

**Internal Revenue Service
Director, Exempt Organizations**

**Department of the Treasury
P.O. Box 2508
Cincinnati, Ohio 45201**

Number: **201128033**
Release Date: 7/15/2011

Date: April 18, 2011

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

**UIL LIST:
4942.03-07**

Dear :

This is in reply to your written request for approval of certain set-asides under section 4942(g)(2) of the Internal Revenue Code. You have been recognized as exempt under section 501(c)(3) of the Code and have been determined to be a private foundation under section 509(a) of the Code.

As we previously informed you, we requested technical advice about your request for advance approval of the set asides. The attached copy of the technical advice memorandum sets forth the specific terms and conditions under which your request has been approved.

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

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,

Lois Lerner
Director, Exempt Organizations

Enclosures:
Unredacted copy of Technical Advice Memorandum
Notice 437
Redacted copy of this letter
Redacted Copy of Technical Advice Memorandum

INTERNAL REVENUE SERVICE
TEGE TECHNICAL ADVICE MEMORANDUM

Manager, EODQA
Cincinnati, OH

Taxpayer's Name:

Taxpayers Address:

Taxpayers ID No.:

Years Involved:

Conference Held:

Legend

Taxpayer =
Counties =
City =
Hospital1 =
Hospital2 =
Date =
Clinics =
Medical Center =
Total Amount =
Amount1 =
Amount2 =
Amount3 =
Amount4 =
Amount5 =
TaxYear1 =
TaxYear2 =
TaxYear3 =
TaxYear4 =
TaxYear5 =
x =

Issue:

Whether Taxpayer's request to set aside Total Amount over a period of 60 months meets the suitability test for a set-aside under section 4942(g)(2)(B) of the Internal Revenue Code (the Code).

Facts:

Taxpayer is exempt under section 501(c)(3) of the Code and classified as a private foundation under section 509(a). Taxpayer was formed to facilitate and support healthcare services and programs in City and Counties.

Taxpayer was funded by the proceeds of the sale of a hospital facility by a City healthcare provider to a regional health care provider. On Date, Hospital1, a healthcare provider located in City sold all of its operating assets to Hospital2, a multiple facilities healthcare provider in the region. Both organizations are exempt under section 501(c)(3) of the Code. The sales agreement guarantees that Hospital2 will continue healthcare operation in City for five years, and gave Taxpayer the right and option to repurchase the assets at fair market value if Hospital2 proposes to close the healthcare facility in City. The option to repurchase shall terminate fifteen years after the date of sale. A primary purpose of Taxpayer is to exercise the option, if the opportunity arises, to ensure that the healthcare facility continues to operate in the community.

In post-conference letters dated July 20, 2010 and September 8, 2010, Taxpayer amended and supplemented its requests of set-asides. Taxpayer is requesting the set-aside of Total Amount of which Amount1 is set aside in TaxYear1, Amount2 in TaxYear2, Amount3 in TaxYear3, Amount4 in TaxYear4, and Amount5 in TaxYear5.

The set aside of Total Amount will be used in exercising its option to reacquire the healthcare facility if Hospital2 decides to close the facility. The reacquisition will enable Taxpayer to maintain hospital and other healthcare services for residents of City and Counties.

If the healthcare facility is not purchased, Taxpayer will use the amount of set-aside to assist in funding the relocation and expansion of Clinics, a medical clinic of Medical Center, which is owned and operated by Hospital2. Clinics is in the City campus of Medical Center and will be relocated to a vacant long-term wing of the hospital facility. The relocation and expansion of Clinics (the Project) is estimated to cost \$x and will include design costs, construction costs, equipment purchase, parking lot improvements and other improvements. Taxpayer has received a written estimate of the total estimated cost of the Project, including the estimated cost for phase 1 of the relocation work of approximately 47% of the total estimated cost of the Project. Taxpayer also has current and post-construction floor plans. Taxpayer represents that Hospital2 is involved in the funding of the Project, and the availability of Taxpayer's fund for it will act as a catalyst for community financial support for the Project.

Taxpayer will distribute the Total Amount set-aside within 60 months after the date of the first set-aside.

Applicable Law

Section 4942(g)(a) of the Code imposes a tax on the undistributed income of a private foundation for any taxable year, which has not been distributed before the first day of the second (or any succeeding) taxable year following such taxable year (if such first day falls within the taxable period).

Section 4942(c) of the Code defines the term "undistributed income" to mean, with respect to any private foundation for any taxable year as of any time, the amount by which (1) the

distributable amount for such taxable year, exceeds (2) the qualifying distributions made before such time out of such distributable amount.

Section 4942(d) of the Code defines the term "distributable amount" to mean, with respect to any foundation for any taxable year, an amount equal to (1) the sum of the minimum investment return plus the amounts described in subsection (f)(2)(C), reduced by (2) the sum of the taxes imposed on such private foundation for the taxable year under subtitle A and section 4940.

Section 4942(g)(1) of the Code defines "qualifying distribution" as (A) any amount paid to accomplish one or more purposes described in section 170(c)(2)(B), other than any contribution to (i) an organization controlled by the foundation or one or more disqualified persons, or (ii) a private foundation which is not an operating foundation, except as otherwise provided; (B) any amount paid to acquire an asset used directly in carrying out one or more purposes described in section 170(c)(2)(B).

