



CLIENT ALERT - NEWMAN'S OWN EXCEPTION MAKES IT EASIER FOR PRIVATE FOUNDATIONS TO HOLD BUSINESS INTERESTS

February 8, 2018

Section 4943(g) was added to the Internal Revenue Code on February 9, 2018. Informally known as “Newman’s Own”, section 4943(g) provides an exception to the private foundation excess business holding rules that will allow certain private foundations to own 100% of a privately held company indefinitely, so long as certain requirements are met.

Excess Business Holdings

Code section 4943 imposes an excise tax on a foundation’s excess business holdings. A foundation has excess business holdings when its holdings, together with those of disqualified persons, exceed 20% of the voting stock (35% in certain circumstances), profits or capital interest in a corporation or partnership. Business holdings do not include interests in a business that is substantially related to the foundation’s exempt purposes, or interests in a business at least 95% of the gross income of which is derived from passive sources.

Generally, if a foundation has excess business holdings, it must dispose of such holdings within a certain time frame depending upon how the foundation came to hold the assets. If the foundation does not dispose of its excess business holdings within the required time frame, the foundation will be subject to an excise tax that can be as high as 200% of the value of the excess business holdings.

Newman’s Own Foundation received 100% of Paul Newman’s for-profit company, No Limit, LLC, and was facing the end of its five year grace period. If Newman’s Own Foundation did not divest itself of 80% of No Limit, LLC, it would be subject to excise taxes. Then section 4943(g) was enacted.

New Exception Under 4943(g)

Section 4943(g) provides an exception to the excess business holdings excise tax in cases where the following requirements are met:

- (1) 100% of the voting stock of the business is held by the private foundation at all times during the tax year;
- (2) the ownership interests were acquired other than by purchase (i.e., by gift or bequest);
- (3) all net operating income of the business for a tax year is distributed to the private foundation within 120 days of the close of the business's tax year;
- (4) no substantial contributor to the foundation (or any family member of the contributor) serves as an officer, director, manager, or employee of the business enterprise;
- (5) a majority of the private foundation's board of directors consists of individuals who are not officers or directors (or family members of such officers or directors) of the business enterprise; and
- (6) there are no outstanding loans from the business to a substantial contributor to the private foundation or to any family member of the contributor.

The exception is effective for tax years beginning after December 31, 2017.

What This Means

Closely held businesses are a popular asset to contribute to private foundations for several reasons. Oftentimes, a family's wealth is highly concentrated in a closely held business. Equity interests can be highly appreciated and result in a high income or estate tax bill, making them a good candidate for a charitable deduction. However, the excess business holding rules have generally limited foundations from accepting such a high ownership percentage. With the Newman's Own exception, certain foundations can now indefinitely hold 100% of a closely held business. This exception is a new planning opportunity for closely held business owners who wish to leave their business to their foundation without plans to have family members control the foundation or be involved with the business, including philanthropists with no children.