations Determinations

P.O. Box 2508

Cincinnati, OH 45201

You cannot make grants to your creators, officers, directors, trustees, foundation managers, or members of selection committees or their relatives.

All funds distributed to individuals must be made on a charitable basis and must further the purposes of your organization. You cannot award grants for a purpose that is inconsistent with Code section 170(c)(2)(B).

You should keep adequate records and case histories so that you can substantiate your grant distributions with the IRS if necessary.

We've sent a copy of this letter to your representative as indicated in your power of attorney.

Please keep a copy of this letter in your records.

If you have any questions, please contact the person listed at the top of this letter.

Sincerely,

Holly O. Paz

Director, Exempt Organizations

Rulings and Agreements

Comments Sought on Exempt Organization Return.

The IRS asked for public comment on Form 990, "Return of Organization Exempt From Income Tax Under Section 501(c), 527, or 4947(a)(1) of the Internal Revenue Code (except black lung benefit trust or private foundation)," and related schedules. Comments are due by June 25, 2013.

Send comments regarding the burden estimate, or any other aspect of the information collection, including suggestion for reducing the burden, to (1) Office of Information and Regulatory Affairs, Office of Management and Budget, Attention: Desk Officer for Treasury, New Executive Office Building, Room 10235, Washington, DC 20503, or email at OIRA_Submission@OMB.EOP.GOV and (2) Treasury PRA Clearance Officer, 1750 Pennsylvania Ave. NW., Suite 8140, Washington, DC 20220, or email at PRA@treasury.gov.

IRS Releases Final Report on Tax-Exempt Colleges and Universities Compliance Project.

The Internal Revenue Service today released its final report summarizing audit results from the IRS' colleges and universities study, which began in 2008. This final report describes the agency's multi-year project on a major segment of tax-exempt organizations.

"The audits identified some significant compliance issues at the colleges and universities examined," said Lois Lerner, Director, Exempt Organizations division. "Because these issues may well be present elsewhere across the tax-exempt sector, all exempt organizations need to be aware of the importance of accurately reporting unrelated business income and providing appropriate executive compensation."

The attached final report focuses on two primary areas within the examinations: reporting of unrelated business taxable income, and compensation, including, employment tax and retirement plan issues.

The full report is available at:

http://www.irs.gov/pub/irs-tege/CUCP_FinalRpt_042513.pdf

IRS: Attend the Exempt Organizations Workshop at the 2013 Tax Forums.

This two-hour workshop will include a review of recent changes to the Form 990, Return of Organization Exempt from Income Tax. In addition, the workshop will present several topics that are of interest to tax professionals who work with exempt organizations.

Exempt Organizations will participate in the IRS Nationwide Tax Forums in six cities starting in July. The forums are a major outreach event providing three packed days of seminars, workshops, focus groups and an exhibit hall for the tax practitioner community. In addition to getting the latest tax information, tax professionals can earn continuing professional education credits for their attendance.

For more information, go to:

<http://www.irs.gov/Tax-Professionals/IRS-Nationwide-Tax-Forum-Information>

FASB: Update No. 2013-06—Not-for-Profit Entities (Topic 958): Services Received from Personnel of an Affiliate (a consensus of the FASB Emerging Issues Task Force)

The amendments in this Update require a recipient not-for-profit entity to recognize all services received from personnel of an affiliate that directly benefit the recipient not-for-profit entity. Those services should be measured at the cost recognized by the affiliate for the personnel providing those services. However, if measuring a service received from personnel of an affiliate at cost will significantly overstate or understate the value of the service received, the recipient not-for-profit entity may elect to recognize that service received at either (1) the cost recognized by the affiliate for the personnel providing that service or (2) the fair value of that service.

The full Update is available at:

<http://www.fasb.org/cs/BlobServer?blobkey=id&blobwhere=1175826718911&blobheader=application%2Fpdf&blobcol=urldata&blobtable=MungoBlobs>

IRS: Foundation's Expenditures for Mentorship Program Aren't Taxable.

The IRS ruled that expenditures made through a private foundation's mentorship program for disadvantaged youth will not be taxable.

Dear * * *:

You asked for advance approval of your educational grant procedures under Internal Revenue Code section 4945(g)(3). This approval is required because you are a private foundation that is exempt from federal income tax.

OUR DETERMINATION

We approved your procedures for awarding educational grants. Based on the information you submitted, and assuming you will conduct your program as proposed, we determined that your procedures for awarding educational grants meet the requirements of Code section 4945(g)(3). As a result, expenditures you make under these procedures won't be taxable.

DESCRIPTION OF YOUR REQUEST

Your letter indicates that you will operate a mentorship program.

The program will provide greater opportunities for disadvantaged youth around the world to realize their full potential and attain mentorships by introducing young adults to leading entrepreneurs, artists, and academics, by sponsoring visa applications, and by covering expenses related to the pursuit of their goals whether in the fields of science, arts, sports, academia, or otherwise.

You intend to both publicize your program on your website, and through foreign and international websites that have the potential of drawing a wide audience from around the world.

You will have application forms completed by both a nominating organization and the potential protégé. In the future you intend to allow applicants to self-nominate.

You aim to support young adults, ages 18 to 30, who have faced, or are facing, significant adversity in life. You do not define what specifically constitutes adversity. It is up to the applicants to demonstrate how their ability to develop in their chosen fields has been stifled by individual circumstances. You will consider individuals who have not had the economic means to pursue their goals, as well as individuals living under oppressive regimes, or in repressive communities. These are just a few examples of the kind of adversity that might qualify a candidate for the mentorship program.

Specific criteria for selection will be based on the following factors:

Age: Applicants should be between the ages of 18 and 30.

Talent: Applicants must demonstrate talent, potential, and perseverance in their chosen fields.

Need: Applicants must demonstrate that they have faced significant adversity, as defined by each applicant's individual circumstances.

Professional Development Potential: Applicants should demonstrate that the foundation can significantly impact his or her ability to realize his or her full potential.

Leadership Potential: Applicants must demonstrate a genuine desire to give back to their communities in a meaningful and realistic way. Specifically, in accordance with W, protégés must work to bring about positive change in one of the following categories: alleviation of poverty and hunger, improvement of education for all, elimination of discrimination, environmental sustainability, improvement of global health, improvement of global economy, or attainment of world

peace.

Substantial contributors, foundation managers, officers, directors, and employees of the foundation, as well as their family members, are ineligible to participate in the mentorship program.

You currently plan to run between two and six mentorships each year. You hope to scale up to ten to twelve mentorships in the future depending on the availability of funding, the particular needs of each recipient, and the overall success of your programs.

You envision providing support to protégés of up to \$z per recipient over the course of a year or, some cases, more than a year. The support will be used to cover the expenses of travel, conference participation, art exhibits, supplies, courses, and other expenses related to each protégés particular field of interest, as well as in some cases a cash stipend.

You have adopted the following mandatory procedure in order to ensure continuing compliance with the post-9/11 Executive Orders and with Office of Foreign Assets Control, OFAC, requirements:

You will operate in compliance with all statutes, Executive Orders, and regulations restricting or prohibiting U.S. persons from engaging in transactions and dealings with countries, entities, or individuals subject to economic sanctions administered by OFAC.

You will check the OFAC List of Specially Designated Nationals, SDN, and Blocked Persons before dealing with persons including individuals, organizations and entities and specifically avoid dealing with any persons on the list.

You will not enter into a relationship with a grantee where doubts exist about the grantees' ability to ensure safe delivery of charitable resources independent of influence by or association with any terrorist organization.

You will not engage in trade or transaction activities that violate the regulation behind OFAC's country-based sanctions programs or engage in trade or transaction activities with sanctions targets named on OFAC's SDN list.

You will acquire from OFAC the appropriate license and registration where necessary.

The selection committee varies per protégé. The President and Executive Director, together field applications to select the most promising candidates. The candidates will then be presented to an individualized selection committee made up of experts and luminaries in the applicant's field, in order to assess the relevance of the stated goals and the potential of the applicant. Once a protégé has been selected, the Board of Directors of the foundation will approve the chosen recipients.

The following are criteria you use for grant renewal.

Recipients must:

Participate actively in their fields, including maintaining frequent contact with you and with their mentors, and participate in conferences, exhibits, or roundtables, as pertinent.

Provide receipts and other documentation showing the use of all grant monies awarded.

Spend the majority of their time in the communities from which they came, and seek to improve the conditions of their particular communities beyond the length of the program. The goal of each protégé should be to one day mentor other youths in his or her chosen field and to bring about

positive change in his or her own community.

You will maintain records of your mentorship participants, including the names and addresses of its protégés and mentors, as well as accounts of their activities and any expenses paid to facilitate the mentorship. Records will also include information obtained to evaluate protégés, confirmation that the protégé is not a disqualified person to the foundation, the amount and purpose of any assets spent, how the mentorship was supervised and how any possible diversion of funds was investigated and addressed.

You closely monitor and evaluate the expenditure of funds and the progress made by each recipient. A representative from the foundation will attend conferences and exhibitions at which protégés are participating, and will also continue to maintain frequent contact with all of the participants of the program, including the mentors. Much of the support is provided in the form of in-kind support (such as hotel rooms), or in the reimbursement of specific expenses documented by the protégé. While mentors provide guidance, support, and networking opportunities, the foundation acts as a kind of sub-mentor by monitoring the protégés' progress, finding adequate housing and other necessary facilities, recording all expenses, and sponsoring foreign individuals for visa or other purposes. To the extent the support is distributed in the form of a stipend/grant to a protégé, the protégé will be required to sign a letter or agreement committing to how the funds will be used, and agreeing to oversight by the foundation and to fulfilling any reporting requirements. Upon completion of each mentorship, the foundation and the protégé will work together to produce a summary report describing the goals achieved, the work produced, and the protégé's use of resources. If the mentorship goes beyond one year in duration, the foundation will require annual interim reports.

Any possible diversion of grant funds will be promptly investigated. If the foundation discovers that funds have been misused, it will take all reasonable and appropriate steps to recover diverted funds, and will make no further distributions to that recipient, unless it is able to obtain assurances that future diversion will not occur and protégé will take extraordinary precautions to prevent future diversion from occurring.

BASIS FOR OUR DETERMINATION

The law imposes certain excise taxes on the taxable expenditures of private foundations (Code section 4945). A taxable expenditure is any amount a private foundation pays as a grant to an individual for travel, study, or other similar purposes.

However, a grant that meets all of the following requirements of Code section 4945(g) is not a taxable expenditure.

The foundation awards the grant on an objective and nondiscriminatory basis.

The IRS approves in advance the procedure for awarding the grant.

The grant is:

A scholarship or fellowship subject to section 117(a) and is to be used for study at an educational organization described in section 170(b)(1)(A)(ii); or

A prize or award subject to the provisions of section 74(b), if the recipient of the prize or award is selected from the general public; or

To achieve a specific objective; produce a report or similar product; or improve or enhance a literary, artistic, musical, scientific, teaching, or other similar skill or talent of the recipient.

To receive approval of its grant procedures, Treasury Regulations section 53.4945-4(c)(1) requires that a private foundation demonstrate that:

The grant procedure includes an objective and nondiscriminatory selection process.

The grant procedure results in the recipients performing the activities the grants were intended to finance.

The foundation plans to obtain reports to determine whether the recipients have performed the activities that the grants were intended to finance.

OTHER CONDITIONS THAT APPLY TO THIS DETERMINATION

This determination covers only the grant program described above. This approval will apply to succeeding grant programs only if their standards and procedures don't differ significantly from those described in your original request.

This determination applies only to you. It may not be cited as precedent.

You cannot rely on the conclusions in this letter if the facts you provided have changed substantially.

You must report any significant changes in your program to the Cincinnati Office of Exempt Organizations at:

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You cannot make grants to your creators, officers, directors, trustees, foundation managers, or members of selection committees or their relatives.

All funds distributed to individuals must be made on a charitable basis and must further the purposes of your organization. You cannot award grants for a purpose that is inconsistent with Code section 170(c)(2)(B).

You should keep adequate records and case histories so that you can substantiate your grant distributions with the IRS if necessary.

We've sent a copy of this letter to your representative as indicated in your power of attorney.

Please keep a copy of this letter in your records.

If you have any questions, please contact the person listed at the top of this letter.

Sincerely,

Holly O. Paz

Director, Exempt Organizations

IRS: Foundation's Expenditures for Mentorship Program Aren't Taxable.

The IRS ruled that expenditures made through a private foundation's mentorship program for disadvantaged youth will not be taxable.

Dear * * *:

You asked for advance approval of your educational grant procedures under Internal Revenue Code section 4945(g)(3). This approval is required because you are a private foundation that is exempt from federal income tax.

OUR DETERMINATION

We approved your procedures for awarding educational grants. Based on the information you submitted, and assuming you will conduct your program as proposed, we determined that your procedures for awarding educational grants meet the requirements of Code section 4945(g)(3). As a result, expenditures you make under these procedures won't be taxable.

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Sincerely,

Holly O. Paz

Director, Exempt Organizations

Rulings and Agreements

IRS: Settlement Agreement Won't Result in Self-Dealing.

The IRS ruled that the execution, delivery, and performance of a settlement agreement providing for the purchase of limited partnership interests by the trustees of a private foundation will not result in self-dealing.

Dear * * *

We have considered your ruling request dated October 5, 2012. You are requesting a ruling under § 4941 of the Code with regard to a Settlement Agreement affecting certain testamentary bequests to a private foundation described in §§ 501(c)(3) and 509(a).

FACTS

A and B are the surviving children of C. C, a resident of State, died on Date 1.

D is a limited partnership, in which each of A, B and C held certain partnership interests at the time of C's death. The assets held by C at C's death included a x% general partnership interest in D and a y% limited partnership interest in D (collectively, the "Interests").

E is a private foundation described in §§ 501(c)(3) and 509(a) of the Code. The two Executors of C's estate also serve as the two co-Trustees of E.

Prior to C's death, A, B and C executed an agreement granting each of A and B the right, upon C's death, to purchase one-half of C's limited partnership interests in D at a price equal to the value of those interests as of the date of C's death as determined by an independent qualified appraiser, subject to increase or decrease equal to the final determination of the value of those interests in the federal estate tax proceedings for C's estate (the "First Option").

C's Will, as submitted for probate in the court with jurisdiction over C's estate, bequeathed C's general partnership interest in D outright to E.

The Will further directed the Executors to offer (subject to the terms and conditions of the Partnership Agreement of D) in writing to each of A and B the option to purchase for cash up to one-half of C's limited partnership interests in D that C owned at C's death, at its value as finally fixed and determined for federal estate tax purposes after independent appraisal (the "Second Option").

In addition, C's Will provided that the residue of C's estate, after satisfaction of certain specific bequests set forth in C's Will and after satisfaction of debts, administrative expenses and taxes attributable to C's estate, would pass to E.

Subsequent to submission to the court of C's Will for probate, a series of arbitration and court proceedings were launched involving A, B, the Executors and the Trustees. Each of the First Option, the Second Option and the bequests to E was challenged as part of the various proceedings. In addition, the Executors filed claims against A and B for alleged over distributions from D to A and B.

After approximately z years of litigation and arbitration proceedings regarding the Interests, the Attorney General of State intervened in an attempt to help resolve the parties' disputes. With the help of the Attorney General of State, A, B, the Executors and the Trustees entered into a Settlement Agreement, effective as of Date 2.

Under the Settlement Agreement, A and B will purchase all of the Interests at a price set forth in the Settlement Agreement. This price is equal to the value of the Interests as reported by C's estate for federal estate tax purposes. In addition, A and B will pay a designated amount in settlement of all additional claims made by the Executors against A and B with regard to the Interests.

The Attorney General of State consented to the Settlement Agreement. On Date 3, the court with jurisdiction over C's estate issued an order approving the Settlement Agreement.

RULING REQUESTED

The execution, delivery, and performance of the Settlement Agreement, and the consummation by the parties of the transactions contemplated therein, will not constitute acts of direct or indirect self-dealing under § 4941, and none of the parties to the Settlement Agreement, including their executors, trustees, directors, officers, owners, employees, agents, and attorneys, will be liable for tax under § 4941 for such actions.

LAW

Section 4941(a) imposes certain excise taxes on direct and indirect acts of self-dealing between a disqualified person and a private foundation, and also imposes a separate excise tax on the participation by any foundation manager in an act of self-dealing between a disqualified person and a private foundation, knowing it is such an act, unless such participation is not willful and is due to reasonable cause.

Section 4941(d)(1)(A) provides that for purposes of § 4942 the term self-dealing means any direct or indirect sale or exchange, or leasing, of property between a private foundation and a disqualified person.

Section 4941(d)(1)(E) defines self-dealing to include any direct or indirect transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a private foundation. Section 4946(a) provides that the term "disqualified person" with respect to a private foundation includes a substantial contributor to the foundation, a family member of a substantial contributor (including children), and foundation managers (including trustees and individuals with similar powers or responsibilities).

Section 53.4946-1(a)(1)(i) of the Foundation and Similar Excise Tax Regulations, with reference to § 507(d)(2) of the Code, defines the term "substantial contributor" as (1) any person who contributed or bequeathed an aggregate amount of more than \$5,000 to the private foundation, if such amount is more than 2 percent of the total contributions and bequests received by the private foundation in the year of such contribution; and (2) in the case of a trust, the creator of the trust.

In *Rockefeller v. United States*, 572 F. Supp. 9 (E.D. Ark. 1982), aff'd 718 F.2d 290 (8th Cir. 1983), cert. den. 466 U.S. 962 (1984), the court held that purchase by a decedent's son, who was also

executor of the estate, of estate property earmarked for a private foundation was indirect self-dealing.

