

assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because the regulation does not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, these regulations have been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business, and no comments were received.

#### Drafting Information

The principal author of these final regulations is Michala Irons, Office of the Associate Chief Counsel (Passthroughs and Special Industries). However, other personnel from the Treasury Department and the IRS participated in their development.

#### List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

#### Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

### PART 1—INCOME TAXES

■ **Paragraph 1.** The authority citation for part 1 continues to read in part as follows:

**Authority:** 26 U.S.C. 7805 \* \* \*

■ **Par. 2.** Section 1.704–1(b)(2)(iii)(e) is revised to read as follows:

#### § 1.704–1 Partner's distributive share.

\* \* \* \* \*

- (b) \* \* \*  
(2) \* \* \*  
(iii) \* \* \*

(e) *De minimis rule*—(1) *Partnership taxable years beginning after May 19, 2008 and beginning before December 28, 2012.* Except as provided in paragraph (b)(2)(iii)(e)(2) of this section, for purposes of applying this paragraph (b)(2)(iii), for partnership taxable years beginning after May 19, 2008 and beginning before December 28, 2012, the tax attributes of de minimis partners need not be taken into account. For purposes of this paragraph (b)(2)(iii)(e)(1), a de minimis partner is any partner, including a look-through entity that owns, directly or indirectly, less than 10 percent of the capital and profits of a partnership, and who is allocated less than 10 percent of each partnership item of income, gain, loss, deduction, and credit. See paragraph

(b)(2)(iii)(d)(6) of this section for the definition of indirect ownership.

(2) *Nonapplicability of de minimis rule.* (i) *Allocations that become part of the partnership agreement on or after December 28, 2012.* Paragraph (b)(2)(iii)(e)(1) of this section does not apply to allocations that become part of the partnership agreement on or after December 28, 2012.

(ii) *Retest for allocations that become part of the partnership agreement prior to December 28, 2012.* If the de minimis partner rule of paragraph (b)(2)(iii)(e)(1) of this section was relied upon in testing the substantiality of allocations that became part of the partnership agreement before December 28, 2012, such allocations must be retested on the first day of the first partnership taxable year beginning on or after December 28, 2012, without regard to paragraph (b)(2)(iii)(e)(1) of this section.

**Steven T. Miller**

*Deputy Commissioner for Services and Enforcement.*

Approved: December 19, 2012.

**Mark J. Mazur,**

*Assistant Secretary of the Treasury (Tax Policy).*

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### DEPARTMENT OF THE TREASURY

#### Internal Revenue Service

#### 26 CFR Parts 1, 53, and 602

[TD 9605]

RIN 1545–BG31; 1545–BL38

#### Payout Requirements for Type III Supporting Organizations That Are Not Functionally Integrated

**AGENCY:** Internal Revenue Service (IRS), Treasury.

**ACTION:** Final and temporary regulations.

**SUMMARY:** This document contains both final regulations and temporary regulations regarding the requirements to qualify as a Type III supporting organization that is operated in connection with one or more supported organizations. The regulations reflect changes to the law made by the Pension Protection Act of 2006. The regulations will affect Type III supporting organizations and their supported organizations. The text of the temporary regulations also serves as the text of the proposed regulations set forth in the Proposed Rules section in this issue of the **Federal Register**.

**DATES:** *Effective Date:* These regulations are effective on December 28, 2012.

**FOR FURTHER INFORMATION CONTACT:** Preston J. Quesenberry at (202) 622–6070 (not a toll-free number).

#### SUPPLEMENTARY INFORMATION:

#### Paperwork Reduction Act

The collection of information contained in the final regulations has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)) under control number 1545–2157. The collection of information in the final regulations is in § 1.509(a)–4(i)(2) and § 1.509(a)–4(i)(6)(v). The collection of information under § 1.509(a)–4(i)(2) flows from section 509(f)(1)(A) of the Internal Revenue Code (Code), which requires a Type III supporting organization to provide to each of its supported organizations such information as the Secretary may require to ensure that the Type III supporting organization is responsive to the needs or demands of its supported organization(s). The collection of information under § 1.509(a)–4(i)(6)(v) is required only if a Type III supporting organization that is not functionally integrated wishes for certain amounts set aside for a specific project to count toward the distribution requirement imposed by § 1.509(a)–4(i)(5)(ii). The likely recordkeepers are Type III supporting organizations and certain of their supported organizations.

*Estimated total annual reporting burden:* 15,122 hours.

*Estimated average annual burden hours per recordkeeper:* 2 hours.

*Estimated number of recordkeepers:* 7,556.

*Estimated frequency of collection of such information:* Annual.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number assigned by the Office of Management and Budget.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and return information are confidential, as required by 26 U.S.C. 6103.

#### Background

This document contains amendments to the Income Tax Regulations (26 CFR part 1) and Foundation Excise Tax Regulations (26 CFR part 53) regarding organizations described in section

509(a)(3) of the Code. An organization described in section 501(c)(3) of the Code is classified as either a private foundation or a public charity. To be classified as a public charity, an organization must meet the requirements of section 509(a)(1), (2), (3), or (4). Organizations described in section 509(a)(3) are known as supporting organizations. Supporting organizations achieve their public charity status by providing support to one or more organizations described in section 509(a)(1) or (2), which in this context are referred to as supported organizations.

To meet the requirements of section 509(a)(3), an organization must satisfy an organizational test, an operational test, a relationship test, and a disqualified person control test. The organizational and operational tests require that the supporting organization be organized and at all times thereafter operated exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more supported organizations. The relationship test requires the supporting organization to establish one of three types of relationships with one or more supported organizations. Finally, the disqualified person control test requires that the supporting organization not be controlled directly or indirectly by certain disqualified persons. Although each of these tests is a necessary requirement for an organization to establish that it qualifies as a supporting organization, these final regulations and temporary regulations focus primarily on one of the relationship tests: the test for supporting organizations that are “operated in connection with” their supported organization(s), otherwise known as “Type III” supporting organizations. Specifically, the temporary regulations address the amount that Type III supporting organizations that are not “functionally integrated” must annually distribute and explain how assets are valued for purposes of this distribution requirement. The final regulations describe all of the other requirements of the relationship test for Type III supporting organizations.

### 1. Three Types of Supporting Organizations

To meet the requirements of section 509(a)(3), a supporting organization must satisfy one of three relationship tests with respect to its supported organization(s). A supporting organization that is operated, supervised or controlled by one or more supported organizations is commonly known as a Type I supporting organization. The

relationship of a Type I supporting organization with its supported organization(s) is comparable to that of a corporate parent-subsidiary relationship. A supporting organization that is supervised or controlled in connection with one or more supported organizations is commonly known as a Type II supporting organization. The relationship of a Type II supporting organization with its supported organization(s) involves common supervision or control by the persons supervising or controlling both the supporting organization and the supported organizations. A supporting organization that is operated in connection with one or more supported organizations is commonly known as a Type III supporting organization.

### 2. Qualification Requirements for Type III Supporting Organizations Prior to Enactment of the Pension Protection Act of 2006

Prior to the enactment of the Pension Protection Act of 2006, Public Law 109–280 (120 Stat. 780 (2006)) (PPA), the regulations under section 509(a)(3) (hereinafter referred to as the “existing” regulations) generally provided that an organization is “operated in connection with” one or more supported organizations if it meets a “responsiveness test” and an “integral part test.”

#### a. Responsiveness Test

Existing § 1.509(a)–4(i)(2)(i) provides that an organization meets the responsiveness test if the organization is responsive to the needs or demands of its supported organizations. Existing § 1.509(a)–4(i)(2)(ii) (hereinafter referred to as the “significant voice responsiveness test”) provides that a supporting organization can demonstrate responsiveness to a supported organization if the relationship between the supporting and supported organization meets one of the following three criteria: (1) The supported organization appoints or elects one or more of the officers, directors, or trustees of the supporting organization; (2) one or more members of the governing body of the supported organization serve as officers, directors, or trustees of, or hold other important offices in, the supporting organization; or (3) the officers, directors, or trustees of the supporting organization maintain a close continuous working relationship with the officers, directors, or trustees of the supported organization. In addition, as a result of one of these three criteria being satisfied, the supported organization has to have a “significant voice” in the investment policies of the

supporting organization, the timing and the manner of making grants, the selection of the grant recipients of the supporting organization, and in otherwise directing the use of the income or assets of the supporting organization.

The existing regulations also provide an alternative means for charitable trusts to satisfy the responsiveness test. Under existing § 1.509(a)–4(i)(2)(iii), a supporting organization is responsive if: (1) It is a charitable trust under State law; (2) each specified supported organization is a named beneficiary under the charitable trust’s governing instrument; and (3) each beneficiary organization has the power to enforce the trust and compel an accounting under State law.

In the case of an organization that is supporting one or more supported organizations before November 20, 1970, existing § 1.509(a)–4(i)(1)(ii) provides that additional facts and circumstances, such as a historic and continuing relationship between the supporting organization and its supported organization(s), also can be taken into account to establish compliance with the responsiveness test.

#### b. Integral Part Test

The integral part test under existing § 1.509(a)–4(i)(3)(i) requires a supporting organization to maintain a significant involvement in the operations of one or more supported organizations that are dependent upon the supporting organization for the type of support that it provides. Under the existing regulations, there are two alternative ways to meet the integral part test: (1) the “but for” test under existing § 1.509(a)–4(i)(3)(ii); or (2) the payout test under existing § 1.509(a)–4(i)(3)(iii).

Under existing § 1.509(a)–4(i)(3)(ii), the “but for” test is satisfied if the activities engaged in by the supporting organization for or on behalf of the supported organizations are activities to perform the functions of, or to carry out the purposes of, such organizations, and, but for the involvement of the supporting organization, would normally be engaged in by the supported organizations themselves.

The payout test under existing § 1.509(a)–4(i)(3)(iii) requires a supporting organization to: (1) Make payments of substantially all of its income to or for the use of one or more supported organizations; (2) provide enough support to one or more supported organizations to ensure the attentiveness of such organization(s) to the operations of the supporting

organization; and (3) pay a substantial amount of the total support of the supporting organization to those supported organizations that meet the attentiveness requirement. The phrase “substantially all of its income” in existing § 1.509(a)–4(i)(3)(iii) has been interpreted to mean at least 85 percent of adjusted net income. See Rev. Rul. 76–208, 1976–1 CB 161.

### 3. PPA Changes to Qualification Requirements for Type III Supporting Organizations

The PPA made five changes to the requirements an organization must meet to qualify as a Type III supporting organization:

(1) It removed the ability to rely solely on the alternative test for charitable trusts as a means of meeting the responsiveness test;

(2) To ensure that a “significant amount” is paid to supported organizations, it directed the Secretary of the Treasury to establish a new payout requirement for Type III supporting organizations that are not “functionally integrated” (with the term “functionally integrated” referring to Type III supporting organizations that are not required to meet a payout requirement due to their activities related to performing the functions of, or carrying out the purposes of, their supported organization(s));

(3) It required a Type III supporting organization to annually provide to each of its supported organizations such information as the Secretary may require to ensure that the supporting organization is responsive to the needs or demands of its supported organization(s);

(4) It prohibited a Type III supporting organization from supporting any supported organization not organized in the United States; and

(5) It prohibited a Type I or Type III supporting organization from accepting a gift or contribution from a person who, alone or together with certain related persons, directly or indirectly controls the governing body of a supported organization of the Type I or Type III supporting organization.

### 4. Advanced Notice of Proposed Rulemaking

On August 2, 2007, the Treasury Department and the IRS published in the **Federal Register** (72 FR 42335) an advanced notice of proposed rulemaking (ANPRM) (REG–155929–06). The ANPRM described proposed rules to implement the PPA changes to the Type III supporting organization requirements and solicited comments regarding those proposed rules. Forty

comments were received in response to the ANPRM and were considered in drafting the notice of proposed rulemaking and these final and temporary regulations. No public hearing was requested or held.

### 5. Notice of Proposed Rulemaking

On September 24, 2009, the Treasury Department and the IRS published in the **Federal Register** (74 FR 48672) a notice of proposed rulemaking (NPRM) (REG–155929–06). The NPRM contained proposed regulations (the “2009 proposed regulations”) setting forth the requirements to qualify as a Type III supporting organization under the PPA. The IRS received more than 30 comments in response to the NPRM. These comments were considered in drafting these final and temporary regulations and are available for public inspection at [www.regulations.gov](http://www.regulations.gov) or upon request. No public hearing was requested or held.

After reviewing all comments received, the Treasury Department and the IRS believe that certain topics require further consideration. The Treasury Department and the IRS will continue to study these topics and will request comments on these topics in a separate notice of proposed rulemaking. Nonetheless, the Treasury Department and the IRS believe that immediate effective guidance is needed for Type III supporting organizations. Accordingly, the Treasury Department and the IRS are issuing both final regulations and temporary regulations. The provisions in the 2009 proposed regulations regarding the amount that non-functionally integrated Type III supporting organizations must annually distribute have been significantly revised in response to comments. As a result, these provisions (as well as provisions related to how assets are valued for purposes of this distribution requirement) are being issued as temporary and proposed regulations, to permit additional opportunity for comment. The other provisions of the 2009 proposed regulations are being issued as final regulations, which are substantially similar to the 2009 proposed regulations but reflect certain revisions that were made based on comments received. The comments and revisions are discussed in the following section.

