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

TAX EXEMPT AND GOVERNMENT ENTITIES DIVISION

Uniform Issue List

Date: FEB 19 2004

4941.03-00
4941.04-00

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Legend:

B =
C =
D =
M =
N =
O =
P =

x =

Dear Sir or Madam:

We have considered the ruling request dated September 18, 2003, submitted on behalf of M and N, concerning issues arising under section 4941 of the Internal Revenue Code as a result of the proposed transaction described below.

FACTS

M is an O nonprofit corporation, formed in 1943, which is exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code. It has also been classified as a private foundation under section 509(a) of the Code. M had investment assets with a fair market value in excess of $650,000x as of the end of June,

Certain individuals, most of whom are descendants and/or spouses of B, the founder of P, as well as (a) certain trusts created by or for such individuals, and (b) certain partnerships and/or limited liability companies of which such individuals and/or trusts own more than 50% of the voting and/or profits interests, have established N, a partnership, into which such individuals, trusts, partnerships and/or limited liability companies (hereinafter the "B Descendants/Entities") will initially, and from time to time thereafter, contribute cash or other assets. N will, in turn, then invest and reinvest the assets which it owns in such investments.

From time to time, the B Descendants/Entities will also withdraw cash and/or other assets from such Partnerships.

You anticipate that the B Descendants/Entities will in the future establish additional new entities (the "Additional Partnerships") for co-investment purposes which will be substantially similar in all material respects to N. However, each Additional Partnership established will in all probability focus on different investments and utilize different objectives than those contemplated for N.

N and each Additional Partnership is being formed to give the B Descendants/Entities, by investing as a group, increased negotiating power and cost savings which the partners would not have if they invested separately, as well as access to certain brokerage, tax, and portfolio services. N and the Additional Partnerships will be treated and taxed as a partnership for federal income tax purposes.

M will have, from time to time, some of the same investment objectives as those which will be pursued by N or the Additional Partnerships. The B Descendants/Entities have invited and will invite, in some cases, M to become either one of the initial members of N or an Additional Partnership or a subsequent member so that M will have access to certain brokerage, tax, and portfolio services, and will also benefit from the increased negotiating leverage and cost savings enjoyed by the partners or members of N or the Additional Partnerships.

There may be individuals or entities other than the B Descendants/Entities and M who will, on occasion, invest in N or the Additional Partnerships, but for purposes of this request, it is assumed that at all times, the majority of the investors in N or the Additional Partnerships, both in terms of ownership percentage and amount invested, will be B Descendants/Entities and M. The Service should also assume that immediately after formation, the B Descendants/Entities will own in excess of 35% of the ownership of N and each Additional Partnership, thereby making N or the Additional Partnership a "disqualified person" with respect to M. B was a disqualified person with respect to M and it can be assumed that each B Descendant/Entity is also a disqualified person with respect to M.

The initial Managers of N will be individuals who are "disqualified persons" with respect to M but only by reason of the fact that they are officers (not directors) of M. However, it is possible that individuals or entities who are B Descendants/Entities who are disqualified persons with respect to M for other reasons may become the Manager or General Manager of N or any Additional Partnership in the future, and it is assumed that this will occur and be the case for the purposes of this ruling request.

M has concluded that it will be beneficial to invest in and through N and the Additional Partnerships because such investment will: (1) permit M to obtain certain brokerage, tax, and portfolio services provided by N or the Additional Partnerships; (2) assist M in diversifying its portfolio; (3) obtain access through N or the Additional Partnerships to investments with higher minimum investment requirements than M would want to satisfy using its assets alone, and (4) permit M to effect economies of scale and resulting cost savings as well as greater negotiating power.

M does not know the aggregate amount of its assets which it will use, from time to time, to invest in N and the Additional Partnerships. However, it is now contemplated that M will invest approximately 1.5 % of its assets in N. It is also anticipated that M's investment in N and in any Additional Partnership will constitute a substantial percentage, perhaps even exceeding fifty percent, of the total assets of each partnership in question.

It is contemplated that as to N and each Additional Partnership, M will become an investor either (1) upon the formation of N or an Additional Partnership, or (2) by making its initial contribution to N or an Additional Partnership in consideration for ownership interests in that entity after it has been funded initially by B Descendants/Entities and become operational. M may also make additional contributions to N or an Additional Partnership in consideration for additional ownership interests. Further, M will make withdrawals from time to time, either of cash or other assets from N or an Additional Partnership. In such instance, M's ownership interest in the particular entity will be correspondingly reduced.