In *Estate of Reis v. Comm'r*, 87 T.C. 1016 (1986), the court held that because a foundation which was a beneficiary of an estate had an expectancy interest in the estate, sale of estate property otherwise passing from the estate to the foundation constituted acts of indirect self-dealing under § 4941.

ANALYSIS

Self-dealing under § 4941 may occur by virtue of the transfer of property held in an estate to which a private foundation has an interest or expectancy. *Rockefeller v. United States*, 572 F. Supp. 9 (E.D. Ark. 1982), *aff'd* 718 F.2d 290 (8th Cir., 1983), *cert. den.* 466 U.S. 962 (1984); *Reis*, 87 T.C. 1016 (1986). Absent the litigation and arbitration proceedings, E arguably had an expectancy under the terms of C's will (as submitted for probate) either in the Interests themselves or, with regard to the limited partnership interests, in an amount of money equal in value to the option price. In fact, E's ultimate expectancy with regard to the Interests depended on final resolution of the litigation and arbitration proceedings.

Although the parties to the Settlement Agreement could have awaited the end of those proceedings, doing so may have taken many more years, cost a considerable amount in legal fees, and ultimately resulted in less property for E. Instead, the parties chose to settle the dispute. All parties to the Settlement Agreement were represented by independent counsel, and there is no suggestion of collusion to benefit any particular party. The Attorney General of State participated in facilitating the Settlement Agreement and consented to its terms. The court with appropriate jurisdiction over C's estate has approved the Settlement Agreement.

Entering into the Settlement Agreement will eliminate the risk that E's expectancy with regard to the Interests might be reduced if the litigation and arbitration proceedings continued, will preclude the need to expend additional charitable funds pursuing the litigation, and will allow E to access the property passing to it from C's estate and begin to use that property in furtherance of its charitable activities. Because the Settlement Agreement was the product of arm's-length negotiations, including the participation and consent of the Attorney General of State and approval of the court with jurisdiction over C's estate, E's expectancy in C's estate with regard to the Interests is established by the Settlement Agreement. All parties acting in performance of the Settlement Agreement are viewed as merely carrying out their legal rights and obligations with regard to the Interests.

RULING

Accordingly, based on the facts and circumstances discussed above, we rule that the execution, delivery and performance of the Settlement Agreement, and the consummation by the parties of the transactions contemplated therein, does not give rise to self-dealing under § 4941, and no tax under § 4941 is due with regard to the transactions described in the Settlement Agreement.

This ruling will be made available for public inspection under § 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 taxpayer 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 federal tax liabilities, 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,

Matthew L. Giuliano

Manager, Exempt Organizations

Guidance Group 1

IRS: Detention Facilities Aren't Healthcare Facilities for REIT Purposes.

The IRS ruled a corporation's correctional, detention, and re-entry residential and nonresidential facilities won't be treated as healthcare facilities under section 856(l)(4)(B) and contract payments from government tenants for the residential facilities will be treated as rents from real property for purposes of section 856(d)(1).

Dear * * *:

This is in reply to a letter dated July 18, 2012, and further submissions, in which Taxpayer requests rulings in connection with its intent to elect to be taxed as a real estate investment trust ("REIT") under section 856 of the Internal Revenue Code.

Taxpayer is a publicly traded State A corporation that intends to elect to be taxed as a REIT. Taxpayer presently owns, leases, and operates correctional, detention, and re-entry facilities. Taxpayer also presently provides community based services to supervise and assist parolees and probationers. Taxpayer's facilities include residential facilities and non-residential facilities. Taxpayer's residential facilities include correctional and detention facilities, community-based services ("CBS") halfway houses, and youth services residential facilities (collectively the "Residential Facilities"). Taxpayer's non-residential facilities include CBS day reporting centers and youth services non-residential facilities ("Non-Residential Facilities").

Following its election to be taxed as a REIT, Taxpayer intends to create one or more TRSs to operate and provide services that it presently provides in connection with its Residential Facilities and Non-Residential Facilities. Taxpayer also intends to create one or more TRSs to which it will contribute certain contracts and facilities, as described below.

Taxpayer is seeking rulings that (1) the Residential Facilities and Non-Residential Facilities are not

“health care facilities” in whole or in part under section 856(l)(4)(B); (2) the amounts received under Taxpayer’s contracts with government tenants for the Residential Facilities will be treated as “rents from real property” for purposes of section 856(d)(1); and (3) the payments Taxpayer collects on behalf of its TRSs for the Services (as later defined) the TRSs provide at a Financed Facility (as later defined) will not be disqualified income for purposes of the REIT income tests.

Taxpayer’s Current Business

Residential Facilities

Correction and Detention Facilities

Taxpayer contracts with federal, state, and foreign government entities (“government tenants”) to provide facilities to house offenders or detainees on their behalf. The contracts are generally awarded through a competitive bid process.

Taxpayer owns or leases correctional and detention facilities that are currently under contract with government tenants. Taxpayer also has manage-only contracts under which it operates correctional and detention facilities that government tenants either own directly or lease from a third party. Taxpayer represents that the fair market value of the personal property that will be owned by the REIT in the owned and leased Residential Facilities will not exceed fifteen percent of the total fair market value of the owned and leased Residential Facilities.

Under a majority of the contracts for the correctional and detention facilities that Taxpayer owns or leases, Taxpayer receives a monthly lump sum amount from a government tenant for the use of the facility. Taxpayer agrees to house a certain number of occupants (the “guaranteed minimum”) and provide related services. The monthly lump sum amount is calculated pursuant to the terms of the contract by multiplying the guaranteed minimum by a daily rate per occupant. If a government tenant needs space for more occupants than are included in the guaranteed minimum, it will pay an additional amount for each day that an extra occupant spends in the facility. The rate for extra occupants is generally lower than the rate for the occupants covered by the guaranteed minimum. Some of Taxpayer’s contracts do not have a guaranteed minimum, and a government tenant’s monthly payment will be based on a daily rate per occupant.

The contracts typically have terms from three to five years with multiple renewal options, ranging from one to five years, with a total contract period ranging from ten to fifteen years. At the end of the contract period, Taxpayer must competitively bid to receive the contract for another term.

Although Taxpayer’s contracts vary by customer, Taxpayer is generally required to provide the following services (the “Services”):

- Facility security, including guard supervision
- Food service
- Counseling and substance abuse treatment
- Basic medical and dental care
- Academic and vocational programming
- Administrative and management services, including recordkeeping and reporting
- Facility maintenance and utilities
- Secure transportation of occupants
- Intake and screening

As mentioned above, the Services required by the contracts include some level of medical, dental,

and mental health services. To avoid the security risk and expense of taking an occupant offsite to receive medical services, Taxpayer employees perform routine medical, dental, and mental health services in a segregated area of the facility. These employees also do an intake screening when a resident arrives at the facility to ascertain the health status of the inmate. The screenings are necessary to shield the other occupants and the staff from exposure to contagious illness. Medical employees may include doctors, nurses, and/or technicians but Taxpayer only provides basic medical services. None of the facilities are licensed as medical or dental facilities. A few of the facilities have a license from a state agency to provide substance abuse counseling. None of the facilities are licensed as medical facilities that are operated by a provider that is eligible for participation in the Medicare program.

CBS Facilities: Halfway Houses

Taxpayer also owns, leases, and manages CBS facilities. There are two types of CBS facilities: halfway houses and youth services residential facilities, which are Residential Facilities, and day reporting centers and youth services non-residential facilities, which are Non-Residential Facilities and are described below.

Residential Facilities

The halfway houses provide a home to federal or state offenders who are reentering society after incarceration. Taxpayer's halfway house contracts are awarded by government tenants in a competitive bid process and generally have a term of one to two years with three to four annual renewal periods. Taxpayer bills government tenants monthly pursuant to the contract terms, based on a formula price. The monthly payment is calculated based on the number of occupants residing at the facility at a daily rate per occupant.

Pursuant to the contracts with government tenants to house these newly released individuals, Taxpayer is required to provide drug testing, recordkeeping and reporting, food services, vocational and educational programming, employment assistance, and substance abuse and family counseling.

A few of the halfway houses employ a psychologist, but generally no other medical care is available onsite. One halfway house employs a nurse who provides basic medical services. None of the halfway houses are licensed as medical facilities that are operated by a provider that is eligible for participation in the Medicare program.

Residential Youth Services Facilities

Taxpayer owns, leases, and manages residential and non-residential youth services facilities. Government tenants use Taxpayer's residential youth services facilities to provide housing for juvenile offenders.

Taxpayer contracts with multiple government tenants to house youths in its residential youth services facilities. Taxpayer bills government tenants monthly pursuant to the contract terms, based on a formula price. The monthly payment is calculated based on the number of youths residing at the facility at a daily rate per youth. Each facility houses residents for several government tenants. The contracts do not have guaranteed minimums and government tenants do not have any specific amount of space reserved.

Taxpayer's residential youth services facilities provide multiple, residential, education programs specifically designed to address the needs of individuals within the juvenile justice system with programs tailored to the specific needs of youthful offenders. The programs typically vary in length

from one to fourteen months. Taxpayer expects youths to stay at the facility for the entire length of the relevant programs, as approximately 90% of youths complete their programs.

As part of its contracts with government tenants for the use of facilities to shelter youths, Taxpayer is required to provide food service, counseling, supervision, vocational and culinary training, and transportation to the occupants.

Employees at the residential youth services facilities provide therapy and substance abuse counseling to the occupants. Nurses provide some basic medical care, but most medical needs are met offsite. Six of the youth services residential facilities are licensed by the state to treat alcoholism and substance abuse. Additionally, three of the youth services residential facilities are licensed by the state to provide mental health services. None of the residential youth services facilities are licensed as medical facilities that are operated by a provider that is eligible for participation in the Medicare program.

Non-Residential Facilities

Community-Based Services: Day Reporting Centers

Taxpayer operates CBS day reporting centers where it is required to provide drug testing, supervision, vocational and educational programming, and some counseling to offenders who are reentering society after incarceration. Offenders report to the day reporting centers a few days a week and spend at most a few hours at the facility per day. These contracts typically require Taxpayer to lease specific storefronts in a shopping center in which to provide the services. For a few CBS day reporting centers, a government tenant leases the space and Taxpayer only operates the center. Several of the CBS day reporting centers employ therapists, but generally no other medical care is available. Furthermore, the day reporting centers are not licensed as medical facilities that are operated by a provider that is eligible for participation in the Medicare program.

Non-Residential Youth Services Facilities

The non-residential youth services facilities are similar to the day reporting centers discussed above. They are operated in storefronts. Taxpayer provides programming, counseling, and mental health case management, but it does not house the youths on behalf of government tenants. No medical care is provided. They are not licensed as medical facilities operated by a provider that is eligible for participation in the Medicare program.

Financed Facility

In some cases, Taxpayer leases land from a state agency, builds a facility on the leased land, and then operates the facility for a government tenant for the duration of the contract. At the end of the contract, title to the facility shifts to the government tenant ("Financed Facilities").¹

Taxpayer's Proposed Restructuring

Taxpayer intends to operate as a REIT beginning with an election to be taxed as a REIT for its Year 1 taxable year. Taxpayer also intends to create one or more wholly-owned subsidiaries, which will elect to be treated as TRSs (Taxpayer's TRSs). Taxpayer's TRSs will provide the Services described above to government tenants and will be compensated by Taxpayer at an arm's length rate. Taxpayer will contribute the manage-only Residential Facilities contracts and the Non-Residential Facilities to TRSs or make TRS elections for the existing entities that hold these assets.

LAW AND ANALYSIS

Section 856(c)(2) provides that at least 95 percent of a REIT's gross income must be derived from specified sources that include rents from real property, and section 856(c)(3) provides that at least 75 percent must be derived from sources, that likewise include, rents from real property.

Section 856(d)(1) provides that rents from real property include (subject to exclusions provided in section 856(d)(2)): (A) rents from interests in real property; (B) charges for services customarily furnished or rendered in connection with the rental of real property, whether or not such charges are separately stated; and (C) rent attributable to personal property leased under, or in connection with, a lease of real property, but only if the rent attributable to the personal property for the taxable year does not exceed 15 percent of the total rent for the tax year attributable to both the real and personal property leased under, or in connection with, the lease. With respect to each lease of real property, rent attributable to personal property for the taxable year is that amount which bears the same ratio to total rent for the taxable year as the average of the fair market values of the personal property at the end of the taxable year bears to the average of the aggregated fair market values of both the real property and the personal property at the beginning and at the end of such taxable year.

Section 1.856-4(b) provides that subject to the exceptions in sections 856(d) and section 1.856-4(b), the term, "rents from real property" means, generally, the gross amounts received for the use of, or the right to use, real property of the REIT. Section 1.856-4(b) provides that the term rents from real property includes charges for services customarily furnished or rendered in connection with the rental of real property, whether or not the charges are separately stated. Services furnished to tenants of a particular building will be considered as customary if, in the geographic market in which the building is located, tenants in buildings of similar class are customarily provided with the service. Where it is customary, in a particular geographic marketing area, to furnish electricity or other utilities to tenants in buildings of a particular class, the submetering of utilities to tenants in such buildings will be considered a customary service.

Section 856(d)(2)(C) provides that any impermissible tenant service income is excluded from the definition of rents from real property. Section 856(d)(7)(A) defines impermissible tenant service income to mean, with respect to any real or personal property, any amount received or accrued directly or indirectly by the REIT for services furnished or rendered by the REIT to tenants at the property, or for managing or operating the property.

Section 856(d)(7)(C) provides certain exclusions from impermissible tenant service income. Section 856(d)(7)(C) provides that for purposes of section 856(d)(7)(A), services furnished or rendered, or management or operation provided, through an independent contractor from whom the REIT does not derive or receive any income or through a TRS of such trust shall not be treated as furnished, rendered, or provided by the REIT, and any amount which would be excluded from unrelated business taxable income under section 512(b)(3) if received by an organization described in section 511(a)(2) shall not be taken into account.

Section 512(b)(3) provides, in part, that there shall be excluded from the computation of unrelated business taxable income all rents from real property and all rents from personal property leased with such real property, if the rents attributable to such personal property are an incidental amount of the total rents received or accrued under the lease, determined at the time the personal property is placed in service.

Section 1.512(b)-1(c)(5) provides that payments for the use or occupancy of rooms and other space where services are also rendered to the occupant, such as for the use or occupancy of rooms or other quarters in hotels, boarding houses, or apartment houses furnishing hotel services, or in tourist camps or tourist homes, motor courts or motels, or for the use or occupancy of space in

parking lots, warehouses, or storage garages, do not constitute rents from real property. Generally, services are considered rendered to the occupant if they are primarily for his convenience and are other than those usually or customarily rendered in connection with the rental of rooms or other space for occupancy only. The supplying of maid service, for example, constitutes such service; whereas the furnishing of heat and light, the cleaning of public entrances, exits, stairways and lobbies, and the collection of trash are not considered as services rendered to the occupant.

Section 856(d)(7)(B) provides that if the amount of impermissible tenant service income exceeds one percent of all amounts received or accrued during the tax year directly or indirectly by the REIT with respect to the property, the impermissible tenant service income of the REIT will include all of the amounts received or accrued with respect to the property.

In Rev. Rul. 2002-38, 2002-2 C.B. 4, a REIT pays its TRS to provide noncustomary services to tenants. The REIT does not separately state charges to tenants for the services. Thus, a portion of the amounts received by the REIT from tenants represents an amount received for services provided by the TRS. TRS employees perform all of the services and TRS pays all of the costs of providing the services. The TRS also rents space from the REIT for carrying out its services to tenants. The revenue ruling concludes that the services provided to the REIT's tenants are considered to be rendered by the TRS, rather than the REIT, for purposes of § 856(d)(7)(C)(i). Accordingly, the services do not give rise to impermissible tenant service income and do not cause any portion of the rents received by the REIT to fail to qualify as rents from real property under § 856(d).

Section 856(l) provides that a REIT and a corporation (other than a REIT) may treat such corporation as a TRS if the REIT directly or indirectly owns stock in the corporation, and the REIT and the corporation jointly elect such treatment.

Section 856(l)(3)(A) provides that a TRS cannot directly or indirectly operate or manage a lodging facility or a health care facility. Section 856(l)(4)(B) provides that the term "health care facility" has the meaning given such term in section 856(e)(6)(D)(ii).

A "health care facility" is defined in section 856(e)(6)(D)(ii) as a hospital, nursing facility, assisted living facility, congregate care facility, qualified continuing care facility (as defined in section 7872(g)(4)), or other licensed facility which extends medical or nursing or ancillary services to patients and which was operated by a provider of such services that is eligible for participation in the Medicare program under Title XVII of the Social Security Act [subchapter XVIII of chapter 7 of Title 42 (42 U.S.C.A. § 1395 et seq.)] with respect to the facility.

Ruling 1: The Residential Facilities and Non-Residential Facilities are not "health care facilities" in whole or in part under section 856(l)(4)(B).

The Residential Facilities and Non-Residential Facilities are not hospitals, nursing facilities, assisted living facilities, qualifying continuing care facilities or other licensed facilities that were eligible for participation in Medicare. Therefore, unless they are congregate care facilities, the Residential Facilities and Non-Residential Facilities are not health care facilities.

Although congregate care facility is not defined in either the statute or the regulations, there are commonly used definitions of congregate care. The common theme among these definitions is the sharing of living space, dining space, transportation, and group activities. The definitions do not describe any level of medical or health care services. Nevertheless, further refinement to these definitions is needed for section 856 definitional purposes.