### Explanation of Provisions and Summary of Comments

Based largely on comments received from commenters, the final and temporary regulations make revisions to various provisions in the 2009 proposed regulations, including (1) the definition

of “supported organization” in § 1.509(a)–4(a)(6); (2) the prohibition on receiving gifts or contributions from persons that control the governing body of a supported organization set forth in § 1.509(a)–4(f)(5); (3) the notification requirement set forth in § 1.509(a)–4(i)(2); (4) the responsiveness test set forth in § 1.509(a)–4(i)(3); (5) the requirements to qualify as a functionally integrated Type III supporting organization set forth in § 1.509(a)–4(i)(4); (6) the requirements to qualify as a non-functionally integrated (NFI) Type III supporting organization set forth in § 1.509(a)–4(i)(5); and (7) the transition rules provided in § 1.509(a)–4(i)(11).

### 1. Definition of Supported Organization

Section 1.509(a)–4(a)(5) defines a “publicly supported organization” as “an organization described in section 509(a)(1) or (2).” This defined term is used throughout § 1.509(a)–4. The 2009 proposed regulations proposed removing the term “publicly supported organization” wherever it appears in § 1.509(a)–4 and replacing it with a new defined term, “supported organization.” The new defined term “supported organization” was narrower than the term “publicly supported organization” because it was limited to those organizations described in section 509(a)(1) or (2) that the supporting organization was organized and operated to support. As a result, the new defined term does not necessarily work in every instance in § 1.509(a)–4 in which the term “publicly supported organization” is used. Accordingly, the final regulations maintain the term “publicly supported organization” and continue to use it in every paragraph of § 1.509(a)–4 other than § 1.509(a)–4(i).

The final regulations also revise the definition of “supported organization” in the 2009 proposed regulations and apply the term only in newly amended § 1.509(a)–4(i). While the definition of supported organization provided in the 2009 proposed regulations tracked the language of section 509(f)(3), the final regulations clarify the definition of supported organization by cross-referencing the previously-existing § 1.509(a)–4(d)(4) and § 1.509(a)–4(d)(2)(iv). Thus, for purposes of § 1.509(a)–4(i), a supported organization of a Type III supporting organization is defined as any publicly supported organization designated by name in the supporting organization’s articles of organization. In addition, a supported organization of a Type III supporting organization can include a publicly supported organization that is not designated by name in the supporting organization’s articles if there has been

a historic and continuing relationship between the supporting organization and the publicly supported organization and, by reason of such relationship, there has developed a substantial identity of interests between such organizations.

## 2. Gifts From Controlling Donors

Like the 2009 proposed regulations, the final regulations prohibit a Type I or Type III supporting organization from accepting a gift or contribution from a person who, alone or together with certain related persons, directly or indirectly controls the governing body of a supported organization of the Type I or Type III supporting organization, or from persons related to a person possessing such control. For these purposes, related persons include family members and 35-percent controlled entities within the meaning of section 4958(f).

One commenter requested a definition of "control" for purposes of this provision. The Treasury Department and the IRS agree that a definition of "control" for these purposes would be beneficial and intend to issue proposed regulations in the near future that will provide such a definition.

## 3. Requirement To Notify Supported Organizations

Like the 2009 proposed regulations, these final regulations require that, for each taxable year, a Type III supporting organization must provide to each of its supported organizations: (1) A written notice addressed to a principal officer of the supported organization describing the amount and type of support provided to the supported organization; (2) a copy of the supporting organization's most recently filed Form 990, "Return of Organization Exempt from Income Tax," or other annual information return required to be filed under section 6033; and (3) a copy of the supporting organization's governing documents, including any amendments. The required notification documents must be postmarked or electronically transmitted by the last day of the fifth calendar month following the close of the supporting organization's taxable year.

Several commenters suggested that the due date for the required notification be amended to correspond to the Form 990 due date, with extensions. Alternatively, some commenters requested clarification that the "most recently filed Form 990" can be a Form 990 filed in a prior year.

The Form 990 is due by the 15th day of the fifth calendar month following the close of the filing organization's

taxable year. However, an organization required to file a Form 990 can request two three-month extensions (the first of which is granted automatically) by filing a Form 8868, "Application for Extension of Time to File an Exempt Organization Return." As a result, if the due date for the required notification were the same as the Form 990 due date, with extensions, a supported organization might not receive its notification from a supporting organization until almost a year after the close of the supporting organization's preceding taxable year. In such cases, a supported organization would have little or no opportunity to use the information in the notification to make recommendations regarding the amount and type of support it wishes to receive from the supporting organization during the taxable year it receives the notification. In addition, if the due date for the notification were the same as the due date for the Form 990, with extensions, a supported organization would not know when to expect or request a notification from a supporting organization unless it knew whether or not a supporting organization requested extensions in any given year. For these reasons, the final regulations retain the due date of the last day of the fifth calendar month following the close of the supporting organization's taxable year.

However, the Treasury Department and the IRS agree with commenters that if an organization has not filed a Form 990 for a taxable year by the last day of the fifth calendar month following the close of the taxable year (because, for example, it has received an extension), the organization's "most recently filed" Form 990 as of that last day of the fifth calendar month is the Form 990 for the supporting organization's immediately preceding taxable year. As a result, the final regulations clarify the relationship between the filing date of the Form 990 and the date notification is provided by referring to the Form 990 "that was most recently filed as of the date the notification is provided" rather than simply the "most recently filed Form 990." Thus, for example, if a Type III supporting organization reporting on a calendar year basis has not filed its 2013 Form 990 by May 31, 2014, because it requested an extension, it can satisfy the Form 990 portion of its notification requirement for 2013 (which it needs to meet by May 31, 2014) by providing a copy of the 2012 Form 990 that it filed in 2013.

In addition, the Treasury Department and the IRS recognize that some Type III supporting organizations that request extensions to file their Forms 990 may

need additional time to prepare their first notification. As a result, as described further in section 8.a. of this preamble, the final regulations provide transition relief for supporting organizations in existence on the effective date of these final and temporary regulations under which the due date for a Type III supporting organization's first required notification is the later of the last day of the fifth calendar month following the close of the supporting organization's taxable year or the due date for the Form 990 for that taxable year, including extensions.

One commenter requested clarification that the required written notice must describe the amount and type of support the supporting organization provided to the supported organization in the supporting organization's "immediately preceding taxable year," rather than "in the past year," as provided in the 2009 proposed regulations. The final regulations clarify that the written notice must describe the support provided in the supporting organization's taxable year ending immediately before the taxable year in which the written notice is provided. Thus, for example, if a Type III supporting organization operating on a calendar year provided the required notification for 2013 on May 31, 2014, the written notice would describe the support the supporting organization provided in 2013.

Another commenter stated that the term "principal officer" as used in the 2009 proposed regulations is ambiguous and requested that the regulations expressly designate the treasurer or chief financial officer (CFO) as the principal officer to whom notification should be given. The final regulations make clear that a person who, regardless of title, has ultimate responsibility for managing the finances of a supported organization (which could include a CFO or treasurer) can be a principal officer of that organization for purposes of the notification requirement. In addition, the final regulations provide that a principal officer can include a person who, regardless of title, has ultimate responsibility for implementing the decisions of the supported organization's governing body or for supervising the management, administration, or operation of the supported organization.

One commenter recommended that a supporting organization be permitted to send the required written notice to the supported organization's general address rather than to its principal officer. The Treasury Department and the IRS have concluded that the

notification should be sent to a principal officer of the supported organization to ensure receipt by a person with sufficient responsibility over the organization. Accordingly, the final and temporary regulations do not adopt this comment.

The same commenter asked that supporting organizations be allowed to satisfy the notification requirement by sending supported organizations an internet link to the Form 990. Like the 2009 proposed regulations, the final regulations provide that the notification requirement may be satisfied by electronic media, which can include a working internet link. However, because all components of the notification requirement must be satisfied, providing only an internet link to the Form 990 would not be sufficient.

One commenter recommended that a Type III supporting organization that is included in a group exemption and supports not only the central organization in the group exemption but also the other subordinate organizations that are part of the group exemption should only be required to provide notice to the central organization, not to all of the other subordinate organizations. Another commenter stated that notification is unnecessary if the principal officer of the supported organization is also the principal officer of the supporting organization. Because section 509(f)(1)(A) of the Code provides that Type III supporting organizations must provide the required notification "to each supported organization," the Treasury Department and the IRS have concluded that a Type III supporting organization must provide notice to all of the organizations it is organized to support. Accordingly, the final and temporary regulations do not adopt these comments.

Finally, because section 6104(d)(3)(A) of the Code and § 301.6104(d)-1(b)(4)(ii) except the name and address of contributors from the general requirement that tax-exempt organizations disclose their annual information returns, the final regulations clarify that a supporting organization may redact the name and address of any contributor to the organization from the Form 990 (or other annual information return) it is required to provide to the supported organization(s) as part of the notification requirement.

#### 4. Responsiveness Test

Like the 2009 proposed regulations, in implementing section 1241(c) of the PPA, the final regulations remove the alternative responsiveness test for charitable trusts contained in existing

§ 1.509(a)-4(i)(2)(iii). Accordingly, the final regulations provide that all Type III supporting organizations must satisfy the "significant voice" responsiveness test by (1) demonstrating one of three necessary relationships between their officers, directors, or trustees and those of their supported organization(s), and (2) showing that this relationship results in the officers, directors, or trustees of the supported organization having a significant voice in directing the use of the income and assets of the supporting organization.

Numerous commenters suggested that *Example 1* of § 1.509(a)-4(i)(3)(iv) of the 2009 proposed regulations, which illustrates how a charitable trust may satisfy the significant voice responsiveness test, imposes too onerous of a requirement for meeting the responsiveness test by describing "quarterly face-to-face meetings" between a bank trustee's representative and an officer of the supported organization. However, *Example 1* does not impose specific requirements on charitable trusts seeking to satisfy the responsiveness test; rather, the example merely illustrates one way the officers, directors, or trustees of a supported organization could maintain a close and continuous relationship with the officers, directors, or trustees of a supporting organization organized as a trust and thereby have a significant voice in directing the use of the income or assets of that supporting organization. In order to better illustrate options for satisfying the significant voice responsiveness test, *Example 1* has been amended in the final regulations to refer to "quarterly face-to-face or telephonic meetings" rather than only face-to-face meetings. As a general matter, the Treasury Department and the IRS anticipate that charitable trusts will be able to demonstrate that they satisfy the responsiveness test in a variety of ways, and whether a supported organization has a close and continuous relationship with, or a significant voice in directing the use of the income or assets of, a supporting organization will be determined based on all the relevant facts and circumstances.

A few commenters requested additional examples of how Type III supporting organizations can satisfy the responsiveness test. The final and temporary regulations do not provide any such additional examples, but these comments will continue to be considered. The Treasury Department and the IRS intend to issue proposed regulations in the near future that amend the responsiveness test by clarifying that Type III supporting organizations must be responsive to all

of their supported organizations. In the preamble to those proposed regulations, the Treasury Department and the IRS intend to request additional comments regarding examples of how to satisfy the responsiveness test.

Several commenters requested clarification that the responsiveness test does not require a supporting organization to follow all of the directions or recommendations of a supported organization's officers, directors, or trustees and that the latter's role can be only advisory. The Treasury Department and the IRS have concluded that the term "significant voice" makes clear that the responsiveness test requires only that the officers, directors, or trustees of a supported organization have the ability to influence the supporting organization's decisions regarding the supporting organization's use of its income or assets—not that the officers, directors, or trustees of the supported organization have control over such decisions.

One commenter noted that some trust instruments specify the recipients, timing, manner, and amount of grants and requested that the regulations provide that a supported organization can still be deemed to have a significant voice over these matters if its supporting organization has such a governing instrument. The Treasury Department and the IRS are continuing to consider the best approach for supporting organizations with such trust instruments and intend to issue proposed regulations in the near future that will provide further clarification on this issue.

Finally, the 2009 proposed regulations stated that a supporting organization is responsive to the needs or demands of a supported organization if it satisfies the requirements of § 1.509(a)-4(i)(3)(ii) and (iii). In order to conform more closely to existing § 1.509(a)-4(i)(2)(i), the final regulations amend this language to state that a supporting organization must satisfy the requirements of § 1.509(a)-4(i)(3)(ii) and (iii) in order to satisfy the responsiveness test.

#### 5. Integral Part Test—Functionally Integrated Type III Supporting Organizations

Like the 2009 proposed regulations, the final regulations provide that a Type III supporting organization is functionally integrated, and thus not subject to a distribution requirement, if it either: (1) Engages in activities substantially all of which directly further the exempt purposes of the supported organization(s) to which it is responsive by performing the functions

of, or carrying out the purposes of, such supported organization(s) and which, but for the involvement of the supporting organization, would normally be engaged in by the supported organization(s); or (2) is the parent of each of its supported organizations. In addition, the final regulations reserve a provision for a special rule for supporting organizations that support a governmental supported organization.

