Uniform Issue List
4942.03-07
4942.03-05
4942.03-01
4942.03-02

199943051

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

AUG 5 1999

Contact Person:

ID Number:

Telephone Number:

OP:E:EO:T:4

Employer Identification Number:
Key District:

Legend:

M =
N =
0 =
P=
Q=
R=
S=
T=
x=

Dear Applicant:

This is in response to the ruling requests contained in your letter dated March 9, 1999, wherein you requested a ruling that a set-aside of funds be recognized as satisfying the suitability test of section 4942(g)(2)(B)(i) of the Internal Revenue Code and section 53.4942(a)-3(b) (2) of the Foundation Excise and Similar Taxes Regulations.

M is a trust that was formed in September, 1997. The Trust Agreement provides, in part, that M may (1) make distributions to charitable organizations, or (2) make payments directly for charitable purposes, without making use of an intermediary organization, provided that in each case the funds are used in ten identified counties located in three States, N, 0, and P. M has been recognized by the Service as exempt from federal income tax as an organization described in section 501(c) (3) of the Code and has been classified as a private foundation under section 509(a).

As of August 31, 1998, the fair market value of M's net assets for purposes of computing M's minimum investment return was approximately $278x. M requests approval to set aside (1) an amount equal to approximately $13.5x earned in the taxable year ending August 31, 1998,and payable in the taxable year ending August 31, 1999, and (2) the lesser of approximately $12.2 x or its minimum distributable amount for the taxable year ending August 31,1999, and payable in the taxable year ending August 31, 2000, so that these amounts will be treated as qualifying distributions under Code section 4942(g) in the taxable years ending August 31, 1999, and August 31, 2000.

277

M plans to undertake a life quality and health care initiative (the "Project"), which initially will be a two-year evaluation of the efficacy of the T Healthcare system. This system has been developed by a department of the University of N. The project will evaluate cost and quality of at-home care provided to individuals with chronic lung diseases or chest cancer. Participants in the study will be residents of Q County, State of N. If the T Health system proves successful, the Project will, in a second phase, be extended to all ten counties. A mobile dental, mammography, and bone density unit may be added.

M requests approval to set aside a maximum of slightly over $25.7 x, comprised of the amounts set forth above for the taxable years ending August 31, 1999, and August 31, 2000. The set-aside will be used to fund the first phase of the Project. If the request is approved, the set-aside amounts will be set aside on the last day of each taxable year. If, at the end of the first phase, the Project is successful and is extended to all ten counties, M may apply for a set-aside at that time to fund the expansion of the Project.

M plans to fund the Project by direct payment of expenses as they are incurred. These expenses will be incurred throughout the planning and two-year evaluation phase. However, you are not certain that these expenses will be incurred prior to the end of the 1999 and 2000 taxable years. Hence, the need to set aside funds so that they are available as the Project incurs expenses.

The Project requires extensive coordination and long-term planning. A planning stage is necessary to enroll patients, hire staff, develop protocol, and perfect and install technology. The Project will involve a number of organizations, including the medical center at the University of N, R, which is involved with epidemiological research, S, a well known clinic, the Q County Health Council, and home health agencies, among others. Project participants, including patients, medical and research personnel and the various organizations, require assurance that funding will be available to complete the Project.

Epidemiological procedures are now being developed by R, which is affiliated with a consortium of regional universities. Wireless physiologic technology will have to be installed in each patient's home. This technology is being developed at S and is represented to be a sensitive, non-invasive technique for determining early changes in cardiac physiology and early signs of respiratory and cardiac failure. Video/phone lines will be set up between home sites and the medical center of University of N or other central site. Similar connections will be made for physician/patient consultations. Patients and at-home caregivers will need to communicate directly with a qualified nursing service, which will supervise home-care activity by video monitoring. Patients will be evaluated over at least a two year period to determine (1) the incidence of hospitalization, (2) the cost of medical care for in-and out-patient services, and (3) the incidence of active home health care, including oxygen therapy, antibiotics, lung toiletry therapy, and home service visits. Patient and physician satisfaction surveys will also be conducted.

You hypothesize that the use of home health care, telecommunication techniques, and wireless, physiologic monitoring through low cost video and phone lines will result in many health care benefits, including direct communication between rural, underserved areas and tertiary health care centers. You perceive additional advantages to include the lessening of rural physician and patient isolation, improved accessibility to specialist care, earlier determination of disturbed physiology, and prompt and more expeditious institution of medical intervention in patients with chronic disorders. Decreased hospitalization and more efficient use of low cost health providers supervised by physicians will be evaluated as to their ability to lower costs while sustaining quality medical services. Patients will be surveyed as to their satisfaction with the care they receive and the benefits of receiving at-home care.