Congregate care facility must be read in context. Section 856(l)(4)(B) and section 856(e)(6)(D)(ii)

describe various facilities that provide health care, not as an auxiliary function, but as part of the primary function of the facility (e.g., hospitals and nursing facilities) or in connection with a facility that has the primary function of providing health care (e.g., assisted living facilities). We conclude that it is not enough that a facility that meets the general definitions of congregate care offers medical services; to be a congregate care facility under section 856(l)(4)(B), the facility's health care concerns must be part of the primary function of the facility or sufficiently related to the provision of health care as implied under section 856(l)(4)(B). In the present case, the Residential and Non-Residential Facilities are not related to a health care facility and the medical care provided by the those facilities is not part of the primary function of those facilities.

Taxpayer is obligated to provide space that government tenants use to incarcerate prisoners and detainees. As part of its operations, Taxpayer provides a certain level of shared dining and living space and group activities. The contracts require Taxpayer to provide the Services, including some level of medical, dental, and mental health services, as required by the prisoners and detainees. While Taxpayer's correctional facilities may provide a certain level of medical care, these services are not part of the primary function of the Residential and Non-Residential Facilities and thus these facilities are not congregate care facilities within the meaning of 856(e)(6)(D)(i).

Ruling 2: The amounts received under Taxpayer's contracts with government tenants for the Residential Facilities (excluding the Financed Facilities) will be treated as "rents from real property" for purposes of section 856(d)(1).

Under Taxpayer's owned and leased Residential Facilities contracts, government tenants pay to use specific real property to house their prisoners, detainees, probationers, and parolees. The contract payments received by Taxpayer are payments for the right to use space within a specific building. Therefore, the contract payments received by Taxpayer will be treated as "rents from real property" under section 856(d). Furthermore, Taxpayer has represented that the aggregate fair market value of the personal property owned by the REIT in the Residential Facilities is less than 15 percent of the aggregate fair market value of all property provided under the contracts. Because less than 15 percent of the contract fees is attributable to personal property under section 856(d)(1)(C), the entire contract fee will be treated as "rents from real property" within the meaning of section 856(d).

The Services provided to government tenants will be provided by a TRS of Taxpayer. The fees for the Services will be included in the rent received by Taxpayer, but Taxpayer will compensate the TRS on an arm's-length basis for providing the Services. All costs associated with providing the Services will be paid by the TRS. Accordingly, income from the Services provided by the TRS to government tenants will be excepted from the definition of impermissible tenant service income, and the amounts received by Taxpayer from government tenants will not be treated as other than rents from real property under section 856(d).

Ruling 3: The payments Taxpayer collects on behalf of its TRSs for the Services the TRSs provide at a Financed Facility² are considered to be rendered by the TRS, rather than the REIT, and do not cause any portion of the payments received by the REIT that otherwise qualify to be disqualified for purposes of the REIT income tests.

Taxpayer represents that it will assign the service components of its Financed Facilities contracts to its TRSs, which will be fully responsible for directly providing the Services in those facilities. Taxpayer will collect the amounts that government tenants pay for the Services in the Financed Facilities on behalf of the TRSs and remit these amounts to the TRSs.

Taxpayer collects the charges for these services on behalf of the TRSs. Therefore, these

arrangements do not cause payments Taxpayer collects on behalf of its TRSs for the Services the TRSs provide at a Financed Facility are considered to be rendered by the TRS, and do not cause any portion of the payments received by the REIT to the extent they otherwise qualify to be disqualified for purposes of the REIT income tests.

CONCLUSION

Based on the facts as represented, we rule that:

- (1) The Residential Facilities and Non-Residential Facilities will not be treated as “health care facilities” in whole or in part under section 856(l)(4)(B);
- (2) The amounts received under Taxpayer’s contracts with government tenants for the Residential Facilities will be treated as “rents from real property” for purposes of section 856(d)(1); and
- (3) The payments Taxpayer collects on behalf of its TRSs for the Services the TRSs provide at a Financed Facility are considered to be rendered by the TRS, rather than the REIT, and do not cause any portion of the payments received by the REIT that otherwise qualify to be disqualified for purposes of the REIT income tests.

Except as specifically ruled upon above, no opinion is expressed concerning any federal income tax consequences relating to the facts herein under any other provision of the Code. Specifically, we do not rule on whether Taxpayer otherwise qualifies as a REIT under part II of subchapter M of Chapter 1 of the Code. We also do not rule on whether a contract for a Financed Facility is treated in part as a loan from Taxpayer to a government tenant with respect to the Financed Facility. Furthermore, we do not rule whether payments received by the REIT on behalf of its TRS at a Financed Facility constitute gross income under section 61. In addition, we do not rule on whether Taxpayer’s TRSs are adequately compensated for the Services.

This ruling is directed only to the taxpayer requesting it. Taxpayer should attach a copy of this ruling to each tax return to which it applies. Section 6110(k)(3) of the Code provides that this ruling 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 representatives.

Sincerely,

Jonathan D. Silver

Assistant Branch Chief, Branch 2

Office of Associate Chief Counsel

(Financial Institutions & Products)

[IRS: Organization's Exemption Jeopardized by Reimbursement Payments.](#)

The IRS ruled that the tax-exempt status of an organization providing environmental cleanup services will be affected by payments the organization makes to a company under a reimbursement agreement and that the reimbursement payments inure to the benefit of the company.

Dear * * *

We have considered your ruling request dated February 11, 2011, on the federal income tax consequences of a proposed agreement between you and Company.

FACTS

You are exempt under § 501(c)(4) of the Internal Revenue Code (“Code”) as an organization that promotes the public welfare by mitigating environmental damage. Your sole member is Parent, a business league that is organized and operated to further the interests of Industry and is exempt under § 501(c)(6).

The relationship between you and members of Parent with respect to your provision of cleanup services, such as Company, is governed by a standard service agreement (SSA). The SSA provides generally that you will provide cleanup services at designated rates, and that a member of Parent, such as Company, will reimburse you for your out-of-pocket expenses and pay a mark-up equal to 10-percent of all third-party service provider charges. The 10-percent markup provision is intended to compensate you for the costs and risks associated with the management and oversight of third-party contractors assisting in the cleanup response.

In this case, Company was responsible for the Incident. You have some of your own equipment, which you keep on call for cleanups. The scale of the Incident, however, was beyond your equipment capacity. Accordingly, and in compliance with the SSA, you hired third party contractors to help with the cleanup. The 10-percent markup resulted in an obligation for Company of approximately x1 dollars.

Company initiated the request for a reconsideration of the 10-percent markup amount because it felt that the size of the Incident and the resulting sizeable 10-percent markup amount produced an unexpected “windfall” to you. After considering the request, you and Company entered into the Agreement on Date and presented it to the board of Parent.

Parent, in the interest of preserving your tax-exempt status, agreed that it was appropriate for you to negotiate the Agreement with Company, but made the receipt of a favorable letter ruling from the Internal Revenue Service (IRS) a condition of Parent’s accepting the Agreement between you and Company.

The Agreement calls for the creation of a fund. You agreed to place in the fund 75 percent of the dollar amount resulting from the 10-percent mark-up assessed with respect to any charges related to the Incident where you invoiced and Company paid a 10-percent markup. Under the Agreement, you are entitled to keep 25 percent of the amounts received from the 10-percent markup paid by Company. The remaining 75 percent placed in the fund may be used by you and Company for specified expenses related to the Incident. Many of the Agreement provisions provide for reimbursement of Company by you from the fund. Once all qualifying expenses are paid from the fund, the remainder, if any, is to be released to you.

Specifically, the Agreement provides, in part, that:

1. Company will be reimbursed from the fund for costs it incurs in auditing third-party contractors who performed work in the cleanup of the Incident. The SSA is silent on who is responsible for paying for such auditing costs, but the standard Contractor Services Agreement (CSA) you use when engaging third-party contractors provides that you have the right to access contractors’ books and records to audit them at your expense.

2. You will be reimbursed from the fund for costs you incur in auditing third-party contractors if Company directs you to do so. As noted above, the CSA provides that you would normally be responsible for paying for such costs. However, under the SSA or CSA, you would audit third-party contractors in your own discretion and Company would not have the power to direct you to audit such contractors.

3. Reimbursements for audit costs in (1) and (2) are capped at x3 percent of the original amount in the fund, approximately x4 dollars.

4. Company will be reimbursed for collections costs in pursuing collections of incorrect billings from third-party contractors. You state that, under the CSA, you would be liable to pay for collections expenses for any overcharges made by contractors discovered through your audits of contractors.

5. You will be reimbursed for collection costs you incur in pursuing collections of incorrect billings from third-party contractors. Under the CSA, you would normally be liable for paying collections expenses.

6. Reimbursements for collection costs in (3) and (4) are capped at the lesser of x5 percent of the amounts collected or x6 percent of the original amount in the fund.

7. Company will be reimbursed for any incorrect billing amounts it identifies but are otherwise not recoverable, in addition to the 10-percent markup on such amounts.

8. Company will be reimbursed for the 10-percent markup on any incorrect billing amounts Company recovers.

9. You will be reimbursed for costs related to certain personal injury claims, to the extent they are not covered by the SSA, payable by insurance, or payable by a third party.

10. You and Company waive the right to challenge the validity of contracts that do not conform to the provisions of the SSA, but were entered in good faith.

Company is represented on the board of Parent by Director, who is employed by Affiliate, an affiliate of Company. You state that Director, while present for, and participating in discussions relating to the original intention underlying the 10-percent markup, the unexpected magnitude of contractor billings on which the 10-percent markup was based in the case of the Incident, and the disproportionate gross revenues produced by the 10-percent markup compared with the extra costs borne by you in connection with managing contractors engaged to assist with the Incident, did not "participate in the final deliberations or decision" by Parent to approve your negotiations with Company. You further state that "the Parent Board's decision was made consistent with the exercise of the remaining board members' fiduciary duties, based solely on the best interests of Parent and its sole grantee, [you]."

You maintain that the reconsideration of the amount that Company owes you under the SSA is consistent with the original intent of the 10-percent markup, which was to cover management and oversight costs of third-party contractors. You state that the actual management and oversight expenses related to the Incident are much lower and are estimated to total approximately x2 dollars. You also state that the exchange under the Agreement between you and Company reflects the "give and take" of negotiations. Further, you state that, had Company not been a member of Parent, you would have been equally receptive to renegotiating the 10-percent markup liability, given the unanticipated size of that liability under the unique facts and circumstances presented by the Incident, and the limitations on liability and other concessions you received from Company under the

Agreement.

To date, you have responded to a total of x7 calls for cleanup services, including the Incident. You have never before discounted any of the rates you charged for cleanup. You state that Company's status as a member of Parent does not affect the reconsideration agreement, and that you would have been willing to make such an agreement as the Agreement for any other organization contracting with you. You also state that you do not intend to modify the existing service agreement with Company or any other entity. You cite the unprecedented size and financial impact of the Incident, which produced a "windfall" for you, as the reasons you were willing to negotiate with Company.

RULINGS REQUESTED

You requested the following ruling:

Payments made to Company pursuant to the Agreement will not adversely affect your tax-exempt status and will not result in inurement or impermissible private benefit directly or indirectly to Company by you.

LAW

Section 501(c)(4) of the Code exempts from federal income tax organizations operated exclusively for the promotion of social welfare, provided that no part of the net earnings of such an organization inures to the benefit of any private shareholder or individual.

Section 1.501(c)(4)-1(a)(2)(i) of the Treasury Regulations ("regulations") provides that an organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community.

Rev. Rul. 69-383, 1969-2 C.B. 113, holds that an agreement for fixed-percentage compensation of a radiologist does not result in inurement when the agreement results from arm's-length negotiation and the radiologist has no control over, or management authority with respect to, the hospital.

Rev. Rul. 79-316, 1979-2 C.B. 228, holds that a nonprofit organization whose purpose is to prevent liquid spills within a city port area and to develop a program for the containment and cleanup of liquid spills that occur is entitled to exemption as a social welfare organization under § 501(c)(4), provided that its services are equally available to members and nonmembers and both members and nonmembers are charged on the same basis for cleanup services rendered.

Contracting Plumbers Cooperative Restoration Corp. v. United States, 488 F.2d 684 (2d Cir. 1973), holds that an organization that repairs damage to city streets in the course of plumbing activities does not promote the common good, although its activities benefit the community, because its services are available only to repair damages caused by members.

Harding Hospital, Inc. v. United States, 505 F.2d 1068 (6th Cir. 1974), holds that "net earnings" is a broader term than net profits according to financial statements. If a particular individual or limited number of individuals reaps commercial benefits from the operation of the instrumentality, though they do not do so by direct acquisition or payment over to them of its earnings, the earnings may nevertheless inure to their benefit.

United Cancer Council, Inc. v. Comm'r., 165 F.3d 1173 (7th Cir. 1999), holds that the inurement prohibition requires an organization not to siphon its earnings to its founder, or the members of its board or their families, or anyone else fairly to be described as an insider, that is, as the equivalent

of an owner or manager. The test is functional. It looks to the reality of control rather than to the insider's place in a formal organizational chart of an organization. The insider could be a mere employee or even a nominal outsider, such as a physician with hospital privileges in a charitable hospital.

The prohibition on inurement denies exempt status to an organization whose founders or controlling members have a personal stake in that organization's receipts. *People of God Community v. Comm'r.*, 75 T.C. 127 (1980).

The term "net earnings" may include refreshments, goods, and services furnished to members of an exempt organization. *Spokane Motorcycle Club v. United States*, 222 F. Supp. 151 (E.D. Wash. 1963).

ANALYSIS

Section 501(c)(4) exempts from federal income tax organizations operated exclusively for the promotion of social welfare. An organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the community. Treas. Reg. § 1.501(c)(4)-2(a)(i).

Revenue Ruling 79-316, 1979-2 C.B. 228, holds that preventing and cleaning up liquid spills that endanger marine life and befoul recreational beaches and shorefront property are activities designed to benefit all inhabitants of the community served by an organization. Furthermore, such an organization is exempt under section 501(c)(4), provided that its services are equally available to members and nonmembers and both members and nonmembers are charged on the same basis for the cleanup services rendered. Similarly, Rev. Rul. 66-221, 1966-2 C.B. 220, holds that an organization engaged in fighting fires and related activities promotes the common good and general welfare of the people of the community as a whole. However, services provided by an organization exclusively, or at a preferential price, to its contributors or members do not promote the common good or general welfare even though they may incidentally benefit a community. See *Contracting Plumbers Cooperative Restoration Corp. v. United States*, 468 F.2d 684 (2d Cir. 1973) (holding that an organization that repaired damage to city streets caused in the course of plumbing activities did not promote the common good, even though its activities benefited the community, because its activities were available only to repair damage caused by its members).

Your historical purpose and operations are consistent with these authorities regarding exemption under § 501(c)(4). However, the Agreement will change the basis upon which members and nonmembers of Parent are charged. You generally have charged members and nonmembers on the same basis. The Agreement, however, changes the basis upon which you charge a particular member, Company, thus providing a member a better price than nonmembers.

Under the Agreement, you will reimburse Company for audit costs for which you would normally be liable under the SSA and CSA. As a result of auditing third-party contractors, Company will be reimbursed for any incorrect billing amounts it identifies, in addition to the associated 10-percent markup for such amounts. Because Company will be reimbursed for audit costs, it is incentivized to audit third-party contractors to identify incorrect billings, and is reimbursed for both the audit costs and incorrect billings. Although Company would normally be reimbursed for incorrect billings and the associated 10-percent markup under the SSA and CSA, the subsidization of Company's auditing is likely to identify more incorrect billings than under the SSA and CSA. This is because, under the SSA and CSA, you are responsible for auditing and have less incentive to audit third parties. Therefore, Company stands to benefit under the Agreement from the subsidized auditing activity. You cite the cap on audit costs as a benefit to you under the Agreement. The cap for reimbursements

for audit costs is capped at x3 percent of the original fund amount. Given that the cap allows for approximately x4 dollars in audit costs, however, the cap is so high that it is not meaningful.

Under the Agreement, you will also reimburse Company for collection costs for which you would normally be liable under the SSA and CSA. Company will be reimbursed for collection costs in recovering incorrect billings and for the 10-percent markup on the amount it recovers. Because Company will be reimbursed for collection costs, it is incentivized to undertake collection activities so that it can be reimbursed for the 10-percent markup on such amounts. Although Company would normally be reimbursed for the recovered incorrect billing amounts under the SSA and CSA, the subsidization of Company's collection activity is likely to cause Company to recover more incorrect billings and be reimbursed for more 10-percent markups on such amounts. This is because, under the SSA and CSA, you are responsible for collections and have less incentive to collect amounts from third parties. You cite the cap on collection costs as a benefit to you under the Agreement. The cap for reimbursements for collection costs is the lesser of x5 percent of amounts collected or x6 percent of the original fund amount. Given that the cap allows for reimbursement of millions of dollars in collection costs, this cap, like the cap on audit costs, is also not particularly meaningful.

As described above, the Agreement reduces the amount Company is required to pay under the SSA and CSA, changing the basis upon which you charge Company, a member of Parent, for your services. You have never reduced the amounts you charge for cleanup services in hundreds of service calls, either for members or nonmembers of Parent. Now, however, you propose to discount the amounts you charge for cleanup services for a member of Parent that is represented on the Board of Parent. Because you will charge a member of Parent (i.e., Company) on a different basis from nonmembers, and at a preferential price, you are not like the organization in Rev. Rul. 79-316, *supra*. Accordingly, upon making such payments pursuant to the Agreement, you may not be operated exclusively for the promotion of social welfare under § 501(c)(4). See Rev. Rul. 79-316, *supra*, and *Contracting Plumbers Cooperative Restoration Corp. v. United States*, 468 F.2d 684 (2d Cir. 1973). As a result, you may jeopardize your exemption under § 501(c)(4).