**a. Substantially All Activities Directly Further the Exempt Purposes of Supported Organizations**

With respect to the test to qualify as functionally integrated by engaging in activities substantially all of which directly further the exempt purposes of the supported organization(s), one commenter recommended that the term “directly further the exempt purposes” be defined with reference to the phrase “directly for the active conduct of activities constituting” the exempt purposes, as used in the definition of a private operating foundation under section 4942(j)(3) and the accompanying regulations at § 53.4942(b)–1(b)(1). The same commenter noted that § 53.4942(b)–1(b)(2) treats certain grants, scholarships, or other payments made or awarded by a private operating foundation to individual beneficiaries as qualifying distributions made directly for the active conduct of exempt activities as long as those payments are to support active programs in which the operating foundation maintains significant involvement. This commenter recommended that similar grants, scholarships, or other payments made or awarded by Type III supporting organizations should be treated as activities that directly further the exempt purposes of a supported organization (“direct furtherance activities”).

The Treasury Department and the IRS agree that the meaning of the phrase “directly further the exempt purposes,” as used in the functionally integrated test, is similar to the meaning of the phrase “directly for the active conduct of activities constituting” the exempt purposes, as used in the definition of a private operating foundation and as described in detail in § 53.4942(b)–1(b)(1). Consequently, in defining direct furtherance activities, the final regulations use language similar to that used in § 53.4942(b)–1(b)(1) by clarifying that direct furtherance activities are activities conducted by the supporting organization itself, rather than by a supported organization. However, most of the remaining language in § 53.4942(b)–1(b)(1) used to

define “directly for the active conduct of activities” is not used in the definition of direct furtherance activities in the final regulations because the former definition is based only on expenditures while the latter concept is based more broadly on the activities of a Type III supporting organization. As a result, the definition of direct furtherance activities in the final regulations is otherwise the same as the definition contained in the 2009 proposed regulations.

The final regulations also provide that certain payments to individual beneficiaries similar to those that would qualify as “directly for the active conduct of activities constituting” a private operating foundation’s exempt purposes under § 53.4942(b)–1(b)(2) will be treated as direct furtherance activities under the Type III supporting organization functionally integrated test. Similar to the payments to individual beneficiaries described in § 53.4942(b)–1(b)(2), the final regulations provide that making or awarding grants, scholarships, or other payments to individual beneficiaries will be treated as an activity that directly furthers the exempt purposes of a supported organization only if the making or awarding of such payments is part of an active program of the supporting organization that directly furthers the exempt purposes of the supported organization(s) and in which the supporting organization maintains significant involvement (as defined in § 53.4942(b)–1(b)(2)(ii)). However, unlike distributions directly for the active conduct of activities constituting a private operating foundation’s exempt purposes, the direct furtherance activities of a functionally integrated Type III supporting organization must directly further the exempt purposes of one or more supported organizations. As a result, the final regulations impose three additional requirements that a supporting organization’s grants, scholarships, or other payments to individual beneficiaries must satisfy in order to be considered direct furtherance activities. First, the individual beneficiaries must be members of the charitable class benefitted by a supported organization. Second, the officers, directors, or trustees of that supported organization must have a significant voice in the timing of the payments, the manner of making them, and the selection of recipients. Third, the individual beneficiaries must be selected on an objective and nondiscriminatory basis (as described in § 53.4945–4(b)).

A number of commenters suggested that fundraising, making grants, and

investing and managing non-exempt-use assets should be considered direct furtherance activities in certain situations, including those in which the supported organization (1) is a community foundation or other publicly-supported grantmaker, (2) is a religiously-affiliated entity, (3) has a close historic and continuing relationship with the supporting organization, or (4) created the supporting organization specifically to house fundraising, grantmaking, and/or investment activities. One commenter further suggested that a Type III supporting organization’s fundraising, grantmaking, and/or investment and management of non-exempt-use assets should be treated as direct furtherance activities as long as a “preponderance” of the supporting organization’s other activities otherwise directly further the supported organization’s exempt purposes. Another commenter recommended that the regulations include an exception that would treat a supporting organization as functionally integrated (or otherwise not subject to a distribution requirement) even if it engaged in grantmaking and the production of investment income as more than an insubstantial part of its activities as long as it (1) has not received any contribution from its founder or family members since 1970, (2) has no substantial contributor (or family member thereof) who is alive, and (3) has already distributed to its supported organization(s), in the aggregate, an amount equal to the amount of its donor contributions.

The Treasury Department and the IRS have determined that a Type III supporting organization should qualify as functionally integrated, and therefore not be subject to the payout requirement, if substantially all of its support for its supported organization(s) consists of charitable activities that the supporting organization itself directly carries out (as distinguished from charitable activities carried out by the supported organization(s) that the supporting organization helps finance by producing and distributing income). This is because a supporting organization that operates substantial, direct charitable programs itself may need more flexibility in structuring its annual operational budget than the annual payout requirement for NFI Type III supporting organizations would allow. The examples of activities that commenters want to be treated as direct furtherance activities or to otherwise qualify them for an exception from the distribution requirement—all of which involve producing income and

distributing a portion of it to the supported organization—are not consistent with this rationale and hence the Treasury Department and the IRS do not adopt these comments.

Commenters also requested additional guidance on how direct furtherance activities will be measured for purposes of determining whether they constitute “substantially all” of a supporting organization’s activities. A number of commenters suggested that all facts and circumstances should be considered in making this determination, including not only the supporting organization’s expenditures but also, for example, the time and effort spent by the organization’s employees and volunteers. The final regulations clarify that all pertinent facts and circumstances are considered in measuring activities for purposes of determining whether substantially all of an organization’s activities are direct furtherance activities.

One commenter stated that the example in the 2009 proposed regulations of a supporting organization that qualifies as a functionally integrated Type III supporting organization by performing publishing and printing functions for churches was not “realistic” because several churches would be unlikely to jointly establish such a publishing operation. Instead of a publishing operation, this commenter suggested that churches would be more likely to jointly establish a charitable organization that performs a social welfare function. As a result, the final regulations replace the example of a nonprofit publishing organization with an example of a nonprofit food pantry.

#### b. Being the Parent of Each Supported Organization

Like the 2009 proposed regulations, the final regulations provide that a Type III supporting organization can qualify as functionally integrated by being the parent of each supported organization. In defining “parent” for these purposes, the final regulations repeat the definition set forth in the 2009 proposed regulations and state that a supporting organization is the parent of a supporting organization if the supporting organization exercises a substantial degree of direction over the policies, programs, and activities of the supported organization, and a majority of the officers, directors, or trustees of the supported organization is appointed or elected, directly or indirectly, by the governing body, members of the governing body, or officers of the supporting organization acting in their official capacity. However, the Treasury Department and the IRS have

determined that this definition of “parent” is insufficiently specific. Consequently, the Treasury Department and the IRS intend to issue proposed regulations in the near future that will provide a new definition of parent that specifically addresses the power to remove and replace officers, directors, or trustees of the supporting organization.

#### c. Supporting a Governmental Supported Organization

The 2009 proposed regulations provided a “governmental entity exception” under which a Type III supporting organization that supports one supported organization whose assets are subject to the appropriations process of a federal, state, local, or Indian tribal government may treat grantmaking to the supported organization and investing and managing non-exempt-use assets on behalf of the supported organization as direct furtherance activities, as long as a substantial part of the supporting organization’s total activities are otherwise direct furtherance activities.

Several commenters requested that this governmental entity exception be expanded to allow supporting organizations to support more than one supported organization. For example, commenters recommended that a supporting organization be allowed to qualify for this exception if it supports (1) up to five governmental supported organizations; (2) not only a governmental entity but also other supported organizations that are responsive to, and have a substantial operational connection with, that governmental entity; or (3) a governmental system, such as a parent and subsidiary units.

The Treasury Department and the IRS are continuing to consider these comments regarding the governmental entity exception and intend to issue proposed regulations in the near future that will provide guidance on how supporting organizations can qualify as functionally integrated by supporting a governmental entity. These proposed regulations will also provide one or more examples of how a Type III supporting organization can qualify as functionally integrated by supporting a governmental entity (similar to the examples contained in the 2009 proposed regulations but omitted from these final and temporary regulations).

In the meantime, as discussed further in section 8.b. of this preamble, Type III supporting organizations can qualify as functionally integrated by meeting the requirements of the “but for” test under existing § 1.509(a)–4(i)(3)(ii) until the

first day of their second taxable year beginning after December 28, 2012. The Treasury Department and the IRS intend to release the proposed regulations on the governmental entity rule sufficiently in advance of the beginning of this second taxable year to enable Type III SOs to determine their eligibility. The Treasury Department and the IRS also anticipate that, for taxable years beginning prior to the date of issuance of the future final regulations on the governmental entity rule, Type III SOs would be permitted to rely on the governmental entity rule as stated in either the future proposed or final regulations.

#### 6. Integral Part Test—Non-Functionally Integrated Type III Supporting Organizations

##### a. Distribution Requirement

The 2009 proposed regulations provided that a NFI Type III supporting organization would have to annually distribute a “distributable amount” equal to 5 percent of the fair market value of its non-exempt-use assets. The Treasury Department and the IRS decided to base this distribution requirement on non-exempt-use assets, rather than on income, due to concerns that the income-based payout test under existing § 1.509(a)–4(i)(3)(iii) could result in little or nothing being paid to charity if the supporting organization’s assets produced little to no income.

Several commenters stated that the 5-percent payout rate in the 2009 proposed regulations would be too high and would erode a supporting organization’s assets over time on a real (inflation-adjusted) basis. A few commenters noted that private non-operating foundations must annually pay out 5 percent of their non-exempt-use assets under section 4942 of the Code but stated that NFI Type III supporting organizations should not be subject to the same payout rate as private non-operating foundations because they are distinguishable from these foundations. For example, some commenters noted that private non-operating foundations can fund any number of charitable organizations in a given year, while Type III supporting organizations are obligated to benefit designated supported organizations and also must satisfy the responsiveness and attentiveness tests with respect to these supported organizations. Commenters also noted that substantial contributors to a supporting organization (as well as certain related persons) cannot control the supporting organization, while private foundations face no such restriction. Some of these commenters



noted that lower effective payout requirements are imposed on private operating foundations and medical research organizations and recommended that similar payout requirements should apply to NFI Type III supporting organizations. Other commenters asked that the final regulations maintain the payout test under existing § 1.509(a)-4(i)(3)(iii), which requires payments of substantially all of the supporting organization's income.

The Treasury Department and the IRS recognize that NFI Type III supporting organizations face a number of requirements and restrictions that do not apply to private foundations, including the organizational, operational, and disqualified person control tests under section 509(a)(3) and the responsiveness and attentiveness test under the regulations regarding Type III supporting organizations. These requirements and restrictions should significantly reduce the likelihood that substantial contributors to a NFI Type III supporting organization will be able to use the supporting organization's assets to further their own interests. These requirements also result in a relationship between the supporting organization and the supported organizations that does not necessarily exist between private foundations and their grantees.

As a result, the Treasury Department and the IRS have determined that an asset-based payout percentage lower than the payout percentage for private non-operating foundations is justified for NFI Type III supporting organizations. At the same time, the payout test under existing § 1.509(a)-4(i)(3)(iii), which requires payments of substantially all of the supporting organization's income (with "substantially all" considered to mean 85 percent or more), has helped prevent unreasonable accumulations of income by NFI Type III supporting organizations that generate significant amounts of current income in a particular taxable year. Accordingly, the temporary regulations require NFI Type III supporting organizations to annually distribute a "distributable amount" equal to the greater of 85 percent of adjusted net income or 3.5 percent of the fair market value of the supporting organization's non-exempt-use assets. For these purposes, "adjusted net income" is determined by applying the principles of section 4942(f) and § 53.4942(a)-2(d). Because this distributable amount is significantly different than the distributable amount described in the 2009 proposed regulations, the Treasury Department

and the IRS have issued the provisions describing the distributable amount as temporary and proposed regulations to provide an opportunity for comment.

In recommending an asset-based payout percentage of less than 5 percent, a number of commenters emphasized that supporting organizations have a relationship with their supported organizations that private foundations do not have with their grantees and that this relationship helps ensure responsiveness to the needs and demands of the supported organization. The Treasury Department and the IRS considered this relationship in determining the appropriate payout rate for NFI Type III supporting organizations. Accordingly, the Treasury Department and the IRS intend to ensure that this relationship exists between a supporting organization and each of its supported organizations by proposing regulations requiring that NFI Type III supporting organizations meet the responsiveness test with respect to each of their supported organizations.

