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

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TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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UIL: 501.00-00
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Person to Contact
Identification Number
Telephone Number

LEGEND:

F =
C =
P =

Dear

We have considered your request and subsequent restatements and amendments for a ruling that a proposed sale of stock and the sale of membership units to disqualified persons will not constitute acts of self-dealing under section 4941 of the Internal Revenue Code (the Code).

F is an organization recognized as exempt from federal income tax as an organization described in section 501(c)(3) of the Code, and later classified as a private foundation under section 509(a).

The founder of F made an initial gift of stock in C, a for-profit corporation, to F, and later devised additional shares of stock in C to F through a will.

On May 26, 1969, F held less than percent of the stock holdings in C, and disqualified persons with respect to F had combined stock holdings in C greater than percent. F has at all times since May 26, 1969, held less than percent of C's outstanding stock. Disqualified persons with respect to F have at all times held more than percent of the voting stock.

P, a limited liability company, was created as a single-member LLC, wholly owned by C, and disregarded for federal income tax purposes. The directors of C declared a distribution of the membership units owned in P. One P membership unit was distributed to the owner of each share of C common stock. All persons receiving an interest in P were required to sign the operating agreement that includes substantial restrictions on transfers of the membership units. Among the restrictions is the requirement that units may be transferred only if an equivalent number of shares in C are transferred to the same transferee. P is now taxed as a partnership for federal income tax purposes.

F's holdings in P's membership units represent less than two percent of the total value of all outstanding membership units. Disqualified persons own more than percent of the voting membership units in P. Therefore, P is also a disqualified person with respect to F.

C proposes to purchase up to the total number of shares of unrestricted non-voting common stock owned by F from F and from all other shareholders who wish to participate, and P proposes to purchase the same number of membership units held by the same entities and individuals. An independent appraiser will establish the fair market value as of a designated valuation date. F has represented that will sell its stock in C and membership shares in P for no less than fair market value. The proceeds will be used to increase the amount of qualifying grants that F makes.

LAW

Section 501(c)(3) of the Code exempts from federal income tax corporations organized and operated exclusively for charitable, educational, and other purposes, provided that no part of the net earnings inure to the benefit of any private shareholder or individual.

Section 509(a) of the Code defines "private foundation" as an organization described in section 501(c)(3), other than:

1. an organization described in section 170(b)(1)(A), other than in clauses (vii) and (viii);
2. an organization which normally receives more than one-third of its support from enumerated public sources and normally receives not more than one-third of it support from gross investment income and unrelated business taxable income;
3. an organization which is organized and operated exclusively for the benefit of or to carry out the purposes of one or more specified organizations described in paragraph 1 or 2; and
4. an organization which is organized and operated exclusively for testing for public safety.

Section 4940(d)(3)(B) of the Code defines "disqualified individual" with respect to any private foundation as an individual who is—

(i) a substantial contributor to the foundation,
(ii) an owner of more than 20 percent of the total combined voting power of a corporation which is a substantial contributor to the foundation, or
(iii) a member of the family of any individual described above.

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

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

Section 4941(d)(2)(F) of the Code provides an exception to the self-dealing rule by which any transaction between a private foundation and a corporation that is a disqualified person, pursuant to a liquidation, merger, redemption, recapitalization, or other corporate adjustment shall not be considered an act of self-dealing if all of the securities of the same class as that held by the foundation are subject to the same terms and the foundation receives no less than fair market value.

Section 4946(a)(1)(C) of the Code defines "disqualified person", in pertinent part, as an owner of more than 20 percent of the total combined voting power of a corporation which is a substantial contributor to the foundation.

Section 53.4941(d)-4(b)(3) of the Foundation and Similar Excise Tax Regulations provides that property acquired by a foundation under the terms of a will executed on or before May 26, 1969 is deemed to be owned by the private foundation on May 26, 1969.

Section 53.4941(d)-3(d)(1) of the regulations provides that all of the securities in a transaction taking advantage of the exception in section 4941(d)(2)(F) of the Code are not considered "subject to the same terms" unless the corporation makes a bona fide offer on a uniform basis to the private foundation and every other person who holds such securities.

ANALYSIS

Pursuant to section 4946(a)(1)(C) of the Code, C is a disqualified person with respect to F because disqualified persons with respect to F have at all times held more than 50 percent of the voting stock of C. Generally, section 4941 imposes a tax on each act of self-dealing between a disqualified person and a private foundation. However, section 4941(d)(2)(F) provides an exception to the imposition of tax on self-dealing between a private foundation and a corporation which is a disqualified person with respect to the foundation. This section allows sales of securities to a corporation pursuant to a corporate adjustment, if all of the securities of the same class as those held by the foundation are subject to the same terms and such terms provide for receipt by the foundation of no less than fair market value. The regulations add the requirement, in section 53.4941(d)-3(d)(1) of the regulations, that the corporation must make a bona fide offer on a uniform basis to the foundation and every other person who holds such securities. We believe that in some situations these stated provisions provide guidance in the disposition of a private foundation's interests in partnership situations.

F proposes a sale of one class of the securities that it owns in the corporation. It represents that an identical bona fide offer will be made to all owners of non-voting common shares and derivative non-voting membership units. The purchase price will not be less than fair market value and will be based upon an appraisal by a qualified independent appraiser.

RULING

Therefore, based on the facts and representations stated above, we rule that F's sale of a class of stock to C and F's sale of a class of membership units in P to C will not constitute acts of self-dealing under section 4941 of the Code.

This ruling is based on the understanding that there will be no material changes in the facts upon which it is based.

Except as we have ruled above, we express no opinion as to the tax consequences of the transaction under the cited provisions of the Code or under any other provisions of the Code. We express no opinion as to future activities that F may undertake.

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

Because this letter could help resolve future tax questions, you should keep a copy of this ruling in your permanent records. A copy of this ruling is being forwarded to the Ohio TE/GE Customer Service office.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

(signed) Marvin Friedlander

Marvin Friedlander
Acting Manager, Exempt Organizations
Technical Group 2