No part of the net earnings of an organization exempt under § 501(c)(4) may inure to the benefit of any private shareholder or individual. The inurement prohibition requires an organization not to pass its earnings to its founder, or the members of its board or their families, or anyone else fairly to be described as an insider — that is, as the equivalent of an owner or manager. *United Cancer Council, Inc. v. Comm'r.*, 165 F.3d 1173 (7th Cir. 1999). The test is functional: it looks to the reality of control rather than to the insider's place in a formal table of organization. The insider could be a mere employee or even a nominal outsider, such as a physician with hospital privileges in a charitable hospital. Similarly, the prohibition on inurement denies exempt status to an organization whose founders or controlling members have a personal stake in that organization's receipts. *People of God Community v. Comm'r.*, 75 T.C. 127 (1980).

"Net earnings," in the context of the prohibition on inurement, is a broader term than net profits according to financial statements. If a particular individual or limited number of individuals reaps commercial benefits from the operation of an instrumentality, though they do not do so by direct acquisition or payment over to them of its earnings, the earnings may nevertheless inure to their benefit. *Harding Hospital, Inc. v. United States*, 505 F.2d 1068 (6th Cir. 1974). The term "net earnings" may even include refreshments, goods, and services furnished to members of an exempt organization. *Spokane Motorcycle Club v. United States*, 222 F. Supp. 151 (E.D. Wash. 1963).

An agreement for fixed-percentage compensation of a radiologist does not result in inurement when the agreement results from arms-length negotiation and the radiologist has no control over, or management authority with respect to, the hospital. Rev. Rul. 69-383, 1969-2 C.B. 113.

Here, Company can fairly be described as an insider with respect to you. See *United Cancer Council v. Comm'r*, 165 F.3d 1173 (7th Cir. 1999). Company is the equivalent of an owner or manager with respect to you, given that it has a voice in the control of Parent through its representative on Parent's board. Parent is your sole member, its board has control over you and, by virtue of its representation on Parent's board, Company has a voice in controlling you. As a member of Parent that stands to benefit from the Agreement, Company has a personal stake in your receipts. See *People of God Community v. Comm'r*, 75 T.C. 127 (1980).

You state that Company's representative, Director, recused himself from Parent's board meetings during deliberations and voting on the Agreement. He was, however, present for discussions of the Agreement. As described, the transaction appears to be at arm's-length. Nonetheless, you are different from the radiologist in Revenue Ruling 69-383, *supra*, because Company has a degree of control over you by virtue of its representation on the board of Parent, which is the sole and controlling member of you. Company is therefore distinguishable from the radiologist in the revenue ruling and can be described as an insider with respect to you.

You cite the unprecedented size of the Incident as the main reason you were willing to negotiate with Company, but you have never reduced the amount you charge for cleanup services for any member or nonmember of Parent. Neither do you propose to make any changes to the SSA to address the problem of similar clean up situations in the future. The only instance in which you have been willing to reduce the fees you charge is with a member of Parent that is also an insider with respect to you. Because you have not reduced your standard cleanup charges and you state that you do not plan to change the SSA going forward, it appears that Company's status as an insider may have influenced your willingness to negotiate with Company. Regardless of whether Company's status as an insider influenced your willingness to negotiate, the Agreement you have negotiated with Company, in fact, benefits Company by relieving it of amounts it owes you under the SSA in return for illusory benefits in your favor. Also, regardless of whether Company's status as an insider actually influenced your decision to accept the Agreement, the Agreement does, in fact, benefit an insider with respect to you.

Given that Company is an insider with respect to you, the reduction of Company's liability under the SSA, pursuant to the Agreement, effectively reduces the price Company pays for your services. Such a reduction in liability, or in price for services, qualifies as "net earnings" within the meaning of section 501(c)(4). See *Harding Hospital, inc. v. United States*, 505 F.2d 1068 (6th Cir. 1974). The reimbursement of Company for expenses for which it is liable to you under the SSA from the Agreement fund will cause your net earnings to inure to the benefit of Company. As a result of your providing services at a preferential price to Company, you will no longer be operated exclusively for the promotion of social welfare and accordingly, your status under § 501(c)(4) will be adversely affected.

CONCLUSION

Based on the foregoing, we rule as follows:

Payments made to Company pursuant to the Agreement will adversely affect your tax-exempt status under § 501(c)(4) and will result in inurement to Company by you.

This ruling will be made available for public inspection under § 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,

Theodore R. Lieber

Manager, Exempt Organizations

Technical Group 3

[IRS Announces Maximum Values of Employer-Provided Vehicles for 2013.](#)

The IRS has announced (Notice 2013-27, 2013-18 IRB 985) the maximum value of employer-provided vehicles first made available to employees for personal use in 2013 for which the vehicle cents-per-mile valuation rule or the fleet-average valuation rule may be applicable.

In previous years, the IRS has provided by revenue procedure the maximum vehicle values and guidance on their calculation and application. Beginning in 2013 with Notice 2013-27, only the maximum vehicle values as adjusted for inflation will be published annually in a notice, the IRS stated.

Maximum Vehicle Values for 2013 for Use of Vehicle Cents-Per-Mile

and Fleet-Average Valuation Rules

PURPOSE

This notice provides the maximum vehicle values for 2013 that taxpayers need to determine the value of personal use of employer-provided vehicles under the special valuation rules provided under section 1.61-21(d) and (e) of the Income Tax Regulations.

BACKGROUND

If an employer provides an employee with a vehicle that is available to the employee for personal use, the value of the personal use must generally be included in the employee's income and wages. Internal Revenue Code § 61; Regulation section 1.61-21. If the employer meets certain requirements, the employer may elect to determine the value of the personal use using certain special valuation rules, including the vehicle cents-per-mile rule and the fleet-average value rule set forth in Regulation section 1.61-21(d) and (e), respectively. Both the vehicle cents-per-mile rule and the fleet-average value rule provide that those rules may not be used to value personal use of vehicles

that have fair market values exceeding specified maximum vehicle values on the first day the vehicles are made available to employees. These maximum vehicle values are indexed for inflation and must be adjusted annually by referring to the Consumer Price Index. In previous years these maximum vehicle values and guidance on their calculation and application have been provided by Revenue Procedure. For example, the maximum vehicle values for vehicles first placed into service in 2012 were published in Revenue Procedure 2012-13 I.R.B. 2012-3 (January 17, 2012). Guidance on the calculation and application of these maximum vehicle values is set forth in section 1.61-21(d) and (e) of the Regulations and does not change from year-to-year. Accordingly, beginning this year, only the maximum vehicle values as adjusted for inflation will be published annually in a shorter notice.

MAXIMUM VEHICLE VALUES

The maximum value of employer-provided vehicles first made available to employees for personal use in calendar year 2013 for which the vehicle cents-per-mile valuation rule provided under Regulation section 1.61-21(e) may be applicable is \$16,000 for a passenger automobile and \$17,000 for a truck or van.

The maximum value of employer-provided vehicles first made available to employees for personal use in calendar year 2013 for which the fleet-average valuation rule provided under Regulation section 1.61-21(d) may be applicable is \$21,200 for a passenger automobile and \$22,300 for a truck or van.

EFFECTIVE DATE

This notice applies to employer provided passenger automobiles first made available to employees for personal use in calendar year 2013.

Comments Requested on Bond Information Return Form.

The IRS requested comments on Form 8038-B, "Information Return for Build America Bonds and Recovery Zone Economic Development Bonds." Comments are due by June 24.

Direct all written comments to Yvette Lawrence, Internal Revenue Service, room 6129, 1111 Constitution Avenue NW., Washington, DC 20224.

IRS Requests Comments on Low-Income Housing Credit Agency Report.

The IRS asked for public comment on Form 8610, "Annual Low-Income Housing Credit Agencies Report," and its related Schedule A, "Carryover Allocation of Low-Income Housing Credit." Comments are due by June 24.

Direct all written comments to Yvette Lawrence, Internal Revenue Service, Room 6129, 1111 Constitution Avenue NW., Washington, DC 20224.

Comments Sought on Exempt Organization Return.

The IRS asked for public comment on Form 990, "Return of Organization Exempt From Income Tax Under Section 501(c), 527, or 4947(a)(1) of the Internal Revenue Code (except black lung benefit trust or private foundation)," and related schedules. Comments are due by June 25, 2013.

Send comments regarding the burden estimate, or any other aspect of the information collection, including suggestion for reducing the burden, to (1) Office of Information and Regulatory Affairs, Office of Management and Budget, Attention: Desk Officer for Treasury, New Executive Office Building, Room 10235, Washington, DC 20503, or email at OIRA_Submission@OMB.EOP.GOV and (2) Treasury PRA Clearance Officer, 1750 Pennsylvania Ave. NW., Suite 8140, Washington, DC 20220, or email at PRA@treasury.gov.

IRS Requests Comments on Private Activity Bond Election Form.

The IRS asked for public comment on Form 8328, "Carryforward Election of Unused Private Activity Bond Volume Cap." Comments are due by June 24, 2013.

Direct all written comments to Yvette Lawrence, Internal Revenue Service, Room 6129, 1111 Constitution Avenue NW., Washington, DC 20224.

Comments Requested on Guidance on Stripping Transactions for Qualified Tax Credit Bonds.

The IRS requested comments on guidance (Notice 2010-28) on stripping transactions for qualified tax credit bonds under section 54A and on some income tax accounting matters associated with holding and stripping qualified tax credit bonds. Comments are due by June 24, 2013.

Direct all written comments to Yvette Lawrence, Internal Revenue Service, room 6129, 1111 Constitution Avenue NW., Washington, DC 20224.

Place Holder

IRS: Affordable Care Act Provisions: What you need to know!

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In keeping with the IRS mission of providing America's taxpayers with top-quality service by helping you understand and meet your tax responsibilities, we will be conducting a phone forum on April 30, 2013 to discuss key provisions of the Affordable Care Act that are currently in effect. These provisions which impact federal, state, and local government employers include:

- W-2 Reporting: Employer Sponsored Health Coverage; and
- Additional Medicare Tax on High Income Earners

To learn more, we cordially invite you to attend the “ACA Provisions: What you need to know!” Phone Forum. This forum is tailored for federal, state and local government employers, payroll and benefits administrators.

During this 60 minute presentation we will cover:

- What is included in the cost of coverage (i.e. health, dental/vision, FSA benefits); and
- Additional Medicare Tax: application, calculation, and reporting.

We are sorry, but we have reached maximum capacity for the ACA Phone Forum. A recorded version and transcript will be posted on our website after the phone forum. If you want notification of the posting, please e-mail your request to te.ge.fslg.outreach@irs.gov. Please add “ACA Recorded Phone Forum” in the subject line. Thank you.

FASB Proposal Addresses Affordable Housing Project Investments.

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The Financial Accounting Standards Board on April 17 issued proposed guidance that would modify the conditions for allowing the use of an effective yield method to account for investments in affordable housing projects that qualify for the low-income housing tax credit.

The Financial Accounting Standards Board on April 17 issued proposed guidance that would modify the conditions for allowing the use of an effective yield method to account for investments in affordable housing projects that qualify for the low-income housing tax credit (LIHTC).

According to FASB, the proposed accounting standards update, “Investments — Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects (a consensus of the FASB Emerging Issues Task Force),” would amend existing guidance and permit a reporting entity to use the effective yield method of accounting if specific conditions are met.

FASB noted in the proposal that stakeholders had indicated that the effective yield method of accounting provides users of financial statements with a better understanding of the entity’s investment returns from affordable housing projects.

The board added that the proposed guidance would apply to all reporting entities that invest in a qualified affordable housing project “through a limited liability entity that is a flow-through entity for tax purposes.” The board said that current guidance requires some LIHTC investments to be accounted for as an equity method investment or cost method investment in accordance with Accounting Standards Codification Topic 970, “Real Estate — General.”

FASB’s proposal also includes disclosure objectives that should enable users of financial statements to understand the nature of investments in qualified affordable housing projects and the effect those investments and related tax credits have on an entity’s financial statements. The proposal provides some information an entity should consider disclosing in order to meet those objectives, including the amount of affordable housing tax credits recognized during the year and the amount and nature of write-downs during the year that resulted from the “forfeiture or ineligibility of tax credits or

other circumstances.”

FASB said that an effective date will be determined after the Emerging Issues Task Force (EITF) reviews the feedback received on the proposal. The board did confirm that the proposed amendments should be applied retrospectively and that early adoption of the guidance will be permitted.

FASB on March 28 agreed to ratify the EITF’s final consensus to expose the proposed guidance on accounting for investments in affordable housing projects for a 60-day comment period. (Prior coverage .)

FASB will accept written comments on the proposal until June 17.

For the proposal, see:

http://www.fasb.org/cs/ContentServer?c=Document_C&pagename=FASB%2FDocument_C%2FDocumentPage&cid=1176162357127

IRS Publishes Proposed Regs on Reporting Requirements for Bond, Acquisition Premium.

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The IRS has published proposed regulations (REG-154563-12) on the information reporting requirements for bond premium and acquisition premium under section 6049.

The text of simultaneously issued temporary regs (T.D. 9616) serves as the text of the proposed regs. Comments are due by July 17.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-154563-12), room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG-154563-12), Courier’s Desk, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, DC, or sent electronically via the Federal eRulemaking Portal at www.regulations.gov (IRS REG-154563-12).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Pamela Lew, (202) 622-3950; concerning submissions of comments, Oluwafunmilayo (Funmi) Taylor, (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background and Explanation of Provisions

Temporary regulations in the Rules and Regulations section of this issue of the Federal Register amend the Income Tax Regulations (26 CFR part 1) relating to section 6049. The temporary regulations set forth information reporting requirements related to bond premium and acquisition premium. The text of the temporary regulations also serves as the text of these proposed regulations.

Consideration of Administrative Burdens Related to Basis Reporting

A number of commenters have indicated that compliance with basis reporting requirements and the use of basis and other information reported by brokers will require considerable resources and effort on the part of return preparers and information recipients. The Treasury Department and the IRS are continuing to review all aspects of the information reporting process and are exploring ways to reduce the compliance burden for both brokers and for information recipients.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866, as supplemented by Executive Order 13563. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because the regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply.

Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small businesses.

Comments and Request for Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS as prescribed in the preamble under the "Addresses" heading. The Treasury Department and the IRS welcome comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available at www.regulations.gov for public inspection and copying. A public hearing may be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for a public hearing will be published in the Federal Register.

[New Requirements for 501\(c\)\(3\) Hospitals Under the Affordable Care Act.](#)

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The Affordable Care Act (ACA), enacted March 23, 2010, added new requirements that hospital organizations must satisfy in order to be described in section 501(c)(3), as well as new reporting and excise taxes.

Because many of these provisions are effective for tax years beginning after the date of enactment, revision of the core Form 990, the Form 990 Schedule H and instructions has been a priority for the Internal Revenue Service (IRS).

As the IRS develops the new forms and guidance to implement the ACA, the IRS goals will be to:

- Allow hospitals to clearly describe their activities and policies;
- Minimize burden to the extent possible; and
- Capture compliance information as required for adherence with the statute.

New Requirements for Charitable 501(c)(3) Hospitals

Section 501(r), added to the Code by the ACA, imposes new requirements on 501(c)(3) organizations that operate one or more hospital facilities (hospital organizations). Each 501(c)(3) hospital organization is required to meet four general requirements on a facility-by-facility basis:

- Establish written financial assistance and emergency medical care policies;
- Limit amounts charged for emergency or other medically necessary care to individuals eligible for assistance under the hospital's financial assistance policy;
- Make reasonable efforts to determine whether an individual is eligible for assistance under the hospital's financial assistance policy before engaging in extraordinary collection actions against the individual; and
- Conduct a community health needs assessment (CHNA) and adopt an implementation strategy at least once every three years. (These CHNA requirements are effective for tax years beginning after March 23, 2012).

The ACA also added new section 4959, which imposes an excise tax for failure to meet the CHNA requirements, and added reporting requirements under section 6033(b) related to sections 501(r) and 4959.

Schools Describe Impact of Proposed Employer Shared Responsibility Regs.

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Many school administrators, board members, and teachers have commented on proposed health insurance regulations (REG-138006-12) implementing the employer shared responsibility provisions, addressing how the regs would affect their schools, staff, and students.

[Editor's Note: The document at this citation contains a representative sampling of a larger number of comment letters submitted to the IRS on REG-138006-12.]

To Whom It May Concern:

The impact of the RULE being proposed for education concerning the PPACA is going to be very detrimental to our school corporation. The majority of our employees have traditionally worked only nine (9) months out of the year. They work for our school corporation because they like being off work in the summer when their children are off school. This saves families the expense of child care year round. These employees are truly seasonal or part-time and therefore should not be included in the rule that forces school corporations to provide insurance to employees working over 30 hour per week. They should be viewed the same as a person that works at a theme park or pool for the summer.

Funding for school corporations keeps getting reduced every year. As a result of limited funds we will be forced to reduce hours for most of our part-time employees who are already on a limited income. In some instances we will have to hire more part-time employees in order to keep offering the same services to our students. Several of the employees that we will be forced to offer insurance to have the spousal rule, but these employees are better off financially on their spouse's insurance. Some of them have already told us that they will quit if they are offered insurance thus making this rule a financial hardship for the employee and the school corporation.

Please reconsider this interpretation of the act so as to not adversely affect the education of our students. Our primary concern is the best education we can provide for the students in our school corporation. As our expenses continue to increase this becomes increasingly more difficult to accomplish.