Many commenters recommended that the distributable amount be based on the average fair market value of non-exempt-use assets over the three years (as opposed to just one year) preceding the year of the required distribution, in order to reduce fluctuations in payments to the supported organization(s) from year to year and avoid significant cuts to supported organizations' budgets during downward market fluctuations. The Treasury Department and the IRS expect that the new notification requirement and the application of the "significant voice" responsiveness test to all Type III supporting organizations, including those organized as trusts, will give supported organizations the opportunity to influence the timing of payments. In addition, the Treasury Department and the IRS expect that the significantly lower payout percentage set forth in the temporary regulations should provide NFI Type III supporting organizations with additional flexibility to respond to requests from supported organizations to adjust the timing of payments to anticipate and respond to market fluctuations. Flexibility to respond to such requests from supported organizations is also made possible by the carryover rule that the final regulations adopt without change from the 2009 proposed regulations. This rule allows a Type III supporting organization that distributes more than its annual distributable amount during a taxable year to carry over that excess amount for five subsequent taxable years. Accordingly, the final and temporary regulations do not adopt the

three-year valuation period suggested by commenters and, like the 2009 proposed regulations, provide that the distributable amount is based on the fair market value of the organization's non-exempt-use assets in the immediately preceding taxable year.

One commenter asked that the reasonable cause exception to the distribution requirement be expanded to expressly include times of great financial distress. Like the 2009 proposed regulations, the final regulations allow the Secretary to provide for a temporary reduction in the annual distributable amount in the case of a disaster or emergency, which the Treasury Department and the IRS intend to include a time of great financial distress. Thus, the final and temporary regulations do not make any changes to the reasonable cause exception.

#### b. Distributions That Count Toward the Distribution Requirement

A number of commenters recommended that a NFI Type III supporting organization should, like a private foundation, be able to count toward its distribution requirement amounts set aside for specific charitable projects that accomplish the exempt purposes of one or more supported organization(s). In response to this recommendation, the final regulations provide that a supporting organization may count a set-aside toward its distribution requirement if it establishes to the satisfaction of the IRS, in a manner similar to that required of private foundations making set-asides under section 4942(g)(2)(B)(i) and the accompanying regulations, that the project is one that can be better accomplished by the set-aside than by the immediate payment of funds. In particular, the supporting organization must apply for IRS approval of the set-aside before the end of the taxable year in which the amount is set aside, establish to the satisfaction of the IRS that the amount set aside will be paid for the specific project within 60 months after it is set aside and that the project is one that can better be accomplished by the set-aside than by the immediate payment of funds, and meet the other approval and information requirements set forth in § 53.4942(a)-3(b)(7)(i). The supporting organization must also obtain a written statement from the supported organization, signed by one of the supported organization's principal officers under penalty of perjury. This written statement must confirm that the specific project accomplishes the exempt purposes of the supported organization and that the supported organization approves the



supporting organization's determination that the project is one that can be better accomplished by the set-aside than by the immediate payment of funds or distribution of assets. The final and temporary regulations do not incorporate a test similar to the "cash distribution test" for set-asides described in section 4942(g)(2)(B)(ii) and the accompanying regulations because such a test would not provide sufficient assurance that the project is one better accomplished by means of a set aside than by an immediate distribution to the supported organization.

A few commenters requested that the regulations clarify that a supporting organization will be able to count toward the distribution requirement expenditures on activities that directly further the exempt purposes of its supported organization(s). Accordingly, the final regulations provide that a NFI Type III supporting organization can count toward the distribution requirement amounts expended on activities that directly further the exempt purposes of the supported organization(s) to which the supporting organization is responsive and that, but for the involvement of the supporting organization, would normally be engaged in by the supported organization(s) (that is, that meet the requirements of § 1.509(a)-4(i)(4)(i)(A)). However, in the case of such a direct furtherance activity that generates revenue for the supporting organization, the supporting organization can only count expenditures on that activity toward its distribution requirement to the extent the expenditures exceed the revenue derived. Thus, for example, if a NFI Type III supporting organization spent \$1 million in a taxable year operating a museum that generated \$800,000 in receipts for the supporting organization during that same year, the supporting organization could only count \$200,000 of the \$1 million spent toward the distribution requirement (assuming the operation of the museum was an activity described in § 1.509(a)-4(i)(4)(i)(A)).

Like the 2009 proposed regulations, the final regulations provide that reasonable and necessary administrative expenses also count toward the distribution requirement. The final regulations clarify, however, that such expenses must be paid to accomplish the exempt purposes of the supported organization(s) and thus do not include expenses incurred in the production of investment income. The list of distributions that count toward the distribution requirement contained in § 1.509(a)-4(i)(6) is not an exhaustive

list and other distributions may count toward the distribution requirement. The Treasury Department and the IRS intend to propose regulations in the near future that will more fully describe the expenditures (including expenditures for administrative and additional charitable activities) that do and do not count toward the distribution requirement.

One commenter recommended that § 1.509(a)-4(i)(6)(i) of the 2009 proposed regulations be revised to conform to § 1.509(a)-4(i)(5)(ii) of the 2009 proposed regulations by providing that distributions made "for the use of" one or more supported organizations, as well as "to" one or more supported organizations, can count toward satisfying the distribution requirement. The commenter stated that such a conforming provision would clarify that supporting organizations have the flexibility to make payments to third parties directly "on behalf of" supported organizations. The Treasury Department and the IRS do not agree that the term "for the use of" is synonymous with "on behalf of" or that it permits grants to organizations other than the supported organizations to count toward the distribution requirement. Accordingly, the final and temporary regulations do not adopt this comment.

Several commenters recommended that program-related investments (PRIs), which count toward satisfying a private foundation's distribution requirement under section 4942, should count toward the distribution requirement of NFI Type III supporting organizations. One commenter further recommended that the value of a PRI be excluded in calculating a supporting organization's distributable amount for a taxable year. These final and temporary regulations do not specifically address whether or not PRIs may count toward the distribution requirement for NFI Type III supporting organizations or be excluded in calculating a supporting organization's distributable amount for a taxable year. The Treasury Department and IRS are continuing to consider these comments and intend to provide further clarification in future proposed regulations.

#### c. Attentiveness Requirement

Like the 2009 proposed regulations, the final regulations modify the attentiveness requirement in existing § 1.509(a)-4(i)(3)(iii) to provide that an organization must distribute one-third or more of its required, annual distributable amount to one or more supported organizations that are attentive to the supporting organization

and with respect to which the supporting organization meets the responsiveness test. Also like the 2009 proposed regulations, the final regulations provide that, to demonstrate that a supported organization is attentive, a supporting organization must: (1) Provide 10 percent or more of the supported organization's total support; (2) provide support that is necessary to avoid the interruption of the carrying on of a particular function or activity of the supported organization; or (3) provide an amount of support that, based on "all pertinent factors," is a sufficient part of a supported organization's total support. For purposes of the second test listed above, support is considered necessary if the supporting organization or the supported organization earmarks the support for a particular program or activity of the supported organization, even if such program or activity is not the supported organization's primary activity, as long as the program or activity is a substantial one.

One commenter suggested that the regulations clarify that, for purposes of determining whether a supporting organization provides 10 percent of a supported organization's total support, the supported organization's total support is its total support received in the immediately preceding taxable year. The final regulations adopt this comment.

Other commenters recommended changes to portions of the attentiveness test in the 2009 proposed regulations that are substantially identical to those in the existing regulations. The final and temporary regulations do not amend or supplement any of these portions of the attentiveness test, none of which were directly changed or affected by the PPA.

One commenter requested that the regulations include a safe harbor under which the attentiveness test would be automatically satisfied if a certain stated dollar amount of support (possibly indexed for inflation) were distributed to a supported organization. The final and temporary regulations do not adopt this suggestion because of the difficulty in identifying a specific dollar threshold that would be sufficient in all cases to ensure the supported organization's attentiveness.

Finally, one commenter requested guidance on how a supporting organization to a community foundation could satisfy the attentiveness test if it makes distributions to third-party organizations that fulfill the mission of the supported organization(s). Grants to organizations other than the supported organization will not ensure the attentiveness of a supported

organization. Moreover, Type III supporting organizations generally are not permitted to make grants to organizations other than their supported organizations. See § 1.509(a)–4(e)(1). Thus, the final and temporary regulations do not permit supporting organizations to satisfy the attentiveness test by making distributions to third-party organizations.

#### d. Valuation of Assets

In describing how a NFI Type III supporting organization determines the fair market value of its non-exempt-use assets for purposes of determining its distributable amount, the 2009 proposed regulations incorporated language used in § 53.4942(a)–2(c), which describes how a private foundation values its assets for purposes of determining its distributable amount. The 2009 proposed regulations also incorporated language used in § 53.4942(a)–2(c) in describing the assets (including exempt-use assets) that are excluded in determining the distributable amount.

Rather than duplicate all of the language in § 53.4942(a)–2(c), the temporary regulations accomplish the same result as the 2009 proposed regulations by cross-referencing § 53.4942(a)–2(c). More specifically, the temporary regulations state that the determination of the aggregate fair market value of a NFI Type III supporting organization's non-exempt-use assets will be made using the valuation methods described in § 53.4942(a)–2(c). The temporary regulations also state that, for these purposes, the "non-exempt-use" assets of the supporting organization do not include assets described in § 53.4942(a)–2(c)(2) or assets used (or held for use) to carry out the exempt purposes of the supported organization(s) (as defined by applying the principles described in § 53.4942(a)–2(c)(3)).

The Treasury Department and the IRS do not intend for cross-referencing (rather than duplicating the language of) § 53.4942(a)–2(c) to result in any substantive changes from the 2009 proposed regulations in how NFI Type III supporting organizations value their assets or in what assets are excluded in determining the distributable amount. However, to the extent that cross-referencing § 53.4942(a)–2(c) could result in any unintended uncertainty on this point, the Treasury Department and the IRS have issued this change in temporary and proposed regulations to provide an opportunity for comment.

#### 7. Consequences of Failure To Meet Requirements

A Type III supporting organization that fails to meet the requirements of these final and temporary regulations—and that also fails to meet the requirements of a Type I or II supporting organization and otherwise fails to qualify as a public charity under section 509(a)(1), (2), or (4)—will be classified as a private foundation. Once classified as a private foundation, the section 507 rules regarding termination of private foundation status apply.

One commenter requested that the regulations reclassify a Type III supporting organization that fails to meet the requirements of the regulations as a private foundation as of the beginning of the taxable year in which the failure occurred only for purposes of section 507 and section 4940 (regarding excise taxes on net investment income) and as of the first day of the next taxable year for all other provisions of Chapter 42 (which contains other excise taxes applicable to private foundations). This commenter also recommended that, for purposes of Chapter 42, the identity of substantial contributors to a supporting organization within the meaning of section 507(d)(2) be determined by taking into account only contributions received after the date the organization is reclassified as a private foundation.

In addition, this same commenter made two recommendations related to termination of private foundation status under section 507. First, the commenter recommended that a Type III supporting organization that is reclassified as a private foundation for certain "non-structural" reasons (such as accepting gifts from persons that control the supported organization(s), failing to provide an annual notice, not making the required payout, or not satisfying the attentiveness test) be treated as having received an advance ruling that it can be expected to satisfy the requirements of a supporting organization during the 60-month termination period under § 1.507–2(d) if the supporting organization includes certain explanatory information in its notice of termination of private foundation status. Second, the commenter recommended allowing a supporting organization to provide a notice of termination after the commencement of the 60-month termination period in appropriate cases—for example, during the one or two years after the regulations become effective.

The PPA changes did not impact the timing of when a Type III supporting organization is reclassified as a private

foundation or when the various provisions of Chapter 42 apply after the Type III supporting organization fails to meet one or more of the requirements necessary to maintain its classification as a Type III supporting organization (or other type of public charity). The PPA changes also did not impact the contributions that are taken into account when determining whether donors are substantial contributors. With respect to termination of private foundation status under section 507, section 507(b)(1)(B)(ii) states that organizations terminating their private foundation status to operate as a supporting organization or other public charity must notify the Secretary before, not after, the commencement of the 60-month termination period. Accordingly, the final and temporary regulations do not adopt this commenter's recommendations.

#### 8. Transition and Other Relief Provisions

##### a. Notification Requirement

The final regulations provide that a Type III supporting organization in existence on December 28, 2012, the effective date of the final regulations, must meet its notification requirement for its taxable year that includes December 28, 2012, by the later of the last day of the fifth calendar month following the close of that taxable year or the due date, including extensions, of its Form 990 (or other annual information return described in section 6033) for that taxable year. Thus, for example, a Type III supporting organization reporting on a calendar year basis that does not have to file its 2012 Form 990 until November 15, 2013, because it was granted two three-month extensions of time to file will have until November 15, 2013, to satisfy its notification requirement for 2012.

##### b. Responsiveness Test

The final regulations, like the 2009 proposed regulations, provide that additional facts and circumstances, such as a historic and continuing relationship with supported organization(s), may be taken into account in establishing compliance with the responsiveness test for organizations that were supporting such supported organization(s) prior to November 20, 1970.

One commenter asked that the final regulations clarify whether this alternative responsiveness test for pre-November 20, 1970 organizations requires a Type III supporting organization to also satisfy the significant voice prong of the responsiveness test under § 1.509(a)–

4(i)(3)(iii). Consistent with the existing regulations, the final regulations clarify that the significant voice prong is simply one factor along with other facts and circumstances that will be taken into account in determining compliance with the responsiveness test for pre-November 20, 1970 organizations.