The initial Managers of N are now contemplated to be C and D, both of whom are officers of M and therefore "disqualified persons" for that reason alone with respect to M. The Managers of N and the Additional Partnerships will select an investment manager or managers to manage and invest the assets of N and the Additional Partnerships. The Operating Agreement provides that neither the custodian nor any investment manager for any partnership may be a "disqualified person" with respect to M.

In Subsection 6(h), M is given certain privileges which are not applicable to other Investors, in particular, the right to receive an "in kind" distribution of its interest in the event it elects to withdraw, i.e., an in kind distribution of its pro rata share of each of N's or an Additional Partnership's assets.

Under the Operating Agreement, the Investors, also referred to as "Participants", are given the right to make certain major decisions, but M is, in effect, given veto rights as it relates to certain defined decisions. The Operating Agreement also limits the ability of N or the Additional Partnerships to take certain actions or make certain investments which could be detrimental to M.

Specific provisions are included in the Operating Agreement to prevent any benefit accruing to any B Descendant/Entity or any other "disqualified person" by reason of the fact that M is also an Investor in N or an Additional Partnership. In particular, to the extent that any costs, fees, or expenses are incurred by N or an Additional Partnership that are based on a percentage of N or Additional Partnership assets that varies depending upon the amount of such assets, M will pay the lowest possible percentage fees and the other Investors will bear the burden of and pay the remainder of such fees. Moreover, to the extent that any cost savings with respect to any costs, fees, or expenses are achieved by N or the Additional Partnerships because the amount of their respective assets exceed minimum asset amount thresholds, and such savings would not be achieved if M were not an Investor, all of such savings will inure to M and none of such savings will inure to the other Investors. You direct our attention to a section

of the Operating Agreement which sets forth examples of how certain costs and expenses will be allocated.

The Operating Agreement for N or the Additional Partnerships also gives M the right to withdraw from the entity, in whole or in part, as of the end of any month.

RULINGS REQUESTED

1. M's initial investment in N or any Additional Partnership either upon its formation or at any time after it is formed will not result in or constitute any act of "self-dealing" under section 4941(d)(1)(A) of the Code.

2. Any additional investments in or contributions to N or Additional Partnership by M after N or Additional Partnership is formed and becomes operational, or to acquire additional ownership interests in N or Additional Partnership, will not result in or constitute any act of "self-dealing" under section 4941(d)(1)(A) of the Code.
3. M's withdrawal at any time of all or any part of its interest or assets in N or Additional Partnership will not result in or constitute any act of "self-dealing" under section 4941(d)(1)(A) of the Code.

4. Any contribution to or withdrawal from N or Additional Partnership by any Investor other than M will not result in or constitute any act of "self-dealing" under section 4941(d)(1)(A) of the Code.

LAW

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

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

Section 4946(a)(1) of the Code provides, in part, that the term "disqualified person" means, with respect to a private foundation, a person who is -

(A) a substantial contributor to the foundation,

(B) a foundation manager,

(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 subparagraphs (A), (B) or (C),

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

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

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

Section 4946(a)(3) of the Code requires that for purposes of determining the ownership of a corporation, there shall be taken into account indirect stockholdings which would be taken into account under section 267(c) of the Code, as modified by the definition of members of family under section 4946(d).

Section 4946(a)(4) of the Code requires that for purposes of determining the profits or beneficial interests in a partnership or trust, the rules of constructive ownership under section 267(c) of the Code, as modified by the definition of members of family under section 4946(d), be taken into account.

Section 4946(d) of the Code provides that, for purposes of section 4946(a)(1), the family of an individual shall include only his spouse, ancestors, children ,grandchildren, great-grandchildren, and the spouses of children, grandchildren, and great-grandchildren.

Section 53.4941(d)-1(a) of the Foundation and Similar Excise Taxes Regulations provides that it is immaterial whether a self-dealing transaction results in a benefit or detriment to the private foundation. Self-dealing does not, however, include a transaction between a private foundation and a disqualified person where the disqualified person status arises only as a result of such transaction.

Section 53.4941(d)-2(f)(2) of the regulations provides that the fact that a disqualified person receives an incidental or tenuous benefit from the use by a foundation of its income or assets will not, by itself, make such use an act of self-dealing.

Section 53.4941(d)-3(c)(1) of the regulations provides that the term "personal services" includes the services of a broker serving as agent for the private foundation, but not the services of a dealer who buys from the private foundation as principal and resells to third parties. This paragraph applies without regard to whether the person who receives the compensation (or payment or reimbursement) is an individual. The portion of any payment which represents payment for property shall not be treated as payment of compensation (or payment or reimbursement of expenses) for the performance of personal services for purposes of this paragraph.