Sincerely,

[signed]

Deputy Treasurer

Southeast Dubois County School

Corporation

Ferdinand, IN

* * * * *

March 6, 2013

To Whom It May Concern,

I would like to express my concern over the proposed IRS regulation 138996-12. Since the Patient Protection and Affordable Care Act was enacted three years ago, public schools were told that they were exempt from the rule because a large number of our school employees work only 180 days a year. On January 2, 2013 this assumption changed with a new IRS regulation. The new rule for public schools will force our school (which has only 200 employees) to provide hundreds of thousands of dollars in health insurance for employees. Public schools have been underfunded since 2007 and this comes at a time when schools cannot afford health insurance for part-time employees. We have also been in deficit financing since 2005 and this has placed a huge strain on the schools.

Although cost is an issue, public schools believe we have been singled out by the rule. Our attorney has informed us that businesses do not have to provide health insurance for their workers who work the 180 days a year. This new rule you are proposing requires public schools to provide health insurance for individuals while businesses are exempt.

Our school would appreciate if you would reconsider IRS regulation 138996-12. Thank you for your time on this matter.

Sincerely,

Andy Wandersee

School Board Member

Centerville-Abington Community

School Corporation

Centerville, IN

School Boards Group Comments on Impact of Proposed Employer Shared Responsibility Regs.

Francisco Negrón Jr. of the National School Boards Association has commented on proposed regulations (REG-138006-12) implementing the employer shared responsibility provisions, suggesting that the regs may have an unintended impact on schools, including the treatment of long-term assignments, substitute teachers, coaches, and school board members.

Dear Ms. Bjornstad and Ms. Taylor:

The National School Boards Association (NSBA), representing through our state associations approximately 13,800 school districts nationwide, offers the following comments to the proposed rule, Shared Responsibility for Employers Regarding Health Coverage, REG-138006-12, issued by the Internal Revenue Service (IRS) on January 2, 2013. NSBA appreciates the opportunity to share with the IRS: (1) the perhaps unanticipated impact certain provisions of the proposed rule may have as public school districts across the country wrestle with questions about which service hours of various categories of staff members are to be included in the full-time equivalent employee counts for “large employer” determinations; and (2) the need for clarification in some before the rule becomes final to minimize any adverse impact on the nation’s schools and students’ educational outcomes.

I. Who is an “Employee” for Purposes of “Large Employer” Determinations?

In the proposed rule, the IRS states that an employer determines if it meets the definition of a “large employer” for “Shared Responsibility” purposes by totaling the number of full-time employees working an average of at least 30 hours per week, along with a calculation using a formula adding all the service hours of the employer’s part-time employees to determine the number of full-time equivalent employees (FTEs) to be added to the employer’s total count. It is this second piece of the calculation that causes some concern for public school districts.

The IRS proposed rule specifically addresses teachers and other employees of educational organizations, including public school districts, in terms of the look-back measurement period, breaks in service for summer and winter breaks, a calendar year versus an academic year (typically, a school’s “fiscal” year), breaks in service for certain types of leave, variable-hour and seasonal employees, and calculating average weekly hours for school employees (both hourly and non-hourly) when they typically will not work a full twelve-month period.

Public school districts employ many different types of employees with various work schedules and duties that make it difficult to determine who is an “employee” such that they should be included in the FTE count, and whether such inclusion is appropriate or fair to the school district. Some

extremely small districts that do not employ more than 50 full-time employees may come under the heading of an “applicable large employer” when the hours of the part-time workers are included in the calculation of the number of FTEs as required by the IRS proposed rule. The question then becomes “who is an employee?”

The IRS proposed rule states that it has adopted the “common law standard” position for determining when an individual is an “employee”. The IRS states in its discussion of this matter that

“[u]nder the common law standard, an employment relationship exists when the person for whom the services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished. Under the common law standard, an employment relationship exists if an employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done. In this connection, it is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if the employer has the right to do so.” 78 Fed. Reg. 218, 221 (Jan. 2, 2013).

While offering some guidance, this standard does not resolve whether many different categories of people who perform work for school districts should be counted as an employee for purposes of determining whether a school district is an “applicable large employer,” and, consequently, who must then be offered health insurance. As demonstrated below in the following examples and questions, certain staffing situations exist on a daily,¹ weekly, and monthly basis that make a public school district’s frequent calculation of full-time employees (including the FTEs) and subsequent insurance-related responsibilities, as suggested by the IRS proposed rule, administratively arduous and quite confusing.

A. Short-Term Substitute Teachers (typically individual assignments of three consecutive months or less)

Some individuals (both licensed and unlicensed) seeking temporary work on a substitute basis have their names on lists for multiple school districts simultaneously. This occurs not through any type of employment agency but through the individual’s own selection of districts for which he/she would like to work. Such substitute work could be for teachers, teaching assistants, bus drivers, cafeteria workers, custodians, etc. For these individuals, school district employers do not have a reasonable expectation at each individual’s start date that any one individual will perform an average of 30 hours/week of substitute employee services. Moreover, any one of these individuals may perform substitute services for more than one district in any number of counties or education service agency configurations in any given week or month.

Thus, under the IRS proposed rule, one individual could be an “employee” of more than one employer simultaneously. This situation calls into question the applicability of the discussion in the IRS proposed rule about “Employees Rehired After Termination of Employment or Resuming Service After Other Absence,” 78 Fed. Reg. at 228. It is uncommon, though not completely impossible, for substitutes to go for long periods of not performing substitute services for any one particular district for several months at a time, all completely unrelated to being “terminated” or on some “other absence”. Thus, substitutes are not being rehired for each assignment, nor are they “returning” to service for a substitute assignment, nor experiencing a “break in service” since the school district may still be “open” and operational when they are called in to cover a substitute assignment. And applying “averaging methods” would be inappropriate, since substitutes are not guaranteed any minimum hours of service on any given day, or in any given week or month during the school year. Notwithstanding, issues arise with one individual subbing for more than one school district in any given school year, and what obligations each school district may have regarding each substitute’s

hours of service.

For example, over the course of one week, Steve Q is a full-day substitute (roughly 7 hours) to cover the Chemistry classes at School District A's high school on Monday. Mr. Q then does a half-day 4th grade substitute assignment (roughly 3.5 hours) at School District B's elementary school on Wednesday. And on Thursday, Mr. Q does a full-day assignment (again, roughly 7 hours) at a School District C middle school to cover 8th grade classes. Mr. Q does not provide any additional substitute services for any other school districts on Tuesday and Friday of that week. Given that schedule for that week, Mr. Q typically would not be performing, nor expected to perform, an average of 30 hours/week for a single employer over the course of a calendar/fiscal year or other measurement period. Under the IRS proposed rule, Mr. Q. would not meet the definition of a "full-time employee", but that of a variable-hour employee, at last.

However, the same IRS proposed rule seems to suggest that Mr. Q's "part-time" hours for each substitute assignment that week would have to be included in the calculation of FTE hours for each respective school district for which the service hours were performed in the "large employer" determination. Thus, on paper, the IRS proposed rule appears to deem Mr. Q as an "employee" of all three school districts for purposes of determining whether each school district is a "large employer." Yet, for some extremely small districts [less than 50 full-time employees (including FTEs)], the inclusion of Mr. Q's "part-time" hours in the FTE hours calculation might have the effect of pushing one or more of these three small districts into the category of an "applicable large employer", which would then be required to offer health insurance coverage to its full-time employees. Similar to long-term substitute teachers as discussed below, it seems unfair that the federal government would allow one individual to have this kind of effect on multiple school districts in any one given year.

NSBA posits that this dilemma would not change if, for example, over the course of an entire school year, Mr. Q completed 65 total hours of substitute assignments for School District A, 36 total hours for School District B, and 47 total hours for School District C. Again, over the course of each week and over the course of the school year (i.e., measurement period), none of these three school districts expects Mr. Q to work an average of 30 hours/week at the start of any of his substitute teacher positions. All the while, the full-time employees who are absent, necessitating the reason for Mr. Q's substitute personnel employment, are also being counted as full-time employees for "large employer" determination purposes, and are still being paid despite their absence. Thus, it would seem that requiring Mr. Q's substitute hours be included in the FTE calculation for "large employer" purposes results in some "double counting" of employees, in a manner unfair to each school district using Mr. Q's substitute services in any given week or month.

To remedy this wrinkle and not place "small-employer" school districts in such an unfair position, NSBA recommends that the IRS revise the Shared Employer proposed rule to permit "small-employer" school districts to exclude the hours of service of short-term substitutes (although otherwise characterized as variable-hour employees) from the calculation of FTEs for purposes of determining if a school district is an "applicable large employer".

B. Long-Term Substitute Teachers (typically individual assignments of more than three consecutive months)

The IRS proposed rule also discusses the treatment of new, variable-employees who, based on the circumstances at the start date, are expected to work an average of at least 30 hours/week, but for a period of limited duration not to last the entire measurement period. Specifically, the IRS proposed rule states that:

"[a] new employee who is expected to be employed initially at least 30 hours per week may be a

variable hour employee if, based on the facts and circumstances at the start date, the period of employment at more than 30 hours per week is reasonably expected to be of limited duration and it cannot be determined that the employee is reasonably expected to be employed on average at least 30 hours per week over the initial measurement period.” 78 Fed. Reg. at 227.

This proposed rule seems reasonable in the case of a long-term substitute placed on a school assignment that is expected to last longer than three months. Though the same concerns arise regarding “double counting”, as mentioned in the Short-Term Substitute section above.

However, the discussion in the IRS proposed rule further states that:

“Effective as of January 1, 2015,. . . , the employer will be required to assume for this purpose that although the employee’s hours of service might be expected to vary, the employee will continue to be employed by the employer for the entire initial measurement period; accordingly, the employer will not be permitted to take into account the likelihood that the employee’s employment will terminate before the end of the initial measurement period.” 78 Fed. Reg. at 227 (emphasis added),

This language is both problematic and unfair for school districts, as it has the potential to result in school districts not hiring individuals for long-term substitute assignments, and instead breaking up the assignment into a series of assignments of a short-term duration, bringing in different people for each segment, resulting in a lack of continuity in teaching methodologies for students and even the assignment of less qualified teaching staff which could ultimately affect students’ educational outcomes. The next example will demonstrate how long-term substitute assignments work in actual practice:

In School District A, a physical education teacher goes on medical leave in mid-January for the rest of the school year (a total of approximately five months) due to a back injury. The P.E. teacher intends to return to the classroom at full-duty status at the beginning of the following school year. School District A brings on Miss T as a long-term substitute teacher to cover the P.E. teacher’s classes during his absence. For purposes of this example, assume this is Miss T’s first substitute assignment for School District A, i.e., she is a new variable hour employee.

At the start of her long-term substitute assignment, the school district and Miss T are fully aware that this is a finite term of service for Miss T while she covers the P.E. classes. Miss T works a full-time schedule during the course of her long-term assignment, just as the original P.E. teacher would have, but for the injury. Additionally, the policies and regulations of School District A contain provisions that specifically state that substitutes and “temporary teachers”, such as Miss T, are not entitled to benefits of any kind from the school district during the course of their assignments. Also, there is no guarantee that Miss T will have any future substitute assignments, short- or long-term, at the conclusion of this particular long-term P.E. class assignment.

Is Miss T an “employee” of School District A for “large employer” determinations under the IRS proposed rule? It is true that at the start date of Miss T’s long-term substitute assignment, she is expected to work an average of at least 30 hours per week during the approximately 5-month period of service. However, once this current assignment is over, School District A will have no basis to reasonably expect that Miss T will work those same hours during the remainder of the measurement period. Thus, Miss T will not experience a “break in service” at the end of the school year, as discussed in the IRS proposed rule. So, would Miss T be considered a part-time employee, even though she worked full-time hours during those 5 months, such that her hours of service should be counted in the FTE hours calculation?

Additionally, school districts would likely find the “Effective as of January 1, 2015, . . . required to

assume . . . will continue to be employed” language problematic in this and similar situations. Specifically, if School District A is a small district, i.e., unlikely to meet — but is close to — the 50-full-time employee threshold, and including Miss T as a “full-time employee” or including her hours of service as a variable-hour employee for FTE hours calculation purposes would push School District A over the 50-full-time employee (plus FTEs) threshold, it seems unfair to now allow a one-time incident (having a long-term substitute) to result in School District A having the responsibilities of a “large employer” for the following school year or applicable stability period, even if School District A is fully aware that Miss T’s period of work has long since ended.

Also, it is not uncommon for individuals who are on multiple school districts’ substitute lists to have worked primarily for some portion of a school year in one school district, but ultimately be hired on as a full-time employee in another neighboring (or even out-of-state) school district mid-school-year, as vacancies occur throughout the school year. Thus, it is unclear what the purpose is of the “Effective as of January 1, 2015” language requiring school districts to assume these types of variable hour employees “will continue to be employed” by those districts for the remainder of the initial measurement period. Thus, NSBA would recommend the IRS final rule regarding Shared Employer Responsibilities exclude such variable hour employees, i.e., short- and long-term substitutes and temporary teachers of any kind, from this proposed “required assumption”.

C. Independent Contractors

The IRS proposed rule does not address independent contractors, and it is not clear under what circumstances, if any, a school district may need to include an independent contractor either as a full-time employee or as an FTE in the total employee count for purposes of “large employer” determinations and for the “assessable payment” (i.e., penalty) provisions contained in the IRS proposed rule. The IRS states in this proposed rule that it plans to follow the “common law standard” for determining who is an employee for consideration of shared employer responsibilities. As such, it is unclear if the IRS intends for such employment arrangements to be considered as establishing an employment relationship and thus an independent contractor could come under the definition of an “employee”. Since the “common law standard” explained by the IRS in this proposed rule looks at the nature of the work itself being done, and the authority of the employer to direct, supervise, and manage such work, it is worth looking at a few examples of typical independent contractors a school district might engage, and into some of the elements of the employment contracts being entered into.

An independent contractor who performs work for a school district usually does so for a finite period of time. For some independent contractors, the period of work may run longer than three months;² for others, it may run shorter. For example, an independent contractor might be a construction company hired to build a new school over the course of a school year. Another might be a private law firm hired under an annually negotiated contract to provide representation to a school board of a public school district in all special education matters before administrative tribunals, and state and federal agencies and courts. Yet another may be a trainer who will provide one week of professional development for a school district’s building principals on new employee evaluation procedures. And still another may be a private auditor who will be conducting an internal investigation of a school district’s finance department, the audit and final reporting of which is expected to last the duration of one school year or nine months.

Ordinarily, the types of independent contractors suggested above are either self-employed or are wholly separate business entities outside the school district, with these entities administering and managing the health insurance plans of the individuals who will be performing the contracted work for the school district. Another possibility is that, for example, the trainer and/or the auditor, if solo practitioners, might have their own individual health insurance policies or be included in their

spouses' policies.

The specifically identified terms of a contract for the services of an independent contractor are usually negotiated between the school board and the independent contractor, and typically are governed by state law. Such contract terms may include the rate of compensation; the scope of work; the expected duration of the contract; what outcomes and forms of work product are expected and by when; the methods and levels of access, if needed, to school property, student/staff records, and district staff both at school sites and at the Central Administration Office; areas of liability in the event of injury or work stoppages; where the independent contractor(s) would be physically performing their work under the contract; the levels of confidentiality in any information gained by the independent contractor in the course of the work; and most importantly, the degree to which the work under the contract can be directed, supervised, and/or controlled by school district employees.

Also, these independent contractor services contracts may, and typically do, contain provisions, negotiated in good faith, that for the life of the contract, the independent contractor(s) performing the work is not considered an "employee" of the school district, and is not eligible for any health or other benefits typically made available to school district employees. This last provision about the lack of eligibility for health or other district benefits is also sometimes contained in school district policies and regulations, similar to short- and long-term substitutes and "temporary" teachers.

While the construction company, the private law firm, and the trainer would seem to provide the easiest examples of individuals working as independent contractors who would not consider themselves to be "employees" of the school district for purposes of this IRS proposed rule, nor likely would the school district, a more definitive statement to this effect from the IRS would be helpful to ensure that all entities are of the same mind with regard to the application of this proposed rule.

The example of the auditor, however, is not as clear. For the sake of argument, assume that while performing her contract, the auditor is given office space at the central administration building, a phone, a school district email address, unlimited access to office supplies and equipment, and is even given a badge to be able to move freely from school to school, and through the various departments. The auditor also has unfettered access to district staff during the internal investigation, and provides regular reports, both verbally and in writing to the superintendent and department of risk management. To some degree, the Superintendent, both directly and through his senior staff, is able to direct the work of the auditor during the course of the contract, but cannot impede the investigation, nor affect the findings and recommendations of the auditor. And during the life of her contract, the auditor averages to work consistently at least 40 hours per week.

Under the IRS proposed rule, would this auditor be considered an "employee" during the life of the contract under the "common law standard" used by the IRS, such that the auditor's hours of service pursuant to the contract must be included in the school district's calculation for determining "large employer" status? If so, would this still be the case even though the contract specifically states that the auditor is not an employee of the district during the life of the contract? In essence, can/does the IRS proposed rule trump whatever language is in the contract that was negotiated in good faith between the school board and the auditor?

Similarly, assuming the IRS would deem the auditor to be an "employee" of the school district, despite the negotiated terms of the employment contract, since the auditor consistently worked at least 40 hours per week for the life of the contract, should the school district have offered the auditor health insurance coverage at the end of the auditor's third completed month of work? If so, would this still be the case even though the contract specifically contains a negotiated provision, which is also consistent with the district's policies and regulations, that the auditor would not be eligible for the district's benefits?