#### c. Integral Part Test

The final regulations provide transition rules with respect to the integral part test for Type III supporting organizations in existence on December 28, 2012, the effective date of the final regulations. The 2009 proposed regulations included a transition rule under which an organization that met and continued to meet the requirements of existing § 1.509(a)–4(i)(3)(ii) (that is, an organization meeting the integral part test by satisfying the “but for” test) would be treated as meeting the requirements of a functionally integrated Type III supporting organization set forth in § 1.509(a)–4(i)(4) until the first day of the organization’s first taxable year beginning after the publication of the final or temporary regulations. However, the Treasury Department and the IRS realize that because the final regulations are being published on December 28, 2012, Type III supporting organizations reporting on a calendar year basis that wish to qualify as functionally integrated may need additional time to comply with § 1.509(a)–4(i)(4). As a result, the final regulations amend this transition rule to provide that a Type III supporting organization that met and continues to meet the “but for” test under existing § 1.509(a)–4(i)(3)(ii) will be treated as meeting the requirements of a functionally integrated Type III supporting organization set forth in § 1.509(a)–4(i)(4) until the first day of the organization’s second taxable year beginning after December 28, 2012.

Like the 2009 proposed regulations, the final regulations provide that a Type III supporting organization in existence on December 28, 2012, that met and continues to meet the requirements of existing § 1.509(a)–4(i)(3)(iii) (that is, an organization meeting the integral part test by satisfying the existing “payout” test) will be treated as meeting the requirements of a NFI Type III supporting organization set forth in § 1.509(a)–4(i)(5) until the first day of the organization’s second taxable year beginning after December 28, 2012. However, for purposes of determining whether a Type III supporting organization treated as NFI under this transition relief creates an “excess amount” that can be carried over for five years, the distributable amount for the

supporting organization’s first taxable year beginning after December 28, 2012, is the greater of 85 percent of net adjusted income or 3.5 percent of the value of assets in the immediately preceding taxable year (that is, the distributable amount as ordinarily determined under the temporary regulations).

Section 1.509(a)–4(i)(11)(iii) of the 2009 proposed regulations provided that the distributable amount for NFI Type III supporting organizations is zero for the first taxable year beginning after the effective date of the final or temporary regulations. The Treasury Department and the IRS did not intend for this provision to apply to a NFI Type III supporting organization that had been meeting the payout test under existing § 1.509(a)–4(i)(3)(iii), as is clear from the example provided in the preamble to the 2009 proposed regulations illustrating the application of the transition rules for a NFI Type III supporting organization. Rather, § 1.509(a)–4(i)(11)(iii) of the 2009 proposed regulations more appropriately applies only to Type III supporting organizations that had been meeting the “but for” test under existing § 1.509(a)–4(i)(3)(ii) in the taxable year of the final regulations’ publication but seek to qualify as NFI (rather than functionally integrated) Type III supporting organizations in succeeding taxable years. Indeed, one commenter specifically asked for clarification regarding the transition relief applicable to Type III supporting organizations that had been satisfying the existing “but for” test but intend to convert to NFI status because they cannot or do not wish to qualify as functionally integrated under the final regulations.

The final regulations provide clarification regarding these transition rules. In particular, the final regulations provide that a Type III supporting organization in existence on December 28, 2012, that meets the requirements of the “but for” test under existing § 1.509(a)–4(i)(3)(ii) in its taxable year including December 28, 2012, but not in its first taxable year beginning after December 28, 2012, is a NFI Type III supporting organization during that first taxable year and will be treated as having a distributable amount of zero for purposes of meeting the distribution and attentiveness requirements under § 1.509(a)–4(i)(5)(ii)–(iii). Notwithstanding this transition relief, for purposes of determining whether such a NFI Type III supporting organization creates an “excess amount” that can be carried over for five years, the distributable amount for the first taxable year beginning after December

28, 2012, is the greater of 85 percent of net adjusted income or 3.5 percent of the value of assets in the immediately preceding taxable year (that is, the distributable amount as ordinarily determined under the temporary regulations). The same rule applies for purposes of determining the excess amount of an organization that has a distributable amount of zero in its first taxable year as a NFI Type III supporting organization under § 1.509(a)–4(i)(5)(ii)(D).

Beginning in the second taxable year beginning after December 28, 2012, and in all succeeding taxable years, all Type III supporting organizations must meet either the requirements of § 1.509(a)–4(i)(4) or § 1.509(a)–4(i)(5). A Type III supporting organization intending to meet the requirements of a NFI Type III supporting organization under § 1.509(a)–4(i)(5) in its second taxable year beginning after December 28, 2012, should value its assets in accordance with the valuation methods described in the final regulations beginning in its first taxable year beginning after December 28, 2012.

In addition, a Type III supporting organization treated as a functionally integrated Type III supporting organization during its first taxable year beginning after December 28, 2012, by virtue of satisfying the “but for” test under existing § 1.509(a)–4(i)(3)(ii) but intending to meet the requirements of a NFI Type III supporting organization under § 1.509(a)–4(i)(5) during its second taxable year beginning after December 28, 2012, will have a distributable amount for that second taxable year based on its income or the value of its assets in the immediately preceding taxable year. Such a Type III supporting organization will not have a distributable amount of zero in its second taxable year beginning after December 28, 2012, notwithstanding the general rule under § 1.509(a)–4(i)(5)(ii)(D) that the distributable amount for the first taxable year an organization is treated as a NFI Type III supporting organization is zero.

Two commenters requested that the regulations provide transition relief to NFI Type III supporting organizations whose governing instrument or other instrument prohibits distributions from capital or corpus, similar to the transition rules provided to certain private foundations organized before May 27, 1969, under § 53.4942(a)–2(e). The final regulations provide transition relief to each NFI Type III supporting organization organized before September 24, 2009, that commences judicial proceedings before June 26, 2013, that are necessary to reform its

governing or other instrument to allow it to meet the distribution requirement. During any taxable year in which such a judicial proceeding is pending, a NFI Type III supporting organization is excepted from the distribution requirement to the extent it is prevented from meeting the requirement by one or more mandatory provisions in its governing instrument or other instrument that prohibits distributions from capital or corpus. The transition relief applies only if the governing or other instrument at issue was executed (and the mandatory provisions were in effect) before September 24, 2009, the date the 2009 proposed regulations were published in the **Federal Register**, and if the judicial proceeding is not subject to any unreasonable delay for which the supporting organization is responsible. Beginning with the first taxable year following the termination of a judicial proceeding, a NFI Type III supporting organization must satisfy the distribution requirement regardless of the outcome of the judicial proceeding—a requirement materially identical to the requirements imposed by § 53.4942(a)-2(e)(3) on pre-May 27, 1969 private foundations whose governing instruments prohibited distributions out of capital or corpus.

Numerous commenters responded to the request in the 2009 proposed regulations for comments regarding the need for a transition rule for NFI Type III supporting organizations whose assets consist predominantly of assets that are not readily marketable. Commenters suggested a longer transition period, varying from four to ten years, for supporting organizations with such assets. Some commenters suggested providing the longer transition period to all supporting organizations with a sufficiently high proportion (for example, a “material” threshold of 20 percent or more) of not-readily-marketable assets. Other commenters recommended allowing a NFI Type III supporting organization to exclude the value of its not-readily-marketable assets from the assets used to calculate the distributable amount during the longer transition period (while possibly also requiring the organization to pay out substantially all of the income generated by its not-readily-marketable assets). A few commenters recommended a phase-in of the required distribution rate during a transition period (either for all NFI Type III supporting organizations or those holding substantial not-readily-marketable assets). As an alternative to transition relief, one commenter recommended a reasonable cause

exception for NFI Type III supporting organizations that are unable to reasonably liquidate their assets that are not readily marketable.

The final and temporary regulations do not include a transition rule, or a reasonable cause exception, for NFI Type III supporting organizations with assets that are not readily marketable. After consideration of the comments received, the Treasury Department and the IRS have concluded that any such transition rule would unfairly impose a higher distribution requirement on those NFI Type III supporting organizations that invested primarily in liquid assets, as compared to those organizations that stayed heavily invested in not-readily-marketable assets. Moreover, all NFI Type III supporting organizations have at least two years after December 28, 2012, to satisfy the distribution requirement, and the Treasury Department and the IRS have concluded that this transition relief will give supporting organizations sufficient time to make any sales of not-readily-marketable assets that may be necessary to meet the distribution requirement.

Finally, like the 2009 proposed regulations, the final regulations continue to provide that a trust that on November 20, 1970, met and continues to meet the requirements under existing § 1.509(a)-4(i)(4) and § 1.509(a)-4(i)(9) of the final regulations will satisfy the integral part test as a NFI Type III supporting organization under § 1.509(a)-4(i)(5). One organization questioned why a pre-November 20, 1970 trust that meets all of the requirements set forth in § 1.509(a)-4(i)(9) should have to petition the IRS for a ruling. In lieu of a ruling, the commenter requested a form on which the trust’s trustee could certify that the trust meets all of the requirements of § 1.509(a)-4(i)(9) or, if a ruling were required, some assurance that the trust could operate on the assumption that it met the requirements of § 1.509(a)-4(i)(9) until a ruling was issued. Like existing § 1.509(a)-4(i)(4), § 1.509(a)-4(i)(9) of the final regulations states that applicable trusts *may* (not “must”) obtain a ruling that they meet the requirements set forth in the provision. Accordingly, a trust that meets the requirements of § 1.509(a)-4(i)(9) is not required to obtain a ruling. The final and temporary regulations do not alter this long-standing, optional ruling procedure.

#### c. Regulations Under Section 4943

This Treasury decision also includes final regulations under section 4943 that provide two transition rules to address

excess business holdings for Type III supporting organizations affected by the PPA. The Treasury Department and the IRS did not receive any comments on these transition rules. The final regulations adopt the 2009 proposed regulations without change.

#### 9. Miscellaneous

Several other incidental changes were made throughout the final regulations in order to increase clarity and consistency, none of which are intended to modify the substance of the 2009 proposed regulations.

#### 10. Effective/Applicability Date

Both the final and temporary regulations are effective and applicable on December 28, 2012. However, supporting organizations should note that section 509(f), which was added by the PPA, is effective on and after August 17, 2006. In the case of section 509(f)(1)(B), which prohibits Type III supporting organizations from supporting foreign organizations, a transition rule applies under which Type III supporting organizations that were supporting a foreign organization on August 17, 2006, could continue supporting the foreign organization until the first day of its third taxable year beginning after August 17, 2006. In addition, pursuant to section 1241(c) of the PPA, the responsiveness test for charitable trusts in existing § 1.509(a)-4(i)(2)(iii) cannot support classification as a Type III supporting organization, effective August 17, 2007, in the case of trusts operated in connection with a supported organization on August 17, 2006. See PPA section 1241(e)(2)(A).

#### Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866, as supplemented by Executive Order 13563. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to the temporary or the final regulations. For the applicability of the Regulatory Flexibility Act (5 U.S.C. chapter 6) to the temporary regulations, refer to the Special Analyses section of the preamble to the cross-reference notice of proposed rulemaking published in the Proposed Rules section in this issue of the **Federal Register**.

It is hereby certified that the collection of information contained in the final regulations will not have a significant economic impact on a substantial number of small entities.

This certification is based on the fact that the final regulations will not impact a substantial number of small entities.

Based on IRS Statistics of Income data for 2009, there are 1,238,201 active nonprofit charitable organizations recognized by the IRS under section 501(c)(3), of which only 7,556 organizations self-identified as Type III supporting organizations. Thus, the number of organizations affected by the collection of information under § 1.509(a)-4(i)(2) will not be substantial. In addition, the collection of information under § 1.509(a)-4(i)(2) will impose a minimal burden on the affected organizations because all of the information that must be provided is information that the organizations are already required to maintain. Therefore, the collection of information under § 1.509(a)-4(i)(2) will not have a significant economic impact.

The collection of information under § 1.509(a)-4(i)(6)(v) is required only if a NFI Type III supporting organization wishes to obtain the benefit of having certain amounts set aside for a specific project count toward the distribution requirement imposed by these proposed regulations. Based on IRS Statistics of Income data for 2009, only 4,438 organizations self-identified as Type III supporting organizations that are not functionally integrated. Because only a very small proportion of private foundations (less than 0.02 percent) submit ruling requests for set-asides each year, the Treasury Department and the IRS similarly expect that this elective provision will apply to only a very small subset of NFI Type III supporting organizations in any given year. Therefore, the number of organizations affected by the collection of information under § 1.509(a)-4(i)(6)(v) will not be substantial. Accordingly, a regulatory flexibility analysis is not required for the final regulations.

Pursuant to section 7805(f) of the Code, the 2009 proposed regulations preceding the final regulations were submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business and no comments were received. The temporary regulations (and the cross-reference notice of proposed rulemaking published in the Proposed Rules section in this issue of the **Federal Register**) will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

### Drafting Information

The principal authors of these regulations are Preston J. Quesenberry, and Stephanie N. Robbins, Office of Associate Chief Counsel (Tax-Exempt and Government Entities). However, other personnel from the Treasury Department and the IRS participated in their development.

### List of Subjects

#### 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

#### 26 CFR Part 53

Excise taxes, Foundations, Investments, Lobbying, Reporting and recordkeeping requirements.