Section 4942(g)(2)(A) of the Code provides that, for all taxable years beginning on or after January 1, 1975, an amount set aside for a specific project within one or more purposes of section 170(c)(2)(B) may be treated as a qualifying distribution if the amount meets the requirements of section 4942(g)(2)(B).

Section 4942(g)(2)(B)(i) of the Code provides that an amount set aside for a specific project may be treated as a qualifying distribution if, at the time of the set-aside, the foundation establishes to the satisfaction of the Secretary the amount set aside will be paid for the specific project within five years, and 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 Tax Regulations provides that 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 in the year in which set aside (but not in the tax year in which actually paid) if the requirements of section 4942(g)(2) and this paragraph (b) are satisfied. The requirements of this paragraph (b) are satisfied if the foundation establishes to the satisfaction of the Commissioner that the amount set aside will be paid for the specific project within 60 months after it is set aside, and (i) the set-aside otherwise meets the suitability test of section 53.4942(a)-3(b)(2) or (ii) the foundation satisfies the cash distribution test described in section 53.4942(a)-3(b)(3). If the suitability test or cash distribution test is otherwise satisfied, the 60 month period for paying the amount set aside may for good cause shown, be extended by the Commissioner.

Section 53.4942(a)-3(b)(2) of the regulations provides that the suitability test is satisfied if the private foundation establishes to the satisfaction of the Commissioner that the specific project for which the amount is set aside is one that can be better accomplished by the set aside than by the immediate payment of funds. Specific projects that can be better accomplished by the use of a set-aside include, but are not limited to, projects 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, or where grants are made as part of a matching-grant program. Such projects include, for example, a plan to erect a building to house the direct charitable, educational, or similar exempt activity of the private foundation, or 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) of the regulations provides that a private foundation must obtain approval of the set-aside under the suitability test by applying before the end of the taxable year in which the amount is set aside.

Section 52.4942(a)-3(b)(7)(i)(e) of the regulations provides that a private foundation must include a statement by an appropriate foundation manager (as defined in section 4946(b)) that the amounts to be set aside will actually be paid for the specific project within a specified period of time that ends not more than sixty months after the date of the first set-aside, or a statement showing good cause why the period for paying the amount set aside should be extended (including a showing that the proposed project could not be divided into two or more projects covering periods of no more than 60 months each) and setting forth the extension of time required.

Rev. Rul. 77-7, 1977-1 C.B. 354, held that a private foundation's set aside of accumulated funds to endow a specific building project of an unrelated public charity is a set-aside of funds for a "specific project" as such term is defined in section 53.4942(a)-3(b)(2) of the regulations.

In Rev. Rul. 74-450, 1974-2 C.B. 388, a private operating foundation planned to set-aside excess earnings for four years to fund a four-year construction plan of converting a portion of its newly acquired land into an extension of its existing wildlife sanctuary and the remainder into a public park. The ruling held that the private operating foundation's plan accomplishes section 170(c)(2)(B) purposes and constitutes a "specific project" for which an amount may be set aside and treated as a qualifying distribution under section 4942(g)(2).

Analysis

Taxpayer's proposed project for the proposed relocation and expansion of the Clinics is like the charitable projects described in Rev. Ruls. 74-450 and 77-7 and qualifies as a "set aside" within the meaning of section 4942(g)(2)(A) of the Code and the accompanying Regulations. Taxpayer has established to our satisfaction that the relocation and improvement is better accomplished by a set aside than by immediate payment of funds, and the amount of the set aside will be paid for the relocation and improvement within five years unless some or all of such funds are first utilized for the repurchase of the healthcare facility.

Taxpayer's proposal to repurchase the healthcare facility is a contingent proposal that does not qualify as a "set aside" within the meaning of the Code and Regulations. The repurchase cannot be accomplished by immediate payment of funds, but it is speculative whether the repurchase will occur within 5 years, or even within the 15 year period. Thus, the repurchase does not meet the requirement under section 4942(g)(2)(B) that the foundation establish that the amount set aside will be paid within 5 years.

Our analysis that Taxpayer's Clinics project qualifies as a set aside under section 4942(g)(2)(A) is not changed by the fact that the contingency may occur that would cause Taxpayer to use some or all of the Clinics set aside funds to repurchase the healthcare facility prior to use for Clinics under the 5 year requirement. The facts establish to our satisfaction that the Clinics project is a serious and significant charitable endeavor of Taxpayer that will be fulfilled barring the occurrence of a double contingency --- (1) closing of a hospital, and (2) the decision by Taxpayer to exercise an option to purchase used assets at fair market value.

Therefore, Taxpayer's total set-aside of the Total Amount in which Amounts1, Amounts2, Amounts3, Amounts4, and Amounts5, will be set aside in TaxYear1, TaxYear2, TaxYear3,

TaxYear4, and TaxYear5, respectively, meets the requirements of section 4942(g)(2)(B)(i), and the amounts set aside constitute qualifying distributions under section 4942(g).

Taxpayer must provide evidence of set-aside as required under section 53.4942(a)-3(b)(8) of the regulations. Under that section, any set-aside approved by the Internal Revenue Service shall 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 under 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 under section 53.4942(a)-2(d).

A copy of this technical advice memorandum is to be given to the taxpayer. Section 6110(k)(3) of the Code provides that it may not be used or quoted as precedent.

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