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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

200204037

Date: OCT 29 2001

Contact Person:

Uniform Issue List: 4942.03-07

Identification Number:

Telephone Number:

T:EO:B2

Employer Identification Number:

LEGEND:
B =
C =
D =
E =

Dear Sir or Madam:

We have considered your ruling request dated December 19, 2000, in which you requested approval of a proposed set-aside of your income under the suitability test of section 4942(g)(2)(B)(i) of the Internal Revenue Code (the "Code") and section 53.4942(a)-3(b)(i) of the Foundation and Similar Excise Taxes Regulations (the "regulations").

You, B, are recognized as exempt from federal income tax as a charitable organization under section 501(c)(3) of the Code, and are classified as a private foundation within the meaning of section 509(a).

You wish to set aside a grant totaling $500,000 to C. C is exempt from federal income tax under section 501(c)(3), and is classified as a public charity under section 509(a)(2). No additions to the set-aside are planned.

The purpose of the grant is to restore and renovate an historic site, known as D, which is operated and maintained by C. C has proposed to renovate and restore D (the "Restoration Project") to the conditions that existed in 1867. The cost of the Restoration Project is estimated at $1,500,000.

Your grant is subject to an agreement with C. Under the agreement, you shall make a grant of $500,000 to C to partially fund the costs of the Restoration Project (the "Restoration Grant"). You shall disburse the funds to C in installments not more frequently than monthly upon receipt from C of a payment request itemizing the amounts required to be paid to architects, engineers, material suppliers, contractors, or others for costs incurred for the work for which your gift is restricted.

Your obligation to make the gift to C is subject to the following conditions precedent:

(a) On or before December 15, 2000, C shall provide you with satisfactory evidence that E has arranged engineering and supervisory services for the Restoration Project.

(b) On or before December 31, 2002, you shall have received satisfactory assurances that C has received additional contributions or committed its own funds to support the Restoration Project in an amount not less than $1,000,000.

(c) On or before March 31, 2002, (i) you shall have received and approved in writing the drawings, plans, and specifications of the Restoration Project; and (ii) you shall be satisfied that C has sufficient funding to complete the Restoration Project.

(d) Prior to the disbursement of any portion of the Restoration Grant, you shall have approved in writing the contractors, vendors, and finally awarded contracts for the Restoration Project.

(e) At the time of disbursement of the Restoration Grant, C shall not be in default in the performance of any of its obligations under the Agreement.

Should any of the conditions not be satisfied, and should you be unwilling to waive the same, then your obligation to make the Restoration Grant may be terminated.

You state that the set-aside was made as of November 27, 2000, and that the amounts set aside must and will actually be paid for the Restoration Project within a period of time that ends not more than 60 months from the date of the set-aside. Your agreement with C requires that payments of the Restoration Grant be requested on or before March 31, 2005, which is less than 60 months from the date of the set-aside.

You state that your grant to C, as part of a matching-grant program, is intended to stimulate grants to C from the community at large. Furthermore, because of the extended period of time required to perform repairs and renovations, a set-aside grant payable over the renovation period as costs are incurred is the most appropriate means to accomplish the renovation and ensure that the grant is utilized to pay for the intended renovations. In addition, because of your concern with the preservation and architectural features of D, you believe it is crucial that you retain a degree of control over the architectural plans and construction process. By making the disbursement of the funds over the period dependent upon approval of architectural design and construction progress, you believe you can best meet the goal of preserving D.

Section 4942(a) of the Code imposes on the undistributed income of a private foundation for any taxable year, which has not been distributed before the first day of the second taxable year following such taxable year, a tax equal to 15 percent of the amount of such income remaining undistributed at the beginning of such second taxable year.

Section 4942(c) of the Code provides that, for purposes of section 4942, the term "undistributed income" means, with respect to any private foundation, for any taxable year as of any time, the amount by which (1) the distributable amount for each taxable year, exceeds (2) the qualifying distributions made before such time out of such distributable amount.

Section 4942(g)(1) of the Code defines the term "qualifying distribution," in general, as any amount paid to accomplish one or more purposes described in section 170(c)(2)(B), or 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 an amount of income that is set aside for a specific project which comes within one or more purposes described in 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).

Section 4942(g)(2)(B) of the Code provides, in pertinent part, 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 private foundation establishes to the satisfaction of the Secretary that the amount set aside will be paid for the specific project within five years and that the suitability test for a set-aside under section 4942(g)(2)(B)(i) 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 that the specific project is one that can better be accomplished by the set-aside of income rather than by the immediate payment of funds.

Section 53.4942(a)-3(b)(1) of the regulations provides that an amount set aside for a specific project that is for one or more of the purposes described in section 170(c)(1) or (2)(B) of the Code may be treated as a qualifying distribution in the year in which set aside (but not in the 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 that the amount set aside will be paid for the specific project within 60 months after it has been 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 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 a 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 (as defined in section 4944(c)) 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 other similar exempt activity of the private foundation, even though the exact location and architectural plans have not been finalized.

Rev. Rul. 77-7, 1977-1 C.B. 354, holds that the term "specific project" includes a building project to be undertaken by a public charity unrelated to the foundation making the set aside.

Section 53.4942(a)-3(b)(7)(i) of the regulations provides that if an amount is set aside under the suitability test of section 4942(g)(2)(B)(i) of the Code and section 53.4942(a)-3(b)(2) of the regulations, the private foundation must apply for the Commissioner's approval of the set-

aside before the end of the taxable year in which the amount is set aside.

You have timely sought approval of your set-aside of income in advance of the time when the amounts of income are to be set aside, as required by section 4942(g)(2)(B)(i) of the Code and section 53.4942(a)-3(b)(7)(i) of the regulations.

Your set-aside of $500,000 as a matching-grant will be for specific projects within the charitable purposes of section 170(c)(2)(B) of the Code, as required by section 4942(g)(2)(A) of the Code and section 53.4942(a)-3(b)(2) of the regulations.

You represent that the amount set aside for this specific project will be paid out for this project within 60 months from the time it is set aside as required by section 4942(g)(2)(B) of the Code and section 53.4942(a)-3(b)(1) of the regulations.

Your project is better accomplished by this set-aside of income, rather than by immediate payment, under the suitability test of section 4942(g)(2)(B)(i) of the Code because, under the matching-grant provision of section 53.4942(a)-3(b)(2) of the regulations, this set-aside will allow continuous funding of your matching grant to C as allowed by that regulation. Thus, your specific project of providing a matching-grant to C meets the requirements for a set-aside of income under the suitability test of section 4942(g)(2)(B)(i) of the Code and section 53.4942(a)-3(b)(2) of the regulations.

Accordingly, we rule that up to $500,000 of your income to be set aside for the matching-grant to C will be treated as a qualifying distribution under section 4942(g)(2)(B)(i) of the Code and section 53.4942(a)-3(b)(2) of the regulations in your tax year when such amount is set aside.

For your information, section 53.4942(a)-3(b)(8) of the regulations provides that any set-aside approved by the Internal Revenue Service must be evidenced by the entry of a dollar amount in your books and records 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 your 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 your adjusted net income (see section 53.4942(a)-2(d) of the regulations).

Because this ruling letter could help to resolve any questions, please keep it in your permanent records and include a copy with your annual return, Form 990-PF.

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.

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

Sincerely,

(signed) Terrell M. Berkovsky

Terrell M. Berkovsky
Manager, Exempt Organizations
Technical Group 2