#### 26 CFR Part 602

Reporting and recordkeeping requirements.

### Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1, 53, and 602 are amended as follows:

#### PART 1—INCOME TAXES

■ **Paragraph 1.** The authority citation for part 1 continues to read in part as follows:

**Authority:** 26 U.S.C. 7805 \* \* \*

■ **Par. 2.** Section 1.509(a)-4 is amended by:

1. Adding paragraphs (a)(6), (f)(5), and (l).

2. Revising paragraph (i).

The revision and additions read as follows:

#### § 1.509(a)-4 Supporting organizations.

(a) \* \* \*

(6) For purposes of paragraph (i) of this section, the term “supported organization” means a specified publicly supported organization described in paragraphs (d)(2)(iv) or (d)(4) of this section.

\* \* \* \* \*

(f) \* \* \*

(5) **Contributions from controlling donors—(i) In general.** For any taxable year, a supporting organization shall not be considered to be operated, supervised, or controlled by, or operated in connection with, one or more publicly supported organizations, if the supporting organization accepts any gift or contribution from any person who is—

(A) A person (other than an organization described in section 509(a)(1), (2), or (4)) who directly or indirectly controls, either alone or together with persons described in

paragraphs (f)(5)(i)(B) or (f)(5)(i)(C) of this section, the governing body of a specified publicly supported organization supported by such supporting organization;

(B) A member of the family (determined under section 4958(f)(4)) of an individual described in paragraph (f)(5)(i)(A) of this section; or

(C) A 35-percent controlled entity (as defined in section 4958(f)(3) by substituting “clause (i) or (ii) of section 509(f)(2)(B)” for “subparagraph (A) or (B) of paragraph (1)” in paragraph (f)(3)(A)(i) thereof).

(ii) *Meaning of control.* [Reserved]

\* \* \* \* \*

(i) *Meaning of operated in connection with—(1) General rule.* For each taxable year, a supporting organization is operated in connection with one or more supported organizations (that is, is a “Type III supporting organization”) only if it is not disqualified by reason of paragraph (f)(5) (relating to acceptance of contributions from controlling donors) or paragraph (i)(10) (relating to foreign supported organizations) of this section, and it satisfies—

(i) The notification requirement, which is set forth in paragraph (i)(2) of this section;

(ii) The responsiveness test, which is set forth in paragraph (i)(3) of this section; and

(iii) The integral part test, which is satisfied by maintaining significant involvement in the operations of one or more supported organizations and providing support on which the supported organization(s) are dependent; in order to satisfy this test, the supporting organization must meet the requirements either for—

(A) Functionally integrated Type III supporting organizations set forth in paragraph (i)(4) of this section; or

(B) Non-functionally integrated Type III supporting organizations set forth in paragraph (i)(5) of this section.

(2) *Notification requirement—(i) Annual notification.* For each taxable year, a Type III supporting organization must provide the following documents to each of its supported organizations:

(A) A written notice addressed to a principal officer of the supported organization describing the type and amount of all of the support the supporting organization provided to the supported organization during the supporting organization’s taxable year immediately preceding the taxable year in which the written notice is provided (and during any other taxable year of the supporting organization ending after December 28, 2012, for which such

support information has not previously been provided);

(B) A copy of the supporting organization's Form 990, "Return of Organization Exempt from Income Tax," or other annual information return required to be filed under section 6033 (although the supporting organization may redact from the return the name and address of any contributor to the organization) that was most recently filed as of the date the notification is provided (and any such return for any other taxable year of the supporting organization ending after December 28, 2012, that has not previously been provided to the supported organization); and

(C) A copy of the supporting organization's governing documents as in effect on the date the notification is provided, including its articles of organization and bylaws (if any) and any amendments to such documents, unless such documents have been previously provided and not subsequently amended.

(ii) *Electronic media.* The notification documents required by this paragraph (i)(2) may be provided by electronic media.

(iii) *Due date.* The notification documents required by this paragraph (i)(2) for any taxable year shall be postmarked or electronically transmitted by the last day of the fifth calendar month following the close of that taxable year.

(iv) *Principal officer.* For purposes of paragraph (i)(2)(i)(A) of this section, a principal officer includes, but is not limited to, a person who, regardless of title, has ultimate responsibility for—

(A) Implementing the decisions of the governing body of a supported organization;

(B) Supervising the management, administration, or operation of the supported organization; or

(C) Managing the finances of the supported organization.

(3) *Responsiveness test*—(i) *General rule.* A supporting organization meets the responsiveness test if it is responsive to the needs or demands of a supported organization. Except as provided in paragraph (i)(3)(v) of this section, in order to meet this test, a supporting organization must satisfy the requirements of paragraphs (i)(3)(ii) and (i)(3)(iii) of this section.

(ii) *Relationship of officers, directors, or trustees.* A supporting organization satisfies the requirements of this paragraph (i)(3)(ii) with respect to a supported organization only if—

(A) One or more officers, directors, or trustees of the supporting organization are elected or appointed by the officers,

directors, trustees, or membership of the supported organization;

(B) One or more members of the governing body of the supported organization are also officers, directors, or trustees of, or hold other important offices in, the supporting organization; or

(C) The officers, directors, or trustees of the supporting organization maintain a close and continuous working relationship with the officers, directors, or trustees of the supported organization.

(iii) *Significant voice.* A supporting organization satisfies the requirements of this paragraph (i)(3)(iii) only if, by reason of paragraphs (i)(3)(ii)(A), (i)(3)(ii)(B), or (i)(3)(ii)(C) of this section, the officers, directors, or trustees of the supported organization have a significant voice in the investment policies of the supporting organization, the timing of grants, the manner of making grants, and the selection of grant recipients by such supporting organization, and in otherwise directing the use of the income or assets of the supporting organization.

(iv) *Examples.* The provisions of this paragraph (i)(3) may be illustrated by the following examples:

*Example 1.* X, an organization described in section 501(c)(3), is a trust created under the last will and testament of Decedent. The trustee of X (Trustee) is a bank. Under the trust instrument, X supports M, a private university described in section 509(a)(1). The trust instrument provides that Trustee has discretion regarding the timing and amount of distributions consistent with the Trustee's fiduciary duties. Representatives of Trustee and an officer of M have quarterly face-to-face or telephonic meetings during which they discuss M's projected needs and ways in which M would like X to use its income and invest its assets. Additionally, Trustee communicates regularly with that officer of M regarding X's investments and plans for distributions from X. Trustee provides the officer of M with quarterly investment statements, the information required under paragraph (i)(2) of this section, and an annual accounting statement. Based on these facts, X meets the responsiveness test of this paragraph (i)(3) with respect to M.

*Example 2.* Y is an organization described in section 501(c)(3) and is a trust under State law. The trustee of Y (Trustee) is a bank. Y supports charities P, Q, and R, each an organization described in section 509(a)(1). Y makes annual cash payments to P, Q, and R. Once a year, Trustee sends to P, Q, and R the cash payment, the information required under paragraph (i)(2) of this section, and an accounting statement. Trustee has no other communication with P, Q, or R. Y does not meet the responsiveness test of this paragraph (i)(3).

(v) *Exception for pre-November 20, 1970 organizations.* In the case of a supporting organization that was

supporting or benefiting a supported organization before November 20, 1970, additional facts and circumstances, such as a historic and continuing relationship between the organizations, may be taken into account, in addition to the factors described in paragraphs (i)(3)(ii) and (i)(3)(iii) of this section, to establish compliance with the responsiveness test.

(4) *Integral part test—functionally integrated Type III supporting organization*—(i) *General rule.* A supporting organization meets the integral part test and will be considered functionally integrated within the meaning of section 4943(f)(5)(B), if it—

(A) Engages in activities substantially all of which directly further the exempt purposes of one or more supported organizations and otherwise meets the requirements described in paragraph (i)(4)(ii) of this section;

(B) Is the parent of each of its supported organizations, as described in paragraph (i)(4)(iii) of this section; or

(C) Supports a governmental supported organization and otherwise meets the requirements of paragraph (i)(4)(iv) of this section.

(ii) *Substantially all activities directly further exempt purposes*—(A) *In general.* A supporting organization meets the requirements of this paragraph (i)(4)(ii) if it engages in activities substantially all of which—

(1) Directly further the exempt purposes of one or more supported organizations to which the supporting organization is responsive by performing the functions of, or carrying out the purposes of, such supported organization(s); and

(2) But for the involvement of the supporting organization, would normally be engaged in by such supported organization(s).

(B) *Meaning of substantially all.* For purposes of paragraph (i)(4)(ii)(A) of this section, in determining whether substantially all of a supporting organization's activities directly further the exempt purposes of one or more supported organization(s) to which the supporting organization is responsive, all pertinent facts and circumstances will be taken into consideration.

(C) *Meaning of directly further.* Activities "directly further" the exempt purposes of one or more supported organizations for purposes of this paragraph (i)(4) only if they are conducted by the supporting organization itself, rather than by a supported organization. Holding title to and managing exempt-use assets described in § 1.509(a)-4T(i)(8)(ii) are activities that directly further the exempt purposes of the supported

organization within the meaning of this paragraph (i)(4). Conversely, except as provided in paragraph (i)(4)(ii)(D) of this section, fundraising, making grants (whether to the supported organization or to third parties), and investing and managing non-exempt-use assets are not activities that directly further the exempt purposes of the supported organization within the meaning of this paragraph (i)(4).

(D) *Payments to individual beneficiaries.* The making or awarding of grants, scholarships, or other payments to individual beneficiaries who are members of the charitable class benefited by a supported organization will be treated as an activity that directly furthers the exempt purposes of that supported organization for purposes of this paragraph (i)(4) only if—

(1) The individual beneficiaries are selected on an objective and nondiscriminatory basis (as described in § 53.4945-4(b));

(2) The officers, directors, or trustees of the supported organization have a significant voice in the timing of the payments, the manner of making them, and the selection of recipients; and

(3) The making or awarding of such payments is part of an active program of the supporting organization that directly furthers the exempt purposes of the supported organization and in which the supporting organization maintains significant involvement, as defined in § 53.4942(b)-1(b)(2)(ii) (except that “supporting organization” shall be substituted for “foundation”).

(iii) *Parent of supported organization(s).* For purposes of paragraph (i)(4)(i)(B) of this section, a supporting organization is the parent of a supported organization if the supporting organization exercises a substantial degree of direction over the policies, programs, and activities of the supported organization and a majority of the officers, directors, or trustees of the supported organization is appointed or elected, directly or indirectly, by the governing body, members of the governing body, or officers (acting in their official capacity) of the supporting organization.

(iv) *Supporting a governmental entity.* [Reserved]

(v) *Examples.* The provisions of this paragraph (i)(4) may be illustrated by the following examples:

*Example 1.* N, an organization described in section 501(c)(3), is the parent organization of a healthcare system consisting of two hospitals (Q and R) and an outpatient clinic (S), each of which is described in section 509(a)(1), and a taxable subsidiary (T). N is the sole member of each of Q, R, and S.

Under the charter and bylaws of each of Q, R, and S, N appoints all members of the board of directors of each corporation. N engages in the overall coordination and supervision of the healthcare system’s exempt subsidiary corporations Q, R, and S in approval of their budgets, strategic planning, marketing, resource allocation, securing tax-exempt bond financing, and community education. N also manages and invests assets that serve as endowments of Q, R, and S. Based on these facts, N qualifies as a functionally integrated Type III supporting organization under paragraph (i)(4)(i)(B) of this section.

*Example 2.* V, an organization described in section 501(c)(3), is organized and operated as a supporting organization to L, a church described in section 509(a)(1). V meets the responsiveness test described in paragraph (i)(3) of this section with respect to L. L transferred to V title to the buildings in which L conducts religious services, Bible study, and community enrichment programs. Substantially all of V’s activities consist of holding and maintaining these buildings, which L continues to use, free of charge, to further its exempt purposes. But for the activities of V, L would hold and maintain the buildings. Based on these facts, V satisfies the requirements of paragraph (i)(4)(ii) of this section.

*Example 3.* O is a local nonprofit food pantry described in section 501(c)(3). O collects donated food from local growers, grocery stores, and individuals and distributes this food free of charge to poor and needy people in O’s community. O is organized and operated as a supporting organization to eight churches of a particular denomination located in O’s community, each of which is described in section 509(a)(1). Control of O is vested in a five-member Board of Directors, which includes an official from one of the churches as well as four lay members of the churches’ congregations. The officers of O maintain a close and continuing working relationship with each of the eight churches and as a result of such relationship, each of the eight churches has a significant voice in directing the use of the income and assets of O. As a result, O is responsive to its supported organizations. All of O’s activities directly further the exempt purposes of the eight supported organizations to which it is responsive. Additionally, but for the activities of O, the churches would normally operate food pantries themselves. Based on these facts, O satisfies the requirements of paragraph (i)(4)(ii) of this section.

