DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
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TAX EXEMPT AND
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Contact Person:

Contact's Identification Number:

Telephone Number :

Legend:
C =
F =
x =

Dear :

This is in reply to corporation C's letter, requesting a ruling that C's redemption of private foundation F's common stock in C will not be an act of self-dealing under section 4941 of the Internal Revenue Code.

C is a for-profit corporation and is a disqualified person under section 4946 of the Code with respect to private foundation F. C's assets consist entirely of publicly listed securities, and all of its gross income is from passive sources (dividends, interest, and sale of securities).

F is a nonprofit charitable corporation that is exempt from federal income tax under section 501(c)(3) of the Code and is a private foundation under section 509(a) of the Code. F, together with other disqualified persons, effectively controls C.

Under the proposed transaction, C will pay in cash to F the fair market value of F's common stock in C. C is the only one of the four common shareholders accepting the redemption offer; the others have declined because they would incur large taxes from capital gains. C has agreed to value the stock on the basis of market quotations on the securities held by C, and to redeem the stock within one month of the valuation. The value of F's shares will not be discounted for lack of marketability or for F's minority ownership status.

The following ruling is requested: C's redemption of F's x shares of stock in C will not constitute an act of self-dealing under section 4941 of the Code.

Section 501(c)(3) of the Code provides for the exemption from federal income tax of nonprofit organizations organized and operated exclusively for the charitable and/or other exempt purposes stated in that section.

Section 509(a) of the Code describes organizations exempt from federal income tax under section 501(c)(3) that are private foundations subject to the provisions of Chapter 42.

Section 4941(a)(1) of the Code imposes an excise tax on any act of self-dealing between a private foundation and a disqualified person as defined in section 4946.

Section 4941(d)(1)(A) of the Code provides, in pertinent part, that the term "self-dealing" means any direct or indirect sale of property between a private foundation and a disqualified person as defined in section 4946.

Section 53.4941(d)-1 of the Foundation and Similar Excise Tax Regulations provides that an act of self-dealing can be a direct or indirect transaction, and it is immaterial whether the transaction results in a benefit to the private foundation.

Section 4941(d)(2)(F) of the Code provides that a stock redemption transaction between a private foundation and a corporation that is a disqualified person as defined in section 4946 is not an act of self-dealing under section 4941 of the Code if all of the securities of the same class as that held by the private foundation are subject to the same terms and such terms provided for the receipt by the private foundation of no less than fair market value.

Section 53.4941(d)-3(d) of the regulations provides that a stock redemption between a private foundation and a corporation which is a disqualified person will not be an act of self-dealing if such transaction is engaged in pursuant to a redemption, recapitalization, or other corporate adjustment, so long as all the securities of the same class as that held (prior to such transaction) by the private foundation are subject to the same terms, and such terms provide for receipt by the foundation of no less than fair market value. Further, all of the securities are not “subject to the same terms” unless, pursuant to such transaction, the corporation makes a bona fide offer on a uniform basis to the foundation and every other person who holds such securities. The fact that a private foundation receives property, such as debentures, while all other persons holding securities of the same class receive cash for their interests, will be evidence that such offer was not made on a uniform basis. This may apply even if no other person holds any securities of the class held by the foundation. In such event, however, the consideration received by holders of other classes of securities, or the interests retained by holders of such other classes, when considered in relation to the consideration received by the foundation, must indicate that the private foundation received at least as favorable treatment in relation to its interests as the holders of any other class of securities. In addition, the foundation must receive no less than the fair market value of its interests.

Section 53.4941(e)-1(f) of the regulations provides that fair market value shall be determined pursuant to the provisions of section 53.4942(a)-2(c)(4).

Section 53.4942(a)-2(c)(4) of the regulations sets forth one rule (53.4942(a)-2(c)(4)(i)) for securities (including stocks) for which market quotations are readily available, and another rule (53.4942(a)-2(c)(4)(iv)) for other securities. The latter rule provides for annual valuation (within the tax year of the foundation), with the following exception:

> If, however, a private foundation owns voting stock of an issuer of unlisted securities and has, or together with disqualified persons or another private foundation has, effective control of the issuer (within the meaning of Sec. 53.4943-3(b)(3)(ii)), then to the extent that the issuer's assets consist of shares of listed securities issues, such assets shall be valued monthly on the basis of market quotations or in accordance with section 4942(e)(2)(B), if applicable. Thus, for example, if a private foundation and a disqualified person together own all of the unlisted voting stock of a holding company which in turn holds a portfolio of securities of issues which are listed on the New York Stock Exchange, in determining the net worth of the holding company, the underlying portfolio securities are to be valued monthly by reference to market quotations for their issues unless a decrease in such value is authorized in accordance with section 4942(e)(2)(b). Such determination may be made by employees of the private foundation or by any other person, without regard to whether such person is a disqualified person with respect to the foundation.

Section 4946 of the Code defines the disqualified persons subject to section 4941.

Section 4946(a)(1)(E) of the Code provides that a disqualified person includes a corporation in which certain persons as described in section 4946(a)(1) of the Code own more than 35 percent of the profits interest.

Deluxe Corporation v. United States, 885 F.2d 848 (Court of Appeals for the Federal Circuit, September 12, 1989), concerns a redemption under section 4941(d)(2)(F) of the Code and emphasizes that a private foundation must receive fair market value for its stock redeemed.

In this case, C will pay F the full fair market value of F's x shares of common stock in C. It is represented that the fair market value here is objectively determinable by the use of quotes for the publicly traded securities and cash-type investments that are the property of C to which the common stock is tied. The valuation will occur within a month of the redemption, as required by section 53.4942(a)-2(c)(4) of the regulations under the circumstances.

Accordingly, we rule, as you have requested, that C's redemption F's x shares of stock in C will not constitute an act of self-dealing under section 4941 of the Code.

Because this ruling letter could help to resolve any questions, please keep it in your permanent records.

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

Sincerely,

Jane Baniewicz
Manager, Exempt Organizations
Technical Group 2