Under this proposed rule, if the IRS should deem the auditor to be an “employee” such that the school district should have offered the auditor health insurance coverage after the end of month three, it seems that the IRS proposed rule is encroaching on a school board’s rights with regard to crafting contract language in such transactions. Additional information would be helpful about whether school boards can continue to include language in those negotiated, good faith contracts as to the independent contractor’s eligibility for district benefits, including health insurance, and for “employee” status.

D. Individuals Performing Extracurricular or Additional Duties

In addition to staff members that help a school district run day-to-day, there are individuals who perform extracurricular or additional duties for after-school activities for which they receive additional pay above their existing annual school district salary, or a separate stipend whether they are a current school district employee or a private citizen. Such individuals (“coaches”) may be athletic coaches, student mentors, leaders of student clubs such as drama or debate, cheerleading, foreign language clubs, music clubs, etc. As school districts of all sizes begin analyzing how the IRS proposed rule is to be implemented, questions have arisen as to how coaches are to be accounted for, both for “large employer” determinations and for determining who must be offered health insurance coverage to avoid the “assessment payments” (the penalty provisions in this proposed rule).

1. Are Coaches “Seasonal Workers” to be Included/Excluded in the FTE Count?

Under the IRS proposed rule, “if an employer’s workforce exceeds 50 full-time employees for 120 days or fewer during a calendar year, and the employees in excess of 50 who were employed during that period of no more than 120 days were seasonal workers, the employer is not an applicable large employer.” 78 Fed. Reg. at 222 (the “seasonal worker exception”). The discussion in the proposed rule also states that “an employee would not necessarily be precluded from being treated as a seasonal worker merely because the employee works, for example, on a seasonal basis for five consecutive months.” Id. Lastly, but most importantly, the discussion in the proposed rule related to the look-back measurement method specifically states that “[i]t is not a reasonable good faith interpretation of the term seasonal employee to treat an employee of an educational organization, who works during the active portions of the academic year, as a seasonal employee.” 78 Fed. Reg. at 227. This issue is very relevant and significant for extremely small school districts, and for certain individuals in large districts, given the timing and amount of work performed by coaches. To assist the IRS in its analysis of these comments related to coaches, we provide a brief description of how coaching services operate at the school site.

After-school athletic teams and certain other extracurricular activities usually run for a defined period of time during the school year: (Depending on the school calendar,) Fall sports typically run from August to October; Winter sports — February to late March; Spring sports — April to late May. These “seasons” are usually defined by each state’s athletic associations. Coaches for these activities typically provide their “coaching” services for two to four hours a day, up to all five school days each week during the particular activity’s “season”. This does not include any outside “planning” that a coach may engage in to prepare for each practice and/or competitive event. Also, coaches generally do not perform coaching services on a full-time basis in public school districts. These services are provided outside of the regular school day.

In reviewing the proposed rule and its application to coaches, school districts need clarification from the IRS on the following situations:

a. Given the above factual descriptions about how coaching activities operate in practice, can each

coach be considered a “seasonal worker”, allowing a school district to exclude their coaching hours of service from the calculation for a “large employer” determination?

b. Under the “seasonal worker exception”, given that a coach typically performs coaching services for roughly 2-4 hours per day, does that 2-4 hour time period each afternoon constitute a “day” toward the 120-day limit in the proposed rule?

c. If an individual performs coaching services for a separate sport in each of the three seasons, again not at full-time status, is that individual’s coaching hours to be included in the FTE count because the 4-month time period has been exceeded? What if even though the four-month period has been exceeded, but the 120-day period has not?

d. When an existing full-time school division employee is also a coach in a given school year, irrespective of for how many seasons that year, and that employee is already included in the full-time employee count for “large employer” determinations due to the employee’s non-coaching full-time job, does the school district also have to include that employee’s coaching hours of service in the FTE count too? Or can the school district exclude the coaching hours of service to avoid “double-counting” that employee? It does not seem fair or reasonable for a small school district that has already included the employee in the count for the full-time work, to then be pushed over the edge into “large employer” status because that same employee is also a coach.

e. When a person performing coaching duties, irrespective of the number of seasons each school year, is NOT otherwise employed by the school district in any capacity but is paid a small stipend for the coaching services provided, is that coach an “employee” under the common law standard to be used by the IRS? Even if, for example, that coach has a separate job wholly unrelated to the school district? And if so, is the school district required to include that coach’s service hours in the FTE count for “large employer” determinations? Would the outcome change if the non-district-employee coach is also a parent of one of the student-athletes on the team?

E. School Board Members

In some local jurisdictions throughout the country, school board members are paid a small salary or per diem for the work they perform on the school board. However, typically, school board members also have jobs elsewhere during the day that are their primary source of income, or they are simply retired workers who are serving on the school board. Questions that affected school districts have are:

1. Under the IRS proposed rule, are those school board members receiving salaries considered “employees” of the school division, given that the school board itself is the governing body of a school district, and is not directed, managed, or supervised by any school district staff, as referenced by the “common law standard”?

2. Since the work involved in being a school board member does not constitute a full-time job, is the school district required to include in the FTE count for “large employer” determinations the hours of service worked by each member in serving on the school board?

F. Re-hired Retired Employees

Many school districts have re-hired employees who have retired from the district or another school district. Such re-hired, retired employees often receive health insurance as part of their retirement package. The IRS proposed rule does not appear to provide school districts with the flexibility to NOT offer health insurance to these rehired retirees who are already receiving health insurance

otherwise. It would be beneficial for school districts if the IRS created an exemption or waiver to give school districts the flexibility to accommodate these re-hired retirees.

II. Issues in the IRS Proposed Rule for Which Public School Districts Seek Clarification

In addition to the individual inquiries of clarification raised in Part I, there are certain broader provisions of the IRS proposed rule for which school districts need assistance from the IRS.

As discussed in the IRS proposed rule, a large employer may be “liable for an assessable payment” (i.e., “penalty”), if (a) for any month, any full-time employee is certified to receive an applicable premium tax credit or cost-sharing reduction because the employer did not offer to at least 95% of “its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage (MEC) under an eligible employer-sponsored plan; or (b) if an employer does not offer an MEC to its full-time employees (and their dependents) under an eligible employer-sponsored plan for which the employer covers at least 60% of the costs of the coverage to the employee, or the MEC costs to the employee for self-only coverage is not affordable to the employee.

A. Section 4980H(a) — Employer Offers MEC to at Least 95%

In those states that have collective bargaining for school district employees (not all of them do), some school districts have more than one, and perhaps even several bargaining units within the district. For example, a school district could have a bargaining unit for its teachers, a bargaining unit for its custodians, a bargaining unit for its bus mechanics, a bargaining unit for its bus drivers, a bargaining unit for the cafeteria workers, etc. And each bargaining unit has its own collective bargaining agreement (CBA) that is negotiated and entered into wholly separate and apart from all the other CBAs. As the health insurance exchanges are coming online in various states, individual school districts are beginning to face an unexpected dilemma, one that was likely unanticipated by the IRS in drafting this proposed rule.

Assume the following facts (which are similar to those some school districts are actually experiencing right now):

School District XYZ has 1,000 full-time employees. The district has been involved in negotiations of the CBAs for some of the district’s bargaining units for the past few months. The district’s CBA negotiators are preparing to enter negotiations with the bargaining unit for custodians. The custodians’ bargaining unit makes up 10% of the district’s full-time employees. As the negotiation period draws near, the custodians’ bargaining unit has informed the district that it has been reviewing the health insurance plans becoming available through the state’s exchange. As a result, the bargaining unit has decided that it does not want to be offered MEC by the district, and wants the forthcoming CBA to reflect that. The district has notified the bargaining unit that it will not do that, because if that language (not offering MEC) was included in the CBA, the district would be put under the 95% threshold stated in Section 4980H(a), subjecting it to the \$2,000 per person penalty in that provision for the other 90% of full-time employees (minus the first 30).

In response, the custodians’ collective bargaining unit warns the district that if it does not include such language in the CBA, the bargaining unit will bring the district before the state’s labor commissioner, who may rule in favor of the bargaining unit and order the district to draft a CBA that specifically does NOT include any provision about offering MEC to the bargaining unit.

Thus, the district will be placed in the untenable situation of either violating the labor commissioner’s order and including the MEC offer language in the CBA to meet the 95% threshold, or complying with the commissioner’s order and excluding the language in the CBA, but then falling

under the 95% threshold and being subjected to an astronomical penalty for each year the custodians' CBA is in effect.

Given that this is surely NOT what the Affordable Care Act intended, how does the school district handle this situation? NSBA recommends creating an exemption or waiver of some sort from this penalty provision when a district is forced NOT to offer MEC to at least 95% of its full-time employees through no fault of its own. Also, districts question whether the penalty under Section 4980H(a) should be the same whether the employer offered MEC to 94% of its full-time employees, or 0% of its full-time employees? Clarification is needed to assist school districts as they navigate through the implementation of the IRS proposed rule.

B. Administrative Burdens for "Long-Term" Assignments

Separate and apart from the aforementioned issues regarding long-term substitutes, the IRS proposed rule requested comments on whether any special rules would be appropriate with respect to "short-term employees" (which the IRS seems to define as those employed for three months or less, 78 Fed. Reg. at 229), with regard to the application of the Section 4980H "assessable payments" (i.e., penalties) provisions. In that discussion, the IRS stated that "section 4980H issues may arise for short-term employment exceeding three months." 78 Fed. Reg. at 229. In school district parlance, "short-term employment" assignments typically exceed three months, thus bearing the moniker of "long-term" assignments, but they may not typically last a full school year. The dilemma school districts face is that, under the IRS proposed rule, if an individual takes on a temporary assignment of longer than three months, but not for a full school year, the individual might become an "employee" during the assignment, and the school division would be required to at least offer health insurance coverage to that temporary employee by the completion of the third month of service.

The administrative burden of offering health insurance coverage by the end of the third continuous month of service to such a temporary employee, knowing that the particular employee is only going to be employed for a 4-month or 6-month or whatever non-permanent period of time is an unreasonable one for the IRS to place on public school districts, given their extremely limited, and ever-decreasing funding resources. The administrative costs and burdens of insuring such an employee for such a limited duration cannot possibly be what the Affordable Care Act intended for public school districts to endure, at the ultimate cost of drawing funding streams away from classrooms and the education of this nation's students and future leaders. NSBA recommends that the proposed rule be revised to incorporate language that removes the requirement that a school district must offer a long-term (more than three months) non-permanent employee MEC after the end of the third month.

NSBA thanks the IRS for its review and consideration of the issues specific to school districts raised as a result of the IRS proposed rule regarding Shared Employer Responsibilities. NSBA and its members look forward to the IRS' response to, and resolution of, these comments, and urge the IRS to do so in a way that minimizes the potential adverse impact on school districts, and the educational services they provide to our nation's students.

Sincerely,

Francisco M. Negrón, Jr.

General Counsel

IRS Releases Report on Avoiding Troubled Tax-Advantaged Bonds.

The Internal Revenue Service office of Tax Exempt Bonds (TEB) released the report, Avoiding Troubled Tax-Advantaged Bonds. This report produced by the TEB Compliance Practice Research Team seeks to provide aid to issuers of tax-advantaged bonds municipal bonds. It identifies some considerations for issuers of such bonds and is TEB's initial step toward producing public resource products that assist issuers in avoiding troubled transactions. For more than a decade, TEB observed some of the worst problems in the municipal industry and then witnessed the efforts taken (by leaders in state and local government, the professional communities that support them, and various regulatory bodies) to address them. Many of these complex compliance issues facing issuers of tax-advantaged municipal debt still exist.

Publishing Avoiding Troubled Tax-Advantaged Bonds is a part of TEB's continuing effort to provide practical steps and products that may be helpful to issuers of tax-advantaged municipal bonds. As such, we welcome comments and feedback from the tax-advantaged municipal bond community that provide further tools and clarification for issuers. Please submit your comments and feedback to TaxExemptBondQuestions@irs.gov inserting "Avoiding Troubled Tax-Advantaged Bonds Question" on the Subject: line.

The report covers three phases of the life cycle of bonds, each with various considerations, of which an issuer should be aware. These three identified phases are: 1) the transaction development phase; 2) the transaction execution phase; and 3) the post-issuance phase.

Watch for the TEB presentation of phase one "Transaction Development," in an upcoming Webinar scheduled for this fall.

TEB hopes that the tax-exempt bond community will use this information to create related products beneficial to their members. These products will provide additional tools that facilitate issuer adoption of practices and procedures that avoid abusive or questionable transactions.

The full report is available at:

<http://www.irs.gov/pub/irs-tege/Avoiding%20Troubled%20Tax%20Advantaged%20Bonds.pdf>

New Voluntary Closing Agreement Program Request Form.

The Internal Revenue Service released the new Form 14429, Tax Exempt Bonds Voluntary Closing Agreement Program Request. Completion, in full, of the new form is a requirement before the submission to the Tax Exempt Bonds Voluntary Closing Agreement Program (TEB VCAP) is accepted. The purpose of the new form is to assist issuers in organizing TEB VCAP submission requests and to ensure that their submissions are complete, in accordance with the requirements under Notice 2008-31, 2008-11 I.R.B. 592 and IRM 7.2.3. Use of the new form should avoid delays in processing a request because of missing information as well as facilitating the process for accepting

and assigning requests.

The Tax Exempt Bonds (TEB) function, within the Tax Exempt & Government Entities Division, administers TEB VCAP. Generally, TEB VCAP provides remedies for issuers of tax-advantaged bonds (tax-exempt bonds, tax credit bonds, and direct pay bonds) who voluntarily come forward to resolve a violation of the federal tax requirements applicable to a bond issue that the issuer cannot self-correct under programs described in the Income Tax Regulations (Regulations) or other published guidance. An issuer will generally receive a more favorable treatment in resolving its tax violation under TEB VCAP than it would for the same tax violation discovered during an IRS examination of their bonds. As such, TEB VCAP encourages issuers, and other parties involved in tax-advantaged bond transactions, to exercise due diligence in complying with the applicable federal tax laws. TEB VCAP also provides a vehicle to correct violations as expeditiously as possible before discovery of the violations during an IRS examination.

The improvement of the TEB VCAP program, through procedural enhancements, is a TEB commitment. The new Form 14429 is an example of the latest effort by TEB to improve the administration of the TEB VCAP program and further this commitment. Last year, TEB provided web content to provide more information about the TEB VCAP program as well as descriptions (provided in IRM 7.2.3.4) of the resolution standards for identified violations both for tax-exempt and certain direct pay bonds. TEB believes that these resolution standards encourage due diligence by providing certainty, to issuers and other parties, in understanding the methodologies available to resolve eligible violations.

The new Form 14429 is available at:

<http://www.irs.gov/pub/irs-pdf/f14429.pdf>

Private Letter Ruling: IRS Provides Information on Changes to Exempt Organization's Activities.

The IRS provided general information about the procedures for an exempt organization to declare any changes in the character, operations, or purpose for which it was originally created.

Dear * * *:

This letter provides general information in response to your letter dated August 17, 2012, regarding follow up submissions to the Determinations office concerning change of a tax-exempt organization's activities.

Procedures for submitting an exempt organization's structural and operational changes to the Service can be found in Publication 4221-PC, Compliance Guide for 501(c)(3) Public Charities, Publication 4221-PF, Compliance Guide for 501(c)(3) Private Foundations and Publication 4221-N, Compliance Guide for Tax Exempt Organizations (Other than 501(c)(3) Public Charities and Private Foundations). The appropriate publication is provided with all current exemption letters. These guides provide that any changes should be reported on the organization's annual information return. It also provides that an organization may submit changes to the EO Determinations office, but that such submissions do not absolve the organization from reporting such changes on its annual return.

Additionally, section 1.6033-2(i)(1) of the regulations provide that exempt organizations that are not required to file an information return must notify the IRS in writing of any changes in its character,

operations, or purpose for which it was originally created.

Revenue Procedure 2012-4, 2012-1 IRB 125, § 7.04(2) provides that the IRS will not issue determination letters approving or disapproving any completed transaction, or determination letters on the effect of changes in activities on tax-exempt status (except for areas enumerated in the revenue procedure). This revenue procedure, updated annually, has contained this provision since 2007.

In order to receive the protection from retroactive revocation of a ruling or determination letter found in Rev. Proc. 2012-4, §§ 13 and 14, that could result from an organization's change in activities, an organization must follow the procedures found in that revenue procedure for requesting a private letter ruling. These procedures include the payment of the \$10,000 fee. These are the only procedures that provide any protection from retroactive revocation upon structural or operational changes. Reporting a change on Form 990, Form 990-EZ, or Form 990-PF will not prevent the retroactive revocation of a ruling or determination letter.

This letter is for informational purposes only and provides general statements of well-defined law. It is not a ruling. (Rev. Proc. 2012-4, 2012-1 I.R.B. 125). We will make this letter available for public inspection after deleting names, addresses and other identifying information, as appropriate, under the Freedom of Information Act (Announcement 2000-2, 2000-2 I.R.B. 295). A copy of this letter with the proposed deletions is attached.

I hope this information is helpful. If you have any questions, please contact me at *** or *** at ** *.

Sincerely,

[signature omitted]

Manager, Exempt Organizations

Guidance

[Private Letter Ruling: IRS Summarizes Purpose of Exempt Entities Code.](#)

The IRS explained that the National Taxonomy of Exempt Entities code assigned to an exempt organization to characterize the organization in terms of its primary exempt activity is not relevant to any determination under the internal revenue laws or to tax-exempt status.