*Example 4.* M, an organization described in section 501(c)(3), was created by B, an individual, to provide scholarships for students of U, a private secondary school and an organization described in section 509(a)(1). U establishes the scholarship criteria, publicizes the scholarship program, solicits and reviews applications, and selects the scholarship recipients. M invests its assets and disburses the funds for scholarships to the recipients selected by U. M does not provide the scholarships as part of an active program in which it maintains significant involvement, as defined in § 53.4942(b)-1(b)(2)(ii). Based on these facts,

M does not satisfy the requirements of paragraph (i)(4)(ii) of this section.

*Example 5.* J, an organization described in section 501(c)(3), is organized as a supporting organization to community foundation G, an organization described in section 509(a)(1). J meets the responsiveness test described in paragraph (i)(3) of this section with respect to G. In addition to maintaining field-of-interest funds, sponsoring donor advised funds, and conducting general grantmaking activities, G also engages in activities to beautify and maintain local parks. Substantially all of J’s activities consist of maintaining all of the local parks in the area of community foundation G by performing activities such as establishing and maintaining trails, planting trees, and removing trash. But for the activities of J, G would normally engage in these efforts to beautify and maintain the local parks. Based on these facts, J satisfies the requirements of paragraph (i)(4)(ii) of this section.

(5) *Integral part test—non-functionally integrated Type III supporting organization—(i) General rule.* A supporting organization meets the integral part test and will be considered non-functionally integrated if it satisfies either—

(A) The distribution requirement of paragraph (i)(5)(ii) of this section and the attentiveness requirement of paragraph (i)(5)(iii) of this section; or

(B) The pre-November 20, 1970 trust requirements of paragraph (i)(9) of this section.

(ii) *Distribution requirement—(A) Annual distribution.* With respect to each taxable year, a supporting organization must distribute to or for the use of one or more supported organizations an amount equaling or exceeding the supporting organization’s distributable amount for the taxable year, as defined in § 1.509(a)-4T(i)(5)(ii)(B), on or before the last day of the taxable year.

(B) *Distributable amount.* [Reserved]. For further guidance, see § 1.509(a)-4T(i)(5)(ii)(B).

(C) *Minimum asset amount.* [Reserved]. For further guidance, see § 1.509(a)-4T(i)(5)(ii)(C).

(D) *First taxable year.* The distributable amount for the first taxable year an organization is treated as a non-functionally integrated Type III supporting organization is zero. Notwithstanding the foregoing, for purposes of determining whether an excess amount is created under paragraph (i)(7)(ii) of this section, the distributable amount for the first taxable year an organization is treated as a non-functionally integrated Type III supporting organization is the distributable amount that would apply under § 1.509(a)-4T(i)(5)(ii)(B) in the absence of this paragraph (i)(5)(ii)(D).



(E) *Emergency temporary reduction.* The Secretary may provide by publication in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b) of this chapter) for a temporary reduction in the distributable amount in the case of a disaster or emergency.

(F) *Reasonable cause exception.* A non-functionally integrated Type III supporting organization that fails to meet the distribution requirement of this paragraph (i)(5)(ii) will not be classified as a private foundation for the taxable year in which it fails to meet the distribution requirement if the organization establishes to the satisfaction of the Secretary that—

(1) The failure was due solely to unforeseen events or circumstances that are beyond the organization's control, a clerical error, or an incorrect valuation of assets;

(2) The failure was due to reasonable cause and not to willful neglect; and

(3) The distribution requirement is met within 180 days after the organization is first able to distribute its distributable amount notwithstanding the unforeseen events or circumstances, or 180 days after the date the incorrect valuation or clerical error was or should have been discovered; however, no amounts paid to meet a distribution requirement for a prior taxable year under this paragraph (i)(5)(ii)(F)(3) may be counted toward the distribution requirement for the taxable year in which such amounts are paid.

(iii) *Attentiveness requirement—(A) General rule.* With respect to each taxable year, a non-functionally integrated Type III supporting organization must distribute one-third or more of its distributable amount to one or more supported organizations that are attentive to the operations of the supporting organization (within the meaning of paragraph (i)(5)(iii)(B) of this section) and to which the supporting organization is responsive (within the meaning of paragraph (i)(3) of this section).

(B) *Attentiveness.* A supported organization is attentive to the operations of the supporting organization during a taxable year if, in the taxable year, at least one of the following requirements is satisfied:

(1) The supporting organization distributes to the supported organization amounts equaling or exceeding 10 percent of the supported organization's total support (or, in the case of a particular department or school of a university, hospital, or church, the total support of the department or school) received during the supported organization's last taxable

year ending before the beginning of the supporting organization's taxable year.

(2) The amount of support received from the supporting organization is necessary to avoid the interruption of the carrying on of a particular function or activity of the supported organization. The support is necessary if the supporting organization or the supported organization earmarks the support for a particular program or activity of the supported organization, even if such program or activity is not the supported organization's primary program or activity, as long as such program or activity is a substantial one.

(3) Based on the consideration of all pertinent factors, including the number of supported organizations, the length and nature of the relationship between the supported organization and supporting organization, and the purpose to which the funds are put, the amount of support received from the supporting organization is a sufficient part of a supported organization's total support (or, in the case of a particular department or school of a university, hospital, or church, the total support of the department or school) to ensure attentiveness. Normally the attentiveness of a supported organization is influenced by the amounts received from the supporting organization. Thus, the more substantial the amount involved in terms of a percentage of the supported organization's total support, the greater the likelihood that the required degree of attentiveness will be present. However, in determining whether the amount received from the supporting organization is sufficient to ensure the attentiveness of the supported organization to the operations of the supporting organization (including attentiveness to the nature and yield of the supporting organization's investments), evidence of actual attentiveness by the supported organization is of almost equal importance. A supported organization is not considered to be attentive solely because it has enforceable rights against the supporting organization under state law.

(C) *Distribution to donor advised fund disregarded.* Notwithstanding paragraph (i)(5)(iii)(B) of this section, in determining whether a supported organization will be considered attentive to the operations of a supporting organization, any amount received from the supporting organization that is held by the supported organization in a donor advised fund described in section 4966(d)(2) will be disregarded.

(D) *Examples.* This paragraph (i)(5)(iii) is illustrated by the following examples:

*Example 1.* K, an organization described in section 501(c)(3), annually pays an aggregate amount equaling or exceeding its distributable amount described in § 1.509(a)–4T(i)(5)(ii)(B) to L, a museum described in section 509(a)(2). K meets the responsiveness test described in paragraph (i)(3) of this section with respect to L. In recent years, L has earmarked the income received from K to underwrite the cost of carrying on a chamber music series consisting of 12 performances a year that are performed for the general public free of charge at its premises. The chamber music series is not L's primary activity but it is a substantial activity. L could not continue the performances without K's support. Based on these facts, K meets the requirements of paragraph (i)(5)(iii)(B)(2) of this section.

*Example 2.* M, an organization described in section 501(c)(3), annually pays an aggregate amount equaling or exceeding its distributable amount described in § 1.509(a)–4T(i)(5)(ii)(B) to the Law School of N University, an organization described in section 509(a)(1). M meets the responsiveness test described in paragraph (i)(3) of this section with respect to N. M has earmarked the income paid over to N's Law School to endow a chair in International Law. Without M's continued support, N could not continue to maintain this chair. The chair is not N's primary activity but it is a substantial activity. Based on these facts, M meets the requirements of paragraph (i)(5)(iii)(B)(2) of this section.

*Example 3.* R is a charitable trust created under the will of B, who died in 1969. R's purpose is to hold assets as an endowment for S (a hospital), T (a university), and U (a national medical research organization), all organizations described in section 509(a)(1) and specifically named in the trust instrument, and to distribute all of the income each year in equal shares among the three named beneficiaries. Each year, R pays to S, T, and U an aggregate amount equaling or exceeding its distributable amount described in § 1.509(a)–4T(i)(5)(ii)(B). Such payments equal less than one percent of the total support that each supported organization received in its most recently completed taxable year. Based on these facts, R does not meet the requirements of paragraph (i)(5)(iii)(B)(1) of this section. However, because B died prior to November 20, 1970, R could meet the requirements of paragraph (i)(5)(i)(B) of this section upon meeting all of the requirements of paragraph (i)(9) of this section.

*Example 4.* O is an organization described in section 501(c)(3). O is organized to support five private universities, V, W, X, Y, and Z, each of which is described in section 509(a)(1). O meets the responsiveness test under paragraph (i)(3) of this section only as to V. Each year, O distributes an aggregate amount that equals its distributable amount described in § 1.509(a)–4T(i)(5)(ii)(B) and distributes an equal amount to each of the five universities. Accordingly, O distributes only one-fifth of its distributable amount to

a supported organization to which O is also responsive (V). Because O does not distribute at least one-third of its distributable amount to supported organizations that are both attentive to the operations of O and to which the O is responsive, O does not meet the attentiveness requirements of this paragraph (i)(5)(iii).

(6) *Distributions that count toward distribution requirement.* For purposes of this paragraph (i)(6), the amount of a distribution made to a supported organization is the amount of cash distributed or the fair-market value of the property distributed as of the date the distribution is made. The amount of a distribution will be determined solely on the cash receipts and disbursements method of accounting described in section 446(c)(1). Distributions by the supporting organization that count toward the distribution requirement imposed in paragraph (i)(5)(ii) of this section shall include, but not be limited to—

(i) Any amount paid to a supported organization to accomplish the supported organization's exempt purposes;

(ii) Any amount paid by the supporting organization to perform an activity that satisfies the requirements of paragraph (i)(4)(ii) of this section, but only to the extent such amount exceeds any income derived by the supporting organization from the activity;

(iii) Any reasonable and necessary administrative expenses paid to accomplish the exempt purposes of the supported organization(s), which do not include expenses incurred in the production of investment income;

(iv) Any amount paid to acquire an exempt-use asset described in § 1.509(a)-4T(i)(8)(ii); and

(v) Any amount set aside for a specific project that accomplishes the exempt purposes of a supported organization to which the supporting organization is responsive, with such set aside counting toward the distribution requirement for the taxable year in which the amount is set aside but not in the year in which it is actually paid, if at the time of the set-aside, the supporting organization—

(A) Obtains a written statement from each supported organization whose exempt purposes the specific project accomplishes, signed under penalty of perjury by one of the supported organization's principal officers, as defined in paragraph (i)(2)(iv) of this section, stating that the supported organization approves the project as one that accomplishes one or more of the supported organization's exempt purposes and also approves the supporting organization's determination that the project is one that can be better

accomplished by such a set-aside than by the immediate payment of funds;

(B) Establishes to the satisfaction of the Commissioner, by meeting the approval and information requirements described in § 53.4942(a)-3(b)(7)(i) of this chapter and by providing the written statement described in paragraph (i)(6)(v)(A) of this section, that the amount set aside will be paid for the specific project within 60 months after it is set aside and that the project is one that can better be accomplished by the set-aside than by the immediate payment of funds; and

(C) Evidences the set-aside by the entry of a dollar amount on the books and records of the supporting organization as a pledge or obligation to be paid at a future date or dates within 60 months of the set aside.

(7) *Carryover of excess amounts—(i) In general.* If with respect to any taxable year, an excess amount, as defined in paragraph (i)(7)(ii) of this section, is created, such excess amount may be used to reduce the distributable amount in any of the five taxable years immediately following the taxable year in which the excess amount is created. An excess amount created in a taxable year can only be carried over for five taxable years.

(ii) *Excess amount.* An excess amount is created for any taxable year beginning after December 28, 2012, if the total distributions made in that taxable year that count toward the distribution requirement exceed the supporting organization's distributable amount for the taxable year, as determined under § 1.509(a)-4T(i)(5)(ii)(B). With respect to any taxable year to which an excess amount is carried over, in determining whether an excess amount is created in that taxable year, the distributable amount is first reduced by any excess amounts carried over (with the oldest excess amounts applied first) and then by any distributions made in that taxable year.

(8) *Valuation of non-exempt-use assets.* [Reserved]. For further guidance, see § 1.509(a)-4T(i)(8).

(9) *Alternate integral part test for certain trusts.* A trust (whether or not exempt from taxation under section 501(a)) that on November 20, 1970, met and continues to meet the requirements of paragraphs (i)(9)(i) through (i)(9)(v) of this section, shall be treated as meeting the requirements of paragraph (i)(5) of this section if for taxable years beginning after October 16, 1972, the trustee of such trust makes annual written reports to all of the trust's supported organizations, setting forth a description of the trust's assets, including a detailed list of the assets

and the income produced by such assets. A trust that meets the requirements of this paragraph (i)(9) may request a ruling that it is described in section 509(a)(3) in such manner as the Commissioner may prescribe. The requirements of this paragraph (i)(9) are as follows:

(i) All the unexpired interests in the trust are devoted to one or more purposes described in section 170(c)(1) or (c)(2)(B) and a deduction was allowed with respect to such interests under sections 170, 545(b)(2), 556(b)(2), 642(c), 2055, 2106(a)(2), 2522, or corresponding provisions of prior law (or would have been allowed such a deduction if the trust had not been created before 1913).

(ii) The trust was created prior to November 20, 1970, and did not receive any grant, contribution, bequest or other transfer on or after such date. For purposes of this paragraph (i)(9)(ii), a split-interest trust described in section 4947(a)(2) that was created prior to November 20, 1970, was irrevocable on such date, and that becomes a charitable trust described in section 4947(a)(1) after such date shall be treated as having been created prior to such date.