In section 53.4941(d)-3(d)(2), Example 2 of the regulations, C, a manager of private foundation X, owns an investment counseling business. Acting in his capacity as an investment counselor, C manages X's investment portfolio for which he receives an amount which is determined to be not excessive. The payment of such compensation to C shall not constitute an act of self-dealing.

Section 4943 of the Code imposes an excise tax on any "excess business holdings" of a private foundation.

Section 4943(c) of the Code defines an "excess business holding" as any interest in a "business enterprise" held in excess of 20% of the business's voting stock or profits interest reduced by any such stock or interest held by disqualified persons.

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

In S. Rep. No. 552, 91st Cong., 1st Sess. [41] (1969), the Senate Finance Committee stated the following regarding the meaning of "business holding" under section 4943 of the Code:

> (S)tock in a passive holding company is not to be considered a business holding, even if the holding company is controlled by the foundation. Instead, the foundation is to be treated as owning its proportionate share of the underlying assets of the holding company. The committee also made it clear that passive investments generally are not to be considered business holdings. For example, the holding of a bond issue is not a business holding, nor is the holding of stock of a company which itself derives income in the nature of a royalty to be treated as a business holding.

ANALYSIS

When N or any Additional Partnership is established, M may contribute cash or other assets to N or an Additional Partnership in consideration for its ownership interest. At approximately the same time, the B Descendants/Entities will contribute cash or assets for their respective ownership interests in N or an Additional Partnership. No act of self-dealing occurs in this situation because at the time that M invests, N or any Additional Partnership is not then a "disqualified person" with respect to M.

M's proposed acquisition of a limited partnership interest in N or any Additional Partnership is in substance a "co-investment arrangement" by M in N or an Additional Partnership along with the other investors in these entities; it is not a sale or exchange between M and N or any Additional Partnership or between M and the other partners of N or any Additional Partnership, including the B Descendants/Entities, for purposes of section 4941(d)(1)(A) of the Code. In joint or co-investment situations, when a private foundation acquires an additional interest in the partnership entity after its formation and initial funding or

withdraws its interest, there is neither an economic benefit to the other investors nor does the ownership or holdings of the other investors change in any economic or other material respect.

Section 4943 of the Code expressly contemplates and permits joint or co-investments by disqualified persons and private foundations. Numerous joint or co-investment situations exist, as permitted by section 4943, where both the private foundations and the disqualified persons involved either buy or sell interests in the investment entity or make withdrawals from such entity after formation and initial funding. The passive investments contemplated by M are not considered a "business enterprise"; see section 4943(d)(3)(B).

M's investment in N or any Additional Partnership permits it to obtain "brokerage and portfolio services". N and any Additional Partnerships will investigate and choose investments for these entities. They will monitor the underlying investments and make changes when deemed appropriate or prudent. They will also provide the necessary brokerage services which are required to invest in the underlying investments. N and any Additional Partnerships will provide M with periodic reports describing the current status of their investments. Prior to its investments, N and any Additional Partnerships will advise M as to the characteristics and objectives of each underlying investment and the tax implications of such investment. These services and benefits which M will receive by investing in N or each Additional Partnership are in the nature of "brokerage and portfolio services", and, as such, they are considered "personal services" within the meaning of section 53.4941(d)-3(c)(1) of the regulations. See also Example 2 in section 53.4941(d)-3(d)(2). Thus, the payment of compensation for such services will not constitute an act of self-dealing.

RULINGS

Based on M's representations, and the applicable law, we are able to rule as follows:

1. M's initial investment in N or any Additional Partnership either upon its formation or at any time after it is formed will not result in or constitute an act of self-dealing under section 4941(d)(1)(A) of the Code.

2. Any additional investments in or contributions to N or any Additional Partnerships by M after N or any Additional Partnership is formed and becomes operational, or to acquire additional ownership interests in N or any Additional Partnership, will not result in or constitute an act of self-dealing under section 4941(d)(1)(A) of the Code.

3. M's withdrawal at any time of all or part of its interest or assets in N or any Additional Partnership will not result in or constitute an act of self-dealing under section 4941(d)(1)(a) of the Code.

4. Any contribution to or withdrawal from N or any Additional Partnership by any investor other than M will not result in or constitute an act of self-dealing under section 4941(d)(1)(a) of the Code.