Release Date: 3/29/2013

Date: January 14, 2013

Dear ** *:

This letter responds to your letter dated July 31, 2012, requesting that we change the National Taxonomy of Exempt Entities (NTEE) Code of ORGANIZATION. You stated that your current activity code, as shown on the Exempt Organizations Business Master File (EOBMF), does not reflect the activities of your organization.

The National Taxonomy of Exempt Entities (NTEE) Code is a three or four-character code that

attempts to characterize the organization in terms of its primary exempt activity. The IRS began issuing new exempt organizations an NTEE code as part of the determination process in 1995. The determination specialist assigns an NTEE code to each organization exempt under I.R.C. § 501(a) as part of the process of closing a case when the organization is recognized as tax-exempt. The many variables involved in applying the codes, including the fact that organizations often have numerous activities, can provide challenges when attempting to precisely capture an organization's primary exempt activity.

Prior to 1995, the exemption application provided space for the taxpayer to identify three activity codes. EOBMF may contain an activity code for these organizations rather than an NTEE code. These activity codes do not coincide with the newer NTEE codes.

The NTEE code is not relevant to any determination under the internal revenue laws or to tax-exempt status. Accordingly, no procedures are currently in place by which an organization can request a change to their self-identified activity codes, or an NTEE code, or to request the issuance of a NTEE code when one was not previously issued.

In addition, there is no formal guidance issued by the IRS that either permits or requires any person, or organization, to rely on NTEE codes for any purpose under the internal revenue laws. An organization's application for tax-exempt status and Forms 990 are required to describe in sufficient detail the organization's exempt purpose and activities.

This letter is for informational purposes only and provides general statements of well-defined law. It is not a ruling and taxpayers cannot rely on it as such. (Rev. Proc. 2011-1, 2011-1 I.R.B. 1; Rev. Proc. 2011-4, 2011-1 I.R.B. 123). We will make this letter available for public inspection after deleting names, addresses and other identifying information, as appropriate, under the Freedom of Information Act (Announcement 2000-2, 2000-2 I.R.B. 295). A copy of this letter with the proposed deletions is attached.

I hope this information is helpful. If you have any questions, please contact me at *** or *** at ** *.

Sincerely,

[signature omitted]

Manager, Exempt Organizations

Guidance

Enclosure

[Private Letter Ruling: IRS Rules on Liquidation of Subsidiary Into Country Club.](#)

The IRS ruled that a country club's tax-exempt status will not be affected when its subsidiary is liquidated into the club because there will be no recognition of gain or loss when the club receives the subsidiary's assets and liabilities.

Release Date: 4/12/2013

Date: January 16, 2013

This is in response to your ruling request, dated October 21, 2009, requesting certain rulings with respect to the income tax consequences to you of the complete liquidation and dissolution of your wholly owned subsidiary that is tax exempt under § 501(c)(2) of the Internal Revenue Code ("Code").

FACTS

You are a State nonprofit membership corporation organized in 1982 and recognized in 1984 as tax-exempt under § 501(c)(7) to operate as a country club. State statutes prohibited stock ownership of not-for-profit entities. Therefore in order to provide a mechanism for members to recoup all or part of their investment in the country club assets upon withdrawal, death, or change in membership classification, in 1984 the members formed Subsidiary, a State for-profit corporation recognized in 1995 as tax-exempt under § 501(c)(2) retroactive to its 1984 inception. Subsidiary owned all tangible property for a country club (the "Property"), leased the Property to you for use in furtherance of your exempt purposes, and paid all income to you less operational expenses. The amount of Subsidiary income you received was typically less than 3% of your gross receipts. Only your members could own stock in Subsidiary.

Your members were the only shareholders of Subsidiary until 2006. You state that this affiliate structure was administratively expensive requiring, among other things, separate accounting, auditing, and tax returns, therefore you decided to simplify and streamline the structure. On Date 1, you bought one (1) share of the common stock of Subsidiary through an issuance of Subsidiary. Immediately thereafter, Subsidiary redeemed all other shares of its stock, which shares were held by your members. As a result, Subsidiary became your wholly owned subsidiary. You and Subsidiary were eligible to file consolidated returns but did not.

All profits derived by Subsidiary, after payment of all ordinary and necessary expenses, have been turned over to you for your use and benefit in its operation as a social club. You propose to completely liquidate Subsidiary (the "Liquidation"). A plan of liquidation was adopted in 2009. Under the liquidation plan, all of the stock of Subsidiary will be redeemed and cancelled and Subsidiary will be dissolved. You, as the sole shareholder of Subsidiary, will receive all assets and assume all liabilities of Subsidiary in the liquidation. You will continue to use the assets distributed from Subsidiary in the direct performance of your exempt function.

Upon the Service's issuance of this private letter ruling, Subsidiary will make its first liquidating distribution. At the same time, Subsidiary will cease to be a going concern and its activities will be limited to winding up its affairs, paying its debts, and distributing its remaining assets to you.

Once all the assets of Subsidiary are liquidated into you, Articles of Dissolution will be filed with State X with respect to Subsidiary, and Subsidiary will be dissolved.

REPRESENTATIONS

In connection with the proposed Liquidation, you represent as follows:

1. You, on the date of adoption of the liquidation plan and at all times until the final liquidating distribution is completed, will be the owner of at least *** percent of the single outstanding class of Subsidiary stock.
2. No shares of Subsidiary stock will have been redeemed during the three (3) years preceding the adoption of the plan of complete liquidation of Subsidiary.

3. Subsidiary has adopted a liquidation plan specifying that the final liquidating distribution is to be completed within 3 years from the close of the taxable year of Subsidiary in which the first liquidating distribution is made.
4. Subsidiary will retain no assets following the final liquidating distribution.
5. As soon as the first liquidating distribution has been made, Subsidiary will cease to be a going concern and its activities will be limited to winding up its affairs, paying its debts, and distributing its remaining assets to its shareholders
6. Subsidiary will not have acquired assets in any nontaxable transaction at any time, except for acquisitions occurring more than 3 years prior to the date of adoption of the liquidation plan.
7. No assets of Subsidiary have been, or will be, disposed of by either Subsidiary or you except for dispositions in the ordinary course of business and dispositions occurring more than three (3) years prior to adoption of the liquidation plan.
8. The liquidation of Subsidiary will not be preceded or followed by the reincorporation in, or transfer or sale to, a recipient corporation ("Recipient") of any of the businesses or assets of Subsidiary, if persons holding, directly or indirectly, more than twenty percent (20%) in value of the Subsidiary stock also hold, directly or indirectly, more than twenty percent (20%) in value of the stock in Recipient. For purposes of this representation, ownership will be determined by application of the constructive ownership rules of § 318(a) as modified by § 304(c)(3).
9. Prior to adoption of the liquidation plan, no assets of Subsidiary will have been distributed in kind, transferred, or sold to you, except for (i) transactions occurring in the normal course of business and (ii) transactions occurring more than 3 years prior to adoption of the liquidation plan.
10. Subsidiary will report all earned income represented by assets that will be distributed to its shareholders such as receivables being reported on a cash basis, unfinished construction contracts, commissions due, etc.
11. The fair market value of the assets of Subsidiary will exceed its liabilities both at the date of the adoption of the liquidation plan and immediately prior to the time the first liquidating distribution is made.
12. There is no intercorporate debt existing between you and Subsidiary and none has been cancelled, forgiven, or discounted, except for transactions that occurred more than three (3) years prior to the date of adoption of the liquidation plan.
13. All other transactions undertaken contemporaneously with, in anticipation of, in conjunction with, or in any way related to, the proposed liquidation of Subsidiary have been fully disclosed.
14. You have satisfied all the requirements to be classified as tax exempt under § 501(c)(7).
15. Subsidiary receives tax-exempt status under § 501(c)(2) and holds all tangible Property of the country club which is leased to you for use in connection with your exempt purpose.
16. Subsidiary has not engaged in activities that would give rise to unrelated business taxable income within the meanings of §§ 511 and 514.
17. All assets (including proceeds of sales of assets) distributed to you by Subsidiary in the liquidation will be used by you in the performance of your exempt function.

18. You will not use any of the assets received in the liquidation, or the proceeds from the sale of such assets, in any activity that would give rise to unrelated business taxable income within the meanings of §§ 511 and 514.

19. You represent that you intend to continue to use the assets distributed from Subsidiary in the direct performance of your exempt function.

20. If Property is sold by Subsidiary or by you, you will, within the period beginning one year before the date of such sale and ending three years after the date of such sale, reinvest the entire amount of the proceeds from the sale in the purchase of new exempt function property.

RULINGS REQUESTED

1: You will recognize no gain or loss upon the receipt of the assets and liabilities of Subsidiary in the liquidation. Section 332.

2: No gain or loss will be recognized by Subsidiary on the distribution of its assets to, or the assumption of liabilities by, you. Sections 337(a) and 336(d)(3). In particular, § 337(b)(2)(A) will not apply to the liquidation.

3: Your basis in each asset received from Subsidiary as a result of the liquidation will be the same as the basis of that asset in the hands of Subsidiary immediately before the liquidation. Section 334(b)(1).

4: Your holding period in each asset received from Subsidiary as a result of the liquidation will include the period during which that asset was held by Subsidiary. Section 1223(2).

5: That the liquidation of Subsidiary into you will not adversely affect your tax exempt status.

LAW

Section 332(a) provides that no gain or loss shall be recognized on the receipt by a corporation of property distributed in a complete liquidation of another corporation. Section 332(b) sets forth various requirements that must be met in order for a distribution to be considered in complete liquidation for purposes of § 332.

Section 337(a) provides that no gain or loss shall be recognized to the liquidating corporation on the distribution to the 80-percent distributee of any property in a complete liquidation to which § 332 applies.

Section 337(b)(2)(A) generally provides that §§ 337(a) and (b)(1) shall not apply where the 80-percent distributee is an organization (with limited exception not relevant on these facts) which is exempt from the tax imposed by Chapter 1.

Section 337(d) authorizes the Secretary to prescribe regulations as may be necessary or appropriate to carry out the purposes of the amendments made by subtitle D of title VI of the Tax Reform Act of 1986, including regulations to ensure that such purposes may not be circumvented through the use of a tax-exempt entity. The legislative history concerning a 1988 amendment to § 337(d) explains that the grant of authority in § 337(d) “includes rules to require the recognition of gain if appreciated property of a C corporation is transferred to . . . a tax-exempt entity in a carryover basis transaction that would otherwise eliminate corporate level tax on the built-in appreciation.” S. Rep. No. 445, 100th Cong., 2d Sess. 66 (1988) (footnote omitted).

Section 501(c)(2) provides for the exemption of corporations organized for the exclusive purpose of holding title to property, collecting income therefrom, and turning over the entire amount thereof, less expenses, to an organization which itself is exempt under § 501(a) of the Code.

Section 501(c)(7) provides for the exemption from federal income tax of clubs organized for pleasure, recreation, and other nonprofitable purposes, substantially all of the activities of which are for such purposes and no part of the net earnings of which inures to the benefit of any private shareholder.

Pub. L. 94-568 amended § 501(c)(7) in 1976 so such organizations could receive some outside income without losing their exempt status.

S. Rep. No. 1318, 94th Cong., 2d Sess. 4 (1976) explains how Congress intends the amended § 501(c)(7) work including limits on gross receipts from outside sources and non-members, and certain exclusions such as unusual income.

Section 1.337(d)-4(a)(1) of the regulations sets forth the general rule that if a taxable corporation transfers all or substantially all of its assets to one or more tax-exempt entities, the taxable corporation must recognize gain or loss immediately before the transfer as if the assets transferred were sold at their fair market values.

RULINGS

Based solely on the information submitted and representations provided, we rule as follows:

1: You will recognize no gain or loss upon the receipt of the assets and liabilities of Subsidiary in the liquidation. Section 332.

2: No gain or loss will be recognized by Subsidiary on the distribution of its assets to, or the assumption of liabilities by, you. Sections 337(a) and 336(d)(3). In particular, § 337(b)(2)(A) will not apply to the liquidation.

3: Your basis in each asset received from Subsidiary as a result of the Liquidation will be the same as the basis of that asset in the hands of Subsidiary immediately before the liquidation. Section 334(b)(1).

4: Your holding period in each asset received from Subsidiary as a result of the liquidation will include the period during which that asset was held by Subsidiary. Section 1223(2).

5: As there is no recognition of gain or loss as described in rulings (1), (2), and (3), the liquidation of Subsidiary into you will not adversely affect your tax exempt status.

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,

Theodore R. Lieber

Manager, Exempt Organizations

Technical Group 3

Private Letter Ruling: Extinguishable Conservation Easement May Qualify as Conservation Contribution.

The IRS stated that granting a deed for a conservation easement that allows the easement to be extinguished under state law if circumstances change to make the easement impractical or impossible may nonetheless be a qualified conservation contribution under section 170(h).

Release Date: 3/29/2013

Date: September 18, 2012

Attention: * * *

Dear * * *:

This letter responds to your request for information dated July 19, 2012.

In your request, you asked whether a contribution of an easement can be a qualified conservation contribution if the easement deed simply allows for extinguishment under applicable State law upon subsequent, unexpected changes in the conditions surrounding the property that make impractical or impossible the continued use of the property for conservation purposes.

Property rights have been described “as a ‘bundle of sticks’ — a collection of individual rights which, in certain combinations, constitute property.” U.S. v. Craft, 535 U.S. 274, 278 (2002) (citations omitted). State law dictates what rights make up a person’s bundle. Id. Once a person’s property rights are established under State law, the tax consequences of a transaction involving that property are decided under Federal law. Patel v. Commissioner, 138 T.C. No. 23, slip op. 16, 2012 WL 2427326 at *7 (2012) (citing Commissioner v. Estate of Bosch, 387 U.S. 456 (1967); Aquilino v. United States, 363 U.S. 509, 512-513 (1960); Morgan v. Commissioner, 309 U.S. 78, 80-81 (1940)).

A “qualified conservation contribution” is a contribution of a qualified real property interest to a qualified organization exclusively for conservation purposes. I.R.C. § 170(h)(1). A contribution is not exclusively for conservation purposes unless it protects the conservation purpose in perpetuity.

I.R.C. § 170(h)(5)(A).

Under the Treasury regulations, a conservation purpose may be treated as protected in perpetuity if, upon a subsequent change in conditions that makes impossible or impractical the continued use of the subject property for conservations purposes, the easement is extinguished by judicial proceeding and all of the donee's proceeds from a subsequent sale, exchange, or involuntary conversion of the property are used by the donee in a manner consistent with the conservation purposes of the original contribution. Treas. Reg. § 1.170A-14(g)(6)(i). The donee's proceeds must be at least equal to the proportionate value of the perpetual conservation restriction. Treas. Reg. § 1.170A-14(g)(6)(ii).

State law may provide a means for extinguishing an easement for State law purposes. However, the requirements of § 170(h) and the regulations thereunder must nevertheless be satisfied for a contribution to be deductible for Federal income tax purposes.

This letter has called your attention to certain general principles of the law. It is intended for informational purposes only and does not constitute a ruling. See section 2.04 of Rev. Proc. 2012-1, 2012-1 I.R.B. 7 (Jan. 3, 2012). If you have any additional questions, please contact me or *** at ***.

Sincerely,

Karin Goldsmith Gross

Acting Branch Chief, Branch 1

(Income Tax & Accounting)

[IRS: Published Volume Cap Limit for Tribal Economic Development Bonds.](#)

In Notice 2012-48, 2012-31 I.R.B. 102 (July 30, 2012), the Treasury Department and the IRS provided guidance regarding applications for allocations of the available amount of national bond volume limitation authority (volume cap) for tribal economic development bonds. The Notice provides that, except as otherwise provided in the Notice, for applications filed with the IRS that meet the requirements detailed in the Notice, the IRS will allocate an amount of available volume cap equal to the amount requested in the application on a first-come, first-served basis by order of submission date (as defined in the Notice).

The Notice also provides that no Indian tribal government will receive an allocation of volume cap that would cause the aggregate amount of volume cap allocated to that Indian tribal government pursuant to the Notice (not including certain amounts forfeited as described in the notice) to exceed the Published Volume Cap Limit in effect for the period that includes the submission date. The Published Volume Cap Limit for any period is the greater of (1) 20% of the amount of available volume cap as of the first day of such period (determined as described in the Notice); or (2) \$100 million

The Published Volume Cap Limit for the period commencing April 1, 2013 is \$308,726,846 (20% of the amount of available volume cap of \$1,543,634,230 determined as described in the Notice).

For purposes of this limitation, an Indian tribal government includes the Indian tribal government, together with any political subdivisions of the Indian tribal government, and any entities controlled

by the Indian tribal government. An application that requests an allocation of volume cap in an amount that would cause the Published Volume Cap Limit in effect on the date of submission to be exceeded will be treated as incomplete until the day the applicant supplements the application in a manner that complies with the requirements of the notice and does not cause such limit to be exceeded.

IRS: Proposed Collection; Comment Request for Regulation Project.

Currently, the IRS is soliciting comments concerning qualified conservation contributions (§ 1.170A-14). Written comments should be received on or before June 11, 2013 to be assured of consideration.

Direct all written comments to Yvette Lawrence, Internal Revenue Service, room 6129, 1111 Constitution Avenue NW., Washington, DC 20224. Requests for additional information or copies of the regulations should be directed to Katherine Dean at Internal Revenue Service, Room 6242, 1111 Constitution Avenue NW., Washington, DC 20224, or at (202) 622-3186, or through the Internet at Katherine.b.dean@irs.gov.

IRS: Comments Sought on Regs on Qualified Conservation Contributions.

