



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Release Number: **201001022**
Release Date: 1/8/10
Date: 10/16/2009

Uniform Issue List:
4942.03-07

Legend:

H =
S =

Date1 =
Date2 =
Date3 =

Dear

This is in reply to your ruling request dated Date1, for authorization to make a set-aside in the amount of S for a purpose described in section 53.4942(a)-3(a)(2) of the Foundation and Similar Excise Taxes Regulations, because you are precluded from making a qualifying distribution for that year by a court order.

FACTS

On Date2, you ceased operating as a hospital and were designated a private foundation under section 509(a) of the Internal Revenue Code. You are subject to section 4942(g), requiring, in general, a minimum annual distribution for exempt purposes.

You continue to remain subject to significant, contingent liabilities that arose prior to the asset sale ending your function as a hospital. Also, you are subject to an "18 plus one" rule under state law, whereby all infants born at your hospital facility, prior its end, have until the age of 18 plus one year to file medical malpractice claims against you.

Significantly, you remain under a state court order providing that, while pending and potential claims exist, none of your assets may be expended, except for your own ordinary and necessary operating expenses or in accord with that court's orders.

You have requested authority to make a set-aside under section 53.4942(a)-3(b)(9) of the regulations, for your tax year ending Date3, in the amount of S for a purpose described in section 53.4942(a)-3(a)(2) of the regulations, because you are precluded from making a qualifying distribution for that year by a court order.

LAW

Section 4942(a) of the Code imposes tax on any private foundation that fails to distribute the required annual distribution for exempt purposes. Absent a set-aside approved by the Service for each tax year, the qualifying distribution for exempt purposes must be made before the first day of the second tax year following the tax year concerned.

Section 4942(g)(2) of the Code provides that an amount set-aside for an approved purpose may be treated as a qualifying distribution.

Section 53.4942(a)-2(d)(2)(iii)(c) of the regulations provides that any amount set aside under paragraph (b) of section 53.4942(a)-3, to the extent it is determined that such amount is not necessary for the purposes for which it is set aside, shall be included in the gross income for the taxable year.

Section 53.4942(a)-3(a)(2) of the regulations defines the term "qualifying distribution," in relevant part, to mean any amount paid to accomplish one or more purposes described in section 170(c)(1) or (2)(B) of the Code, other than any contribution to a private foundation which is not an operating foundation or to an organization controlled (directly or indirectly) by the contributing private foundation or one or more disqualified persons with respect to such foundation.

Section 53.4942(a)-3(b)(9) of the regulations provides that in the event that a private foundation is involved in litigation and may not distribute assets or income because of a court order, the private foundation may seek and obtain a set-aside for a purpose described in section 53.4942(a)-3(a)(2). The amount of the set-aside shall be equal to that portion of the private foundation's distributable amount which is attributable to the assets or income that are held pursuant to court order and which, but for the court order precluding the distribution of such assets or income, would have been distributed. In the event that the litigation encompasses more than one taxable year, the private foundation may seek additional contingent set-asides.

ANALYSIS

You may not distribute your assets except to the extent provided by a court order reserving your assets for possible liabilities. Because of the court order, you cannot make a qualifying distribution as defined under section 53.4942(a)-3(a)(2) of the regulations and therefore you cannot avoid the initial tax under section 4942(a) of the Code without a set-aside. Section 53.4942(a)-3(b)(9) of the regulations specifically addresses the situation in which a court order prevents a private foundation involved in litigation from making its full required distribution. It directs such a private foundation to seek permission for a set-aside for a purpose described in section 53.4942(a)-3(a)(2). Under Code section 4942(g)(2), the amount of the set-aside will be treated as a qualifying distribution.

Because no portion of your assets, aside from your own operating expenses, may be distributed while the court order is pending, the amount you seek to set aside is equal to the entire portion of the distributable amount you would have distributed for a purpose described in section 53.4942(a)-3(a)(2). Your situation is exactly like that provided for in section 53.4942(a)-3(b)(9) of the regulations. Accordingly, we rule that you may make a set-aside for tax year ending Date3 in the amount of \$.

We direct your attention to section 53.4942(a)-3(b)(8) of the regulations, entitled "Evidence of set-aside." That section provides that a set-aside approved by the Internal Revenue Service shall be evidenced by the entry of a dollar amount on the books and records of the private foundation as a pledge or obligation to be paid at a future date or dates. Section 53.4942(a)-3(b)(9) states that the set-aside must actually be distributed by the last day of the taxable year following the taxable year in which the litigation is terminated. Amounts not distributed by the close of the appropriate taxable year shall be treated as described in section 53.4942(a)-2(d)(2)(iii)(c) during the succeeding year.

RULING

You may make a contingent set-aside in the amount of \$, under section 53.4942(a)-3(b)(9) of the regulations, that will be treated as a qualifying distribution under section 4942(g)(2) of the Code for your tax year ending Date3.

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes in these facts. Any changes that may have a bearing upon your tax status should be reported to the Service. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept in your permanent records. Pursuant to a Power of Attorney on file in this office, a copy of this letter is being sent to your authorized representative.

Except as we have specifically ruled herein, we express no opinion as to the consequences of this transaction under the cited provisions or under any other provision of the Code.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

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

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

Sincerely,

Manager, Exempt Organizations
Technical Group 2

Enclosure
Notice 437