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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: APR 17 2003

Contact Person:

UIL 4942.00-00

Identification Number:

Telephone Number:

T:EO:B4

Employer Identification Number:

B=
C=
D=
E=
F=
x=
y=

Dear Sir or Madam:

This is in response to a letter dated December 27, 2002, which requested rulings on a contingent set-aside under section 53.4942(a)-3(b)(9) of the Foundation and Similar Excise Taxes Regulations.

B was created on April 12, 2001, and received a letter from the Internal Revenue Service dated July 2, 2001, granting exempt status under section 501(c)(3) of the Internal Revenue Code and classification as a private foundation under section 509(a).

B received all of its funding in July 2001, by a bequest from C after her death. C left a gross estate consisting principally of parcels of rental real estate held in a funded revocable trust named D. Based on the estate tax return filed for C's estate, these properties had a net fair market value of x on the date of C's death.

Under the terms of D, as amended prior to C's death, the trustees of D were directed, upon C's death, to distribute all property then held in D to B. Pursuant to this direction, all the properties were transferred to B.

On August 14, 2001, several of C's relatives filed an equity complaint with E. The claimants challenged (i) the validity of Wills executed by C in 1994 and 2001, and/or (ii) the validity of amendments C made to D in the months preceding her death, and/or (iii) the legality of the funding of D. Moreover, the claimants have requested that their legal fees be paid by C's estate.

A temporary restraining order was issued by E precluding B from taking any action with respect to the property held by B; and at a September, 2001 hearing, a preliminary injunction was issued to the same effect. In late September, 2001, B filed a motion seeking a relaxation of the preliminary injunction, asserting that the property needed to be maintained and managed, that rents had to be collected and bills paid, and that the preliminary injunction paralyzed all of those actions. After a hearing on the motion, the court denied the motion, but the court appointed F as a receiver of B, pending resolution of the aforementioned claims.

Under the terms of the court appointment, the receiver is granted only limited powers relating to B's operation pending outcome of the litigation, such as the power to maintain rental real estate held by B and to file relevant tax returns. Such powers do not include the power to make distributions in furtherance of B's charitable purpose. The limitation on the receiver's powers applies to all of B's assets, including principal and income. B appealed the preliminary injunction. That appeal was denied.

On October 10, 2001, a petition for administration was filed by C's two sisters, seeking, among other things, to have the 2001 Will disallowed due to unsound mind and undue influence. In addition, on October 18, 2001, a petition to probate a copy of the 2001 Will was filed by the named co-executors of the 2001 Will, and on April 29, 2002, a petition to probate the 1994 Will was filed by the named successor executor of the 1994 Will. Depending on the success of these claims, B may lose its right to retain some or all of its assets.

Based on a draft of the Form 990-PF for B for 2001, and assuming that B is entitled to retain all property that it has received to date pending the ongoing litigation, B's distributable amount for income earned in 2001(as defined in section 4942(f) of the Code) that was to be distributed by December 31, 2002 is y.

Section 4942(a) of the Code provides that there is hereby imposed 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), a tax equal to 15 percent of the amount of such income remaining undistributed at the beginning of such second (or succeeding) taxable year.

Section 53.4942(a)-3(b)(9) of the regulations provides that in the event a private foundation is involved in litigation and may not distribute assets or income because of a court order, the private foundation may (except as provided in section 53.4942(a)-2(e)(1)(i) or (ii) 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 section 53.4942(a)-2(d)(2)(iii)(c) for the succeeding taxable year.

B has provided representations and documentation that a contingent set-aside is appropriate due to a court order which prohibits it from making expenditures until pending litigation is resolved.

Based on the foregoing, we rule that B can make a contingent set-aside for the tax year ending December 31, 2002. The amount to be set-aside is equal to the entire portion of B's 2002 distributable amount, because no portion of B's assets, aside from operating expenses, may be distributed while litigation is pending. Based on B's preliminary calculations, the set-aside amounts should be approximately y. When a final determination is made as to the assets, if any, to which B is entitled, B will, by the end of the taxable year in which such final determination is made, make a qualifying distribution of the distributable amount attributable to B's assets.

We direct your attention to section 53.4942(a)-3(b)(4) of the regulations, entitled "Evidence of set-aside". This 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 a private foundation as a pledge or obligation to be paid at a future date or dates.

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

We are informing the Ohio TE/GE office of this action. Please keep a copy of this ruling with your organization's permanent records.

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.

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,

Gerald V. Sack

Gerald V. Sack
Manager, Exempt Organizations
Technical Group 4