Internal Revenue Code section 170(h) describes situations in which a taxpayer is entitled to a deduction for a charitable contribution for conservation purposes of a partial interest in real property. This regulation requires a taxpayer claiming a deduction to maintain records of (1) the fair market value of the underlying property before and after the donation and (2) the conservation purpose of the donation.

Request for Comments: Comments submitted in response to this notice will be summarized and/or included in the request for OMB approval. All comments will become a matter of public record. Comments are invited on: (a) Whether the collection of information is necessary for the proper performance of the functions of the agency, including whether the information shall have practical utility; (b) the accuracy of the agency's estimate of the burden of the collection of information; (c) ways to enhance the quality, utility, and clarity of the information to be collected; (d) ways to minimize the burden of the collection of information on respondents, including through the use of automated collection techniques or other forms of information technology; and (e) estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information.

IRS: Comments Sought on EO Reporting Requirement Guidance.

The IRS has requested public comment on information collections under Rev. Proc. 98-19, which provides guidance to tax-exempt organizations on exceptions to the reporting and notice requirements under section 6033(e)(1) and the tax imposed by section 6033(e)(2); comments are due by June 11, 2013.

Direct all written comments to Yvette Lawrence, Internal Revenue Service, room 6129, 1111 Constitution Avenue NW., Washington, DC 20224. Requests for additional information or copies of the revenue procedure should be directed to Katherine Dean at Internal Revenue Service, Room 6242, 1111 Constitution Avenue NW., Washington, DC 20224, or at (202) 622-3186, or through the Internet at kathernie.b.dean@irs.gov.

Comments are invited on: (a) Whether the collection of information is necessary for the proper performance of the functions of the agency, including whether the information shall have practical utility; (b) the accuracy of the agency's estimate of the burden of the collection of information; (c) ways to enhance the quality, utility, and clarity of the information to be collected; (d) ways to minimize the burden of the collection of information on respondents, including through the use of automated collection techniques or other forms of information technology; and (e) estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information.

IRS: Comments Sought on Reimbursement Bond Regs.

The IRS requested public comment on information collections under final regulations (T.D. 8394) under section 150 that provide rules to tax-exempt bond issuers for allocating proceeds of reimbursement bonds; comments are due by June 11, 2013.

Direct all written comments to Yvette Lawrence, Internal Revenue Service, room 6129, 1111 Constitution Avenue NW., Washington, DC 20224. Requests for additional information or copies of the regulation should be directed to Katherine Dean, at (202) 622-3186, or at Internal Revenue Service, room 6242, 1111 Constitution Avenue NW., Washington, DC 20224, or through the Internet, at Katherine.b.dean@irs.gov.

This regulation clarifies when the allocation of bond proceeds to reimburse expenditures previously made by an issuer of the bond is treated as an expenditure of the bond proceeds. The issuer must express a reasonable official intent, on or prior to the date of payment, to reimburse the expenditure in order to assure that the reimbursement is not a device to evade requirements imposed by the Internal Revenue Service.

Which states and counties have the highest taxes?

With taxes a hot topic in Washington and around the dinner table in millions of American homes, this analysis features interactive maps that look at how states and counties stack up against one another when it comes to income and property taxes. There is also a map that shows the ZIP codes throughout the U.S. where residents are most likely to use tax software to prepare their returns.

The map is available at:

<http://smartblogs.com/finance/2013/04/12/tax-day-cometh/>

IRS Issues Proposed Regs on Community Health Needs Assessment Requirement for Tax-Exempt Hospitals.

The IRS has issued proposed regulations (REG-106499-12) that provide guidance to charitable hospital organizations on the community health needs assessment (CHNA) requirements and related excise tax and reporting obligations. The regs also clarify the consequences for failing to meet these and other requirements for charitable hospital organizations.

Comments and requests for a public hearing must be received by July 5. The regs are proposed to be effective for returns filed on or after the date they are published in the Federal Register as final or temporary regulations.

Section 501(r)(1) imposes four additional requirements that organizations described as hospital organizations must satisfy to be tax exempt under section 501(c)(3), one of which is to conduct a CHNA every three years. In July 2011 Treasury and the IRS issued guidance (Notice 2011-52) on the anticipated regulatory provisions.

As a general rule, the proposed regs provide that a hospital organization operates a hospital facility if it is a partner in a joint venture, limited liability company, or other entity treated as a partnership for federal income tax purposes that operates the hospital facility. A hospital organization also operates a hospital facility under the proposed regs if it does so through a wholly owned entity that is disregarded as separate from the hospital organization for federal tax purposes. A hospital organization is not required, however, to meet the requirements of section 501(r) for any activities unrelated to the operation of a hospital facility.

The proposed regs provide that a hospital organization meets the requirements of section 501(r)(3) in any tax year for a hospital facility it operates only if the hospital facility has conducted a CHNA in that tax year or in either of the two immediately preceding tax years. Also, an authorized body of the hospital facility is required to have adopted an implementation strategy to meet the community health needs identified through the CHNA by the end of the tax year in which the hospital facility conducts the CHNA. The regs include extensive rules for conducting a CHNA and developing implementation strategies.

Under the proposed regs, a hospital facility's omission of required information from a policy or report described in reg. section 1.501(r)-3 or 1.501(r)-4 or error regarding the implementation or operational requirements described in reg. section 1.501(r)-3 through 1.501(r)-6 will not be considered a failure to meet a requirement of section 501(r) if the omission or error was minor, inadvertent, and due to reasonable cause and the hospital facility corrects the omission or error as promptly after discovery as is reasonable given the nature of the omission or error. Also, the IRS will consider for purposes of determining whether revocation of section 501(c)(3) status is warranted the relative size, scope, nature, and significance of any failures to meet the section 501(r) requirements as well as the reasons for the failures and whether the same type of failures have previously occurred. The proposed regs include rules that apply if one hospital facility within a hospital organization fails to meet a section 501(r) requirement during a tax year, even though the hospital organization as a whole continues to be recognized as a section 501(c)(3) organization.

[http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/New-Requirements-for-501\(c\)\(3\)-Hospitals-Under-the-Affordable-Care-Act](http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/New-Requirements-for-501(c)(3)-Hospitals-Under-the-Affordable-Care-Act)

Tax Analysts: Joint Strategies for Meeting Community Health Needs Possible Under Proposed Regs.

Tax-exempt hospital facilities that collaborate with other facilities and organizations to develop ways to meet the healthcare needs of their communities could in some cases also adopt joint implementation strategies, according to proposed regulations released April 3.

Tax-exempt hospital facilities that collaborate with other facilities and organizations to develop ways to meet the healthcare needs of their communities could in some cases also adopt joint implementation strategies, according to proposed regulations released April 3.

Under REG-106499-12 , which provides proposed guidance under section 501(r) on rules requiring nonprofit hospitals to conduct community health needs assessments (CHNAs) at least once every three years and develop strategies to meet identified needs, a hospital facility may work with other facilities and organizations to develop its implementation strategy but must document its strategy in a separate written plan. The facility could adopt a joint implementation strategy if it also adopts a joint report of its CHNA and the strategy is clearly identified as applying to the facility, identifies the facility's role in developing the strategy, and includes a summary or other tool to help people find the portions of the strategy that involve the facility.

Douglas M. Mancino of Hunton & Williams LLP told Tax Analysts the provision recognizes that "there is a lot of joint planning that gets done even among unrelated hospitals in a particular region." T.J. Sullivan of Drinker Biddle & Reath LLP said the provision reflects an IRS effort to provide added flexibility to hospitals while ensuring that the intent underlying the statute is carried out. Although only a few systems are likely to choose the approach, it may save them a lot of time without undercutting the contributions of the CHNAs, Sullivan said.

Also under the proposed regs, only significant health needs identified through a CHNA would have to be addressed in an implementation strategy, which would have to describe how the hospital facility would address the health needs and what the expected result would be. If a hospital facility does not plan to address a particular need, it would need to explain why not. Some of the reasons could be resource constraints, lack of expertise, or that the need is being addressed by other facilities or organizations.

The proposed regs also would require a hospital facility to adopt an implementation strategy by the end of the tax year in which the CHNA is conducted. Commentators responding to Notice 2011-52, 2011-30 IRB 60 , which spelled out the expected provisions in the proposed regs, asked for more time. The proposed regs deny that request, although they offer transition relief for hospitals that may not have had three full years during which to conduct their first CHNA.

Sullivan said that while he did not like that approach, "the definition of when a CHNA is 'conducted' that is keyed to when it is posted on the Web makes it much easier to control the timing than it may have initially appeared."

Reporting Requirements

A hospital organization also would have to attach to its Form 990, "Return of Organization Exempt From Income Tax," the most recent implementation strategies for each of its hospital facilities. Alternatively, it could report on the return the URLs of the Web pages on which the implementation strategies have been posted.

“Widely Available” Requirement

The proposed regs would require CHNA reports to be posted conspicuously online and remain there until two subsequent CHNA reports have been added. Also, a hospital facility could not require an individual to create an account or otherwise provide identifiable information to access an online report, which also would have to be available in paper format.

Mancino said he doubted making multiple reports available online would be burdensome and that he did not think there would be many requests for paper copies because the documents are available electronically. It’s also unlikely many people will ask to see the reports, he said.

“There will be some public health advocates and people who are advocates for different disadvantaged classes of individuals that will be interested in this,” Mancino said. “But by and large I think the general public probably will have little or no interest in the community health needs assessment documentation.”

Sullivan also said he did not think the requirements will be too burdensome, adding that the IRS is becoming increasingly deft at balancing the interests of the hospital community and those of patient advocates.

Self-Correction

The proposed regs say Treasury and the IRS will publish guidance to help hospital facilities correct failures to fulfill CHNA requirements and other rules under section 501(r) and disclose how the errors were corrected.

Mancino commended the government for offering clear guidance on self-correction and self-disclosure.

“That aspect of the proposed regulations is probably the most welcome, in my mind,” Mancino said, adding that in his experience, it is rare for a nonprofit hospital to intentionally break laws.

Public Health Departments

In conducting a CHNA, a hospital facility would be required to seek input from state or local public health departments. Sullivan was pleased that the proposed regs eliminated a provision in Notice 2011-52 that would have required consultation with a public health expert, explaining that having to identify particular individuals consulted by hospitals probably would not have been well received.

Revocations, Excise Taxes

The proposed regs also say that although section 501(r) empowers the IRS to revoke the exempt status of noncompliant hospitals, the agency should consider all facts and circumstances when considering revocation, including the scope of and reasons for the noncompliance and whether the same sorts of violations have occurred before. Willful or egregious violations ordinarily will lead to revocation, according to the proposed regs.

Hospital organizations that do not meet the CHNA requirements face a \$50,000 excise tax. The tax is applied on a facility-by-facility basis, meaning a hospital organization with multiple facilities could be taxed \$50,000 on each facility.

[IRS: Upcoming Workshops for Small and Medium-Sized 501\(c\)\(3\)](#)

Organizations.

IRS Exempt Organizations offers one-day workshops for small and medium-sized 501(c)(3) organizations around the country in collaboration with colleges and universities as part of our Academic Institutions Initiatives in an effort to help develop the nonprofit leaders of tomorrow. These popular workshops are presented by experienced IRS Exempt Organizations specialists and explain the nuts and bolts of what 501(c)(3) entities must do to keep their tax-exempt status and comply with tax obligations.

[http://www.irs.gov/Charities-&-Non-Profits/Upcoming-Workshops-for-Small-and-Medium-Sized-501\(c\)\(3\)-Organizations](http://www.irs.gov/Charities-&-Non-Profits/Upcoming-Workshops-for-Small-and-Medium-Sized-501(c)(3)-Organizations)

NABL Seeks Guidance on Tax-Exempt Status of Debt Issued by Accountable Care Organizations.

Scott Lilienthal of the National Association of Bond Lawyers has written to Treasury and the IRS requesting guidance on what constitutes private business use when a tax-exempt bond borrower participates in an accountable care organization.

H.R. 1268 Would Provide Flood Mitigation Expenses Credit.

H.R. 1268, the Flood Mitigation Expense Relief Act of 2013, introduced by Rep. Steven M. Palazzo, R-Miss., would provide a tax credit for qualified flood mitigation expenses incurred for homes with increasing premium rates under the national flood insurance program, and increase funding for mitigation programs.

Firm Seeks Guidance on Reinvestment of Redemption Proceeds in Treasury Bills.

Alexander Deland of Winston & Strawn LLP has urged Treasury and the IRS to immediately issue guidance to relieve some qualified and recovery zone facility bonds from a significant risk created by a recently enacted law suspending the debt limit that could cause the loss of tax-exemption or the premature redemption of the bonds.

IRS: Government Grants for Railroad's Crossing Improvements Are Tax Free.

In field attorney advice, the IRS concluded that grants a railroad received under Transportation Department regulations governing railroad crossing safety improvements did not constitute gross income to the railroad.

The railroad received one type of grant for constructing a grade crossing and installing train-

activated warning devices. Those grants included a statement that the funds provided no net benefit to the railroad. A second type of grant was for installing active warning devices and required the railroad to pay no more than 10 percent of the construction costs. That portion, according to the grant, would represent the railroad's net benefit. The railroad argued the grants were not taxable income because it did not receive a net benefit as described under the Transportation Department regulations and that therefore it had no accession to wealth.

The IRS agreed with the railroad, finding that any benefit it received was incidental and not an accession to wealth. The IRS explained that the Transportation Department provisions governing railroad crossing safety improvements appear to be a cost-sharing arrangement between the federal government and the railroads and imply that Congress views the grants as having a public rather than a private purpose.

[White House Announces Plan to Encourage Private Infrastructure Investment.](#)

President Obama's "Rebuild America Partnership" plan to stimulate private infrastructure investment would exempt foreign pension funds from taxes on gains from U.S. real property investments, create a new permanent bonds program, and modify some of the restrictions on qualified private activity bonds, according to a March 29 White House release.

[IRS Addresses Reporting Requirements for Condemnation Payments.](#)

In e-mailed advice, the IRS concluded that a state's transportation department that makes payments for property acquired through condemnation proceedings has a section 6045(e) reporting requirement and must issue Forms 1099-S reflecting the entire cash payments unless the transaction or recipient is exempt from the reporting requirement.

[IRS Publishes Population Figures for Housing Credit, Private Bond Purposes.](#)

IRS Publishes Population Figures for Housing Credit, Private Bond Purposes.

Notice 2013-15, page 739. This notice advises State and local housing credit agencies that allocate low-income housing tax credits under section 42 of the Code, and States and other issuers of tax-exempt private activity bonds under section 141, of the population figures to use in calculating: (1) the 2013 calendar year population-based component of the State housing credit ceiling (Credit Ceiling) under section 42(h)(3)(C)(ii); (2) the 2013 calendar year volume cap (Volume Cap) under section 146; and (3) the 2013 volume limit (Volume Limit) under section 142(k)(5).

Generally, § 146(j) requires determining the population figures for the population-based component of both the Credit Ceiling and the Volume Cap for any calendar year on the basis of the most recent census estimate of the resident population of a State (or issuing authority) released by the U.S. Census Bureau before the beginning of the calendar year. Similarly, § 142(k)(5) bases the Volume Limit on the State population.

Sections 42(h)(3)(H) and 146(d)(2) require adjusting for inflation the population-based component of the Credit Ceiling and the Volume Cap. The adjustments for the 2013 calendar year are in Rev. Proc. 2012-41, 2012-45 I.R.B. 539. Section 3.03 of Rev. Proc. 2012-41 provides that, for calendar year 2013, the amount for calculating the Credit Ceiling under § 42(h)(3)(C)(ii) is the greater of \$2.25 multiplied by the State population, or \$2,590,000. Further, section 3.07 of Rev. Proc. 2012-41 provides that the amount for calculating the Volume Cap under § 146(d)(1) for calendar year 2013 is the greater of \$95 multiplied by the State population, or \$291,875,000.

For the 50 states, the District of Columbia, and Puerto Rico, the population figures for calculating the Credit Ceiling, the Volume Cap, and the Volume Limit for the 2013 calendar year are the resident population estimates released electronically by the U.S. Census Bureau on December 20, 2012, in Press Release CB12-250. For American Samoa, Guam, the Northern Mariana Islands, and the U.S. Virgin Islands, the population figures for the 2013 calendar year are the 2012 midyear population figures in the U.S. Census Bureau's International Data Base (IDB). The U.S. Census Bureau electronically announced an update of the IDB on June 27, 2012, in Press Release CB12-118.

IRS Confirms Excludability of Income Derived From Essential Governmental Function.

The IRS has ruled that the income of a nonprofit corporation created to coordinate the operation of electric generation resources and the purchase and sale of electricity on behalf of members will continue to be excluded from gross income under section 115(1), even if the corporation enters into proposed transactions with nongovernmental entities. Letter Ruling 201310010.

IRS Releases New Required Form for TEB VCAP Submissions.

The Internal Revenue Service has released Form 14429, Tax Exempt Bonds Voluntary Closing Agreement Program Request, which is a new form required for a Tax Exempt Bonds Voluntary Closing Agreement Program submission request. The purpose of the new form is to assist issuers in organizing submission requests and to ensure that their submissions are complete and in accordance with the requirements under Notice 2008-31, 2008-11 I.R.B. 592 and IRM 7.2.3.

<http://www.irs.gov/pub/irs-pdf/f14429.pdf>

IRS: Trust's Income Excludable From Gross Income.

The IRS has ruled that the income of a trust established to fund post-employment health benefits for the employees of a government entity was excludable from gross income under section 115(1) because the income was derived from the exercise of an essential government function. Citations: Letter Ruling 201310026.
