

**Internal Revenue Service  
Director, Exempt Organizations**

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

**Number: 201134024**  
**Release Date: 8/26/2011**

**Date: June 2, 2011**

**Contact Person:**

**Identification Number:**

**Telephone Number:**

**Employer Identification Number:**

**UIL: 4942.03-07**

**LEGEND**

A = State  
B = Name of Hospital Beneficiary 1 of Trust  
C = Name of Health Care System  
D = Name of Hospital Beneficiary 2 of Trust  
F = Name of Hospital  
G = Name of Court  
H = Date of B's closure  
R = Date of Sale of B's assets to F  
J = Date of petition Filing  
K = Date of G's order to suspend distributions  
L = Date of Judgement Entry  
M = Date by which set-aside must be distributed  
N = Location of F –New Beneficiary under Trust  
v = \$ Amount of contingent set-aside.  
w = \$ Amount distributed to C in 2009  
x = \$ Amount distributable for 2008  
y = \$ Amount distributable for 2009

**Dear :**

Your letter dated December 31, 2009 requested approval of a contingent set-aside under section 53.4942(a)-3(b)(9) of the Foundation Excise Taxes Regulations for the taxable year ended December 31, 2009.

You have been recognized as exempt under section 501(c)(3) of the Internal Revenue Code of 1986. You were previously a supporting organization described in section 509(a)(3) of the Code, but were reclassified as a private nonoperating foundation described in Section 509(a) effective January 1, 2008.

## FACTS

You are a charitable trust under the laws of the state of A. According to the terms of your trust instrument, you must distribute annually the income of your endowment in equal parts to hospitals B and D, for programs and equipment benefiting children. B was not separately incorporated, but a program or division of C. .

On H, beneficiary B closed its doors and on R the assets were sold to F. On J you filed in the G, a Petition to Modify Trust and to Apply the Doctrines of Cy Pres and Deviation citing the closure of B as the reason for the petition and seeking instructions how you should redirect the distributions payable to B under the terms of the trust. Distributions to D have not been interrupted. Both C and F put forward claims to the succession to B's interest under the doctrine of Cy Pres. C filed for bankruptcy, resulting in an automatic stay in proceedings in your case, from which you had to obtain relief. F then objected to C's request that the distributions be made to C as scheduled until G has rendered its decision.

On K, G ordered you to make no current or future distributions to C until the issues relating to the entitlement of the funds were settled by the court, with the exception of \$w, due to C for the period prior to the closing of B. The requested set-aside of \$v is for the amounts which, but for the court order, would have been distributed by December 31, 2009, to the successor to B's interest. These consist of the distributable amounts for 2008 and 2009, \$x and \$y, respectively, less \$w, which was distributed to C in 2009 as ordered by the court.

On L, G rendered its decision in the case. As per G's Decree, F of the N was substituted as a residual beneficiary under the Trust.

## LAW

Section 4942(a) of the Internal Revenue Code imposes an excise 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. For purposes of section 4942, the term "distributed" means distributed as qualifying distributions under section 4942(g).

Section 4942(c) defines "undistributed income" as the amount by which the distributable amount for such taxable year, exceeds the qualifying distributions made before such time out of such distributable amount.

As defined by Section 4942(d) the computation of the "distributable amount" for a taxable year is based on the private foundation's minimum investment return for that year, as defined in Section 4942(e).

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 53.4942(a)-2(d)(2)(iii)(c) of the Foundation and Similar Excise Taxes Regulations includes in gross income for the taxable year any amount set aside under Section 53.4942(a)-3(b) to the extent it is determined that such amount is not necessary for the purposes for which it was set aside.

Section 53.4942(a)-3(a)(2)(iii) of the Regulations defines as a qualifying distribution, in relevant part, to mean, any amount set aside within the meaning of paragraph (b) of section 3.

Section 53.4942(a)-3(b)(9) of the Regulations provides that if 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 the purpose described in section 53.4942(a)-3(a)(2). The amount to be 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. Such amounts 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 Sec. 53.4942(a)-2(d)(2)(iii)(c) for the succeeding taxable year.

## ANALYSIS

While litigation was pending, a court order prevented you from making the distributions which are the subject of the set-aside. These are precisely the circumstances described in section 53.4942(a)-3(b)(9) of the regulations.

Section 53.4942(a)-3(b)(9) states that the set-aside amount must actually be distributed by the last day of the taxable year following the taxable year in which the litigation is terminated. The litigation having terminated on L, you must distribute the set-aside amount \$v to F by M. If not distributed by this date the undistributed part of the set-aside shall be treated as described in section 53.4942(a)-2(d)(2)(iii)(c) for the succeeding tax year.

## RULING

Accordingly, we rule that, \$v, the amount which would have been distributed before

December 31, 2009, but for the court order precluding the distribution of such assets or income, qualifies as a contingent set-aside described in Section 53.4942(a)-3(b)(9) for said taxable year.

This ruling is based on the understanding there will be no material changes in the facts upon which it is based. Any changes that may have a bearing on your tax status should be reported to the Internal Revenue Service. This ruling does not address the applicability of any section of Code or regulations to the facts submitted other than with respect to the sections described.

We direct your attention to Section 53.4942(a)-3(b)(8) of the regulations, entitled "Evidence of Set-Aside." This section provides that 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 (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 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.

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 the 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.

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 yours,

Lois G. Lerner  
Director, Exempt Organizations

Enclosure:

Notice 437  
Redacted copy of Letter