The Project will evaluate residents of Q County, State of N, who (1) are homebound or severely restricted in activity because of chronic lung disease, or (2) have been diagnosed with chest cancer and require acute care.

In 1997, per capita income in Q County was approximately $12,000.00. Some 8.9% of the work force was unemployed. Over 50% of the residents rely on health insurance provided by the State of N as their primary source of health insurance. Q County has been made a federal primary care shortage site because of low income and State and federal dental shortages. In 1997, the incidence of chronic lung disease in Q County was approximately double that of the State of N as a whole.

Patients participating in the Project will be monitored for a minimum of two years. Assuming a total of 300 patients, the proposed budget for the first phase of the Project is approximately $25.8x. Approximately $4.2x will be allocated to personnel, including a project manager, data manager, epidemiologist, statistician, and investigators. Approximately $15.8x will be allocated to equipment. The equipment budget includes one telemedicine site per county, home health remote site equipment, and biosensors for each patient. The remainder of the budget is allocated to contractual services, e.g., home health nurses and rent.

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 (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 4942(c) defines the term "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.

Section 4942(d)(1) of the Code provides that the term "distributable amount" means, 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 a "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; or (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 which comes within one or more purposes described in section 170(c)(2)(B) may be treated as a qualifying distribution if it meets the requirements of subparagraph (B) of section 4942(g)(2).

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 that the amount will be paid for the specific project within five years, and the

project is one which can be better accomplished by such set-aside rather than by immediate payment of funds (the"suitability test").

Section 53.4942(a)-3(b)(1) of the Foundation and Similar Excise Taxes 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 if the requirements of that section and section 4942(g)(2) are satisfied. The foundation must establish that the amount set aside will be paid for the specific project within 60 months after it is set aside, and (1) the set-aside satisfies the suitability test, or (ii) the foundation satisfies the cash distribution test.

Section 53.4942(a)-3(b)(2) of the regulations provides that the suitability test is satisfied if the foundation establishes that the specific project is one 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. The regulation cites as an example of a suitable project 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 detail of the program have been finalized.

The proposed set-aside for the taxable years ending August 31, 1999, and August 31, 2000, is in furtherance of M's stated charitable purposes. As described above, the funds to be set aside will be used to promote the health care of residents of ten rural, medically underserved counties in the States of N , O, and P. Initially , the project will focus on Q County in N, which is very poor and whose incidence of chronic lung disease is approximately double that of N as a whole. Thus, the proposed set-aside will be used to accomplish a purpose described in Code section 170(c)(2)(B), as required by section 4942(g)(1). You have also established to our satisfaction that the project can be better accomplished by such set-aside rather than by immediate payment of funds. You have submitted a sworn statement from a trustee of M stating that the funds to be set aside on August 31,1999, and August 31, 2000, will actually be paid prior to the expiration of 60 months from the date of the set-aside.

Based on the foregoing, we rule that the set-aside of approximately $13.5x for the taxable year ending August 31, 1998, payable in the taxable year ending August 31, 1999, and the lesser of approximately $12.2x or M's minimum distributable amount for the taxable year ending August 31, 1999, payable in the taxable year ending August 31, 2000, satisifies the requirements of section 4942(g)(2)(B)(i) of the Code and section 53.4942(a)-3(b)(2) of the regulations (the "suitability test"). Accordingly, the set-asides in question can be treated as qualifying distributions for M's taxable years ending August 31,1999, and August 31, 2000.

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. Further, any amount which is set aside shall be taken into account for purposes of determining the foundation's minimum invest return (see section 53.4942(a)-2(c)(1)), and any income attributable to such set-aside shall be taken into account in computing adjusted net income (see section 53.4942(a)-2(d)).

This ruling is based on the understanding that there will be no material changes in the facts upon which it is based. Any changes that may have a bearing upon your tax status should be reported to your key District Director.

We are sending a copy of this ruling to your Key District Director for exempt organization matters. Because this letter could help resolve any questions about your tax status, you should keep it with your permanent records.

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.

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.

Thank you for your cooperation.

Sincerely,

Gerald V. Sack

Gerald V. Sack
Chief, Exempt Organizations
Technical Branch 4

281