Bond Case Briefs

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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,

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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 vale 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 it 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 you 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.

Issue 15

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