



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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Contact Person:

UIL: 4942.00-00
4942.03-00
4942.03-07

Identification Number:

Telephone Number:

Employer Identification Number:

LEGEND:

K =
L =
x =
y =
z =

Dear _____ :

K requests approval of a set-aside grant under the suitability test of section 4942(g)(2) of the Internal Revenue Code.

FACTS

K is exempt from federal income tax under section 501(c)(3) of the Code and is classified as a private foundation under section 509(a).

K proposes to set aside a grant totaling \$x to L. L is a exempt from federal income tax under section 501(c)(3) of the Code and is classified as a publicly supported organization under sections 509(a)(1) and 170(b)(1)(A)(iv). No additions to the set-aside are planned.

The purpose of the grant is to restore and renovate an existing building on L's campus into a _____ ("facility"). K will pay the grant in five equal annual installments commencing y, with a final payment scheduled for z.

K represents the set-aside is necessary to provide L with a funding commitment, while

permitting K to retain control over the distribution of its funds to ensure (i) construction progresses as planned, (ii) funding is received from other sources, and (iii) contributions from K are used solely for the purpose of constructing the facility.

Funding will be conditioned upon completion of progress reports by L containing information regarding the progress of development and construction of the facility. L will provide K with a progress report every six months until L spends all grant funds. Although the agreement provides anticipated dates for the grant payments, the payments are contingent upon completion of, and the use of grant funds for, the facility.

K represents the payment period for this project will be paid out within _____ from the date the first amount of income is set aside.

LAW

Section 4942 of the Code imposes an excise tax on any private foundation that does not expend qualifying distributions for exempt purposes at least equal to its distributable amount for its tax year.

Section 4942(g)(1) of the Code, in substance and generally, defines "qualifying distribution" as any amount paid for tax exempt purposes as defined in section 170(c)(2)(B) of the Code.

Section 4942(g)(2)(A) of the Code provides an amount of income set aside for a specific project within one or more purposes of section 170(c)(2)(B) of the Code may be treated as a qualifying distribution if the amount meets the set-aside requirements of section 4942(g)(2)(B) of the Code.

Section 4942(g)(2)(B) of the Code provides, in pertinent part, an amount set aside for a specific project may be treated as a qualifying distribution if, at the time of the set-aside, the private foundation establishes to the satisfaction of the Secretary the amount set aside will be paid for the specific project within five years and the suitability test for a set-aside under section 4942(g)(2)(B)(i) of the Code is met.

Section 4942(g)(2)(B)(i) of the Code provides a suitability test in which the private foundation at the time of the set-aside must establish to the satisfaction of the Secretary the specific project is one that can better be accomplished by the set-aside of income rather than by the immediate payment of funds (the "suitability test").

Section 53.4942(a)-3(b)(1) of the Foundation and Similar Excise Taxes Regulations provides the amounts of income set aside for a specific project for one or more of the purposes in section 170(c)(1) or 170(c)(2)(B) of the Code may be treated as qualifying distributions for the tax year(s) in which such amounts are set aside, but not in the tax year in which actually paid, if the requirements of section 4942(g)(2)(B)(i) of the Code are met, the foundation establishes to the satisfaction of the Commissioner the amount set aside will be paid for the specific project

within 60 months after it is set aside, and the set-aside otherwise meets the suitability test of section 53.4942(a)-3(b)(2) of the regulations.

Section 53.4942(a)-3(b)(2) of the regulations provides its suitability test for a set-aside is met if the foundation establishes the specific project is one in which relatively long-term grants or expenditures must be made in order to assure the continuity of particular charitable projects or program-related investments. The regulation cites as an example of a suitable project a plan to fund a specific research program that is of such magnitude as to require an accumulation of funds before beginning the research, even though not all of the details of the program have been finalized.

Section 53.4942(a)-3(b)(7)(i) of the regulations provides a private foundation must obtain Internal Revenue Service approval of its set-aside of income under the suitability test by applying before the end of the tax year in which the amount is set aside.

ANALYSIS

K is an exempt private foundation and its set-aside of income for a specific project is within the charitable purposes of section 170(c)(2)(B) of the Code. K's project is better accomplished by a set-aside of income, rather than by immediate payment of funds, because this set-aside will allow K to retain control over the distribution of its funds to ensure (i) construction progresses as planned, (ii) funding is received from other sources, and (iii) contributions from K are used solely for the purpose of constructing the facility. K has sought timely approval of its set-aside of income in advance of the time when the amounts of income are to be set aside. K represents its income to be set aside for this specific project will be paid out within _____ from the time when the first amount is set aside.

RULING

Based on the foregoing, we rule a set-aside of funds in the amount \$x, satisfy the requirements of section 4942(g)(2)(B)(i) of the Code and section 53.4942(a)-3(b)(2) of the regulations. Accordingly, the proposed set-asides may be treated as qualifying distributions in its tax year(s) when such amounts are set aside.

Section 53.4942(a)-3(b)(8) of the regulations provides any set-aside approved by the Internal Revenue Service must be evidenced by the entry of a dollar amount in the books and records of a private foundation as a pledge or obligation to be paid at a future date or dates. Further, the amount of the set-aside must be taken into account in determining the foundation's minimum investment return (see section 53.4942(a)-2(c)(1) of the regulations), and any income attributable to a set-aside must be taken into account in computing adjusted net income (see section 53.4942(a)-2(d) of the regulations).

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

Pursuant to a Power of Attorney on file in this office, a copy of this letter is being sent to the authorized representative. This ruling letter does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described.

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

Please keep a copy of this ruling letter in your permanent records.

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

Sincerely,

Debra J. Kawecki
Manager, Exempt Organizations
Technical Group 1

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