(iii) The trust is required by its governing instrument to distribute all of its net income currently to a designated beneficiary supported organization. If more than one beneficiary supported organization is designated in the governing instrument of a trust, all of the net income must be distributable and must be distributed currently to each of such supported organizations in fixed shares pursuant to such governing instrument. For purposes of this paragraph (i)(9)(iii), the governing instrument of a charitable trust shall be treated as requiring distribution to a designated supported organization when the trust instrument describes the charitable purpose of the trust so completely that such description can apply to only one existing supported organization and is of sufficient particularity as to vest in such organization rights against the trust enforceable in a court possessing equitable powers.

(iv) The trustee of the trust does not have discretion to vary either the beneficiary supported organizations or the amounts payable to the supported organizations. For purposes of this paragraph (i)(9)(iv), a trustee shall not be treated as having such discretion if the trustee has discretion to make payments of principal to the single supported organization that is currently entitled to receive all of the trust's income or if the trust instrument provides that the trustee may cease making income payments to a particular

supported organization in the event of certain specific occurrences, such as the loss of exemption under section 501(c)(3) or classification under section 509(a)(1) or (a)(2) by the supported organization or the failure of the supported organization to carry out its charitable purpose properly.

(v) None of the trustees would be disqualified persons within the meaning of section 4946(a) (other than foundation managers under section 4946(a)(1)(B)) with respect to the trust if such trust were treated as a private foundation.

(10) *Foreign supported organizations.* A supporting organization is not operated in connection with one or more supported organizations if it supports any supported organization organized outside of the United States.

(11) *Transition rules—(i) Notification requirement.* A Type III supporting organization will be treated as having satisfied the notification requirement described in paragraph (i)(2) of this section for its taxable year that includes December 28, 2012, if the required notification is postmarked or electronically transmitted by the later of the last day of the fifth calendar month following the close of that taxable year or the due date (including extensions) of the supporting organization's annual information return described in section 6033 for that taxable year.

(ii) *Integral part test—(A) Qualification as a functionally integrated Type III supporting organization.* A Type III supporting organization in existence on December 28, 2012, that met and continues to meet the requirements of Treas. Reg. § 1.509(a)-4(i)(3)(ii), as in effect prior to December 28, 2012, will be treated as meeting the requirements of paragraph (i)(4) of this section until the first day of the organization's second taxable year beginning after December 28, 2012.

(B) *Qualification as a non-functionally integrated Type III supporting organization.* A Type III supporting organization in existence on December 28, 2012, that met and continues to meet the requirements of Treas. Reg. § 1.509(a)-4(i)(3)(iii), as in effect prior to December 28, 2012, will be treated as meeting the requirements of paragraph (i)(5)(i)(A) of this section until the first day of its second taxable year beginning after December 28, 2012. Notwithstanding the foregoing, in determining whether an excess amount is created under paragraph (i)(7)(ii) of this section in the first taxable year beginning after December 28, 2012, the distributable amount for that taxable year of a Type III supporting organization treated as meeting the

requirements of paragraph (i)(5)(i)(A) of this section under this paragraph (i)(11)(ii)(B) is the amount described in § 1.509(a)-4T(i)(5)(ii)(B).

(C) *Transitioning to a non-functionally integrated Type III supporting organization in the first taxable year after effective date.* A Type III supporting organization in existence on December 28, 2012, that meets the requirements of Treas. Reg. § 1.509(a)-4(i)(3)(ii), as in effect prior to December 28, 2012, in its taxable year including December 28, 2012, but not in its first taxable year beginning after December 28, 2012, is a non-functionally integrated Type III supporting organization and will be treated as having a distributable amount of zero for purposes of meeting the requirements of paragraph (i)(5)(i)(A) of this section during the organization's first taxable year beginning after December 28, 2012. Notwithstanding the foregoing, in determining whether an excess amount is created under paragraph (i)(7)(ii) of this section in the first taxable year beginning after December 28, 2012, the distributable amount for that taxable year of a Type III supporting organization described in this paragraph (i)(11)(ii)(C) is the amount described in § 1.509(a)-4T(i)(5)(ii)(B), determined without regard to paragraph (i)(5)(ii)(D) of this section.

(D) *Second taxable year after effective date.* Beginning in the second taxable year beginning after December 28, 2012, and in all succeeding taxable years, all Type III supporting organizations described in this paragraph (i)(11)(ii) must meet either the requirements of paragraph (i)(4) or (i)(5) of this section. If a Type III supporting organization described in paragraph (i)(11)(ii)(A) of this section does not meet the requirements of paragraph (i)(4) of this section during its second taxable year beginning after December 28, 2012, its distributable amount for that second taxable year will be determined under § 1.509(a)-4T(i)(5)(ii)(B), without regard to paragraph (i)(5)(ii)(D) of this section. Any Type III supporting organization intending to meet the requirements of paragraph (i)(5) of this section in its second taxable year beginning after December 28, 2012, must value its assets in accordance with § 1.509(a)-4T(i)(8) beginning in its first taxable year beginning after December 28, 2012.

(E) *Judicial proceedings to reform instruments.* During any taxable years in which there is pending a judicial proceeding that meets the requirements of this paragraph (i)(11)(ii)(E), a non-functionally integrated Type III supporting organization organized

before September 24, 2009, will not have to comply with the distribution requirement under paragraph (i)(5)(ii) of this section to the extent such compliance would be inconsistent with mandatory provisions of a governing instrument or other instrument executed before September 24, 2009, that prohibits distributing capital or corpus. Beginning with the first taxable year following the taxable year in which such judicial proceeding is terminated, such a non-functionally integrated Type III supporting organization must satisfy the distribution requirement under paragraph (i)(5)(ii) of this section, regardless of the outcome of the judicial proceeding. Thus, if, during a taxable year after such a judicial proceeding, an organization fails to comply with paragraph (i)(5)(ii) of this section, the organization will not qualify as a non-functionally integrated Type III supporting organization, regardless of whether such failure to comply was a result of the organization operating in accordance with its governing instrument or other instrument. To meet the requirements of this paragraph (i)(11)(ii)(E), a judicial proceeding must be—

(1) Necessary to reform, or to excuse the supporting organization from compliance with, a governing instrument or other instrument (as in effect on September 24, 2009, and all times thereafter) in order to permit the organization to satisfy paragraph (i)(5)(ii) of this section;

(2) Commenced before June 26, 2013; and

(3) Not subject to any unreasonable delay for which the supporting organization is responsible.

\* \* \* \* \*

(1) *Effective/applicability date.* Paragraphs (a)(6), (f)(5), and (i) of this section are effective on December 28, 2012.

**Par. 3.** Section 1.509(a)-4T is added to read as follows:

**§ 1.509(a)-4T Supporting organizations (temporary).**

(a) through (i)(5)(ii)(A) [Reserved]. For further guidance, see § 1.509(a)-4(a) through (i)(5)(ii)(A).

(B) *Distributable amount.* Except as provided in §§ 1.509(a)-4(i)(5)(ii)(D) and 1.509(a)-4(i)(5)(ii)(E), the distributable amount for a taxable year is an amount equal to the greater of 85 percent of the supporting organization's adjusted net income (as determined by applying the principles of section 4942(f) and § 53.4942(a)-2(d) of this chapter) for the taxable year immediately preceding the taxable year of the required distribution ("immediately preceding taxable year")

or its minimum asset amount (as defined in paragraph (i)(5)(ii)(C) of this section) for the immediately preceding taxable year, reduced by the amount of taxes imposed on the supporting organization under subtitle A of the Internal Revenue Code during the immediately preceding taxable year.

(C) *Minimum asset amount.* For purposes of this paragraph (i)(5), a supporting organization's minimum asset amount for the immediately preceding taxable year is 3.5 percent of the excess of the aggregate fair market value of all of the supporting organization's non-exempt-use assets (determined under paragraph (i)(8) of this section) in that immediately preceding taxable year over the acquisition indebtedness with respect to such non-exempt-use assets (determined under section 514(c)(1) without regard to the taxable year in which the indebtedness was incurred), increased by—

(1) Amounts received or accrued during the immediately preceding taxable year as repayments of amounts which were taken into account by the organization to meet the distribution requirement imposed in § 1.509(a)–4(i)(5)(ii)(A) for any taxable year;

(2) Amounts received or accrued during the immediately preceding taxable year from the sale or other disposition of property to the extent that the acquisition of such property was taken into account by the organization to meet the distribution requirement imposed in § 1.509(a)–4(i)(5)(ii)(A) for any taxable year; and

(3) Any amount set aside under § 1.509(a)–4(i)(6)(v) to the extent it is determined during the immediately preceding taxable year that such amount is not necessary for the purposes for which it was set aside and such amount was taken into account by the organization to meet the distribution requirement imposed in § 1.509(a)–4(i)(5)(ii)(A) for any taxable year.

(i)(5)(ii)(D) through (i)(7) [Reserved]. For further guidance, see § 1.509(a)–4(i)(5)(ii)(D) through (i)(7).

(8) *Valuation of non-exempt-use assets.* For purposes of determining its distributable amount for a taxable year, a supporting organization determines its minimum asset amount, as defined in paragraph (i)(5)(ii)(C) of this section, by determining the aggregate fair market value of all of its non-exempt-use assets in the immediately preceding taxable year. For these purposes, the determination of the aggregate fair market value of all non-exempt-use assets shall be made using the valuation methods described in § 53.4942(a)–2(c) of this chapter. The aggregate fair

market value of the supporting organization's non-exempt-use assets shall not be reduced by any amount that is set aside under § 1.509(a)–4(i)(6)(v). For these purposes, the non-exempt-use assets of the supporting organization are all assets of the supporting organization other than—

(i) Assets described in § 53.4942(a)–2(c)(2)(i) through (iv) of this chapter (with “supporting organization” being substituted for “foundation” or “private foundation” and “August 17, 2006” being substituted for “December 31, 1969”); and

(ii) Exempt-use assets, which are assets that are used (or held for use) to carry out the exempt purposes of the supporting organization's supported organization(s) (determined by applying the principles described in § 53.4942(a)–2(c)(3) of this chapter) by either—

(A) The supporting organization; or  
(B) One or more supported organizations, but only if the supporting organization makes the asset available to the supported organization(s) at no cost (or nominal rent) to the supported organization(s).

(i)(9) through (l) [Reserved]. For further guidance, see § 1.509(a)–4(i)(9) through (l).

(m) *Effective/applicability date.* This section is effective on December 28, 2012. The applicability of this section expires on or before December 21, 2015.

**PART 53—FOUNDATION AND SIMILAR EXCISE TAXES**

■ **Par. 4.** The authority citation for part 53 continues to read as follows:

**Authority:** 26 U.S.C. 7805 \* \* \*

■ **Par. 5.** Section 53.4943–11 is amended by revising the section heading and adding paragraphs (f) and (g) to read as follows:

**§ 53.4943–11 Effective/applicability date.**

\* \* \* \* \*

(f) *Special transitional rule for private foundations that qualified as Type III supporting organizations before August 17, 2006.* The present holdings of a private foundation that qualified as a Type III supporting organization under section 509(a)(3) immediately before August 17, 2006, and that was reclassified as a private foundation under section 509(a) on or after August 17, 2006, solely as a result of the rules enacted by section 1241 of the Pension Protection Act of 2006, Public Law 109–280 (120 Stat. 780), will be determined using the same rules that apply to Type III supporting organizations under section 4943(f)(7).

(g) *Special transitional rule for Type III supporting organizations created as*

*trusts before November 20, 1970.* A trust that qualifies as a Type III supporting organization under section 509(a)(3) and meets the requirements of § 1.509(a)–4(i)(9) of this chapter will be treated as a “functionally integrated Type III supporting organization” for purposes of section 4943(f)(3)(A).

**PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT**

■ **Par. 6.** The authority citation for part 602 continues to read as follows:

**Authority:** 26 U.S.C. 7805.

■ **Par. 7.** In § 602.101, paragraph (b) is amended by adding the following entry in numerical order to the table to read as follows:

**§ 602.101 OMB Control numbers.**

\* \* \* \* \*  
(b) \* \* \*

CFR part or section where identified and described	Current OMB Control No.
* * * * *	* * * * *
1.509(a)–4 .....	1545–2157
* * * * *	* * * * *

**Steven T. Miller,**  
*Deputy Commissioner for Services and Enforcement.*

Approved: December 19, 2012.

**Mark J. Mazur,**  
*Assistant Secretary of the Treasury (Tax Policy).*

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**DEPARTMENT OF TREASURY**

**Internal Revenue Service**

**26 CFR Part 301**

[TD 9608]

RIN 1545–B185

**Disclosure or Use of Information by Preparers of Returns**

**AGENCY:** Internal Revenue Service (IRS), Treasury.

**ACTION:** Final regulations and removal of temporary regulations.

**SUMMARY:** This document contains final regulations that provide rules relating to the disclosure or use of tax return information by tax return preparers. These regulations provide updated guidance affecting tax return preparers regarding the use of information related to lists for solicitation of tax return