



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, P.N. 20224

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4942.03-07

Date: 01/04/05

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

LEGEND:

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

Dear _____ :

This is in response to a letter dated December 30, 2003, which requests a ruling for a contingent set-aside under section 53.4942(a)-3(b)(9) of the Foundation and Similar Excise Taxes Regulations.

Our records show that B 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. Thus, we ruled that B could make a contingent set-aside for the tax year ending _____. B submitted information showing that pending litigation is still applicable. Accordingly, B requests a ruling for a contingent set-aside under section 53.4942(a)-3(b)(9) of the Foundation and Similar Excise Taxes Regulations for its tax year ending December 31, 2003.

B was created on _____, and received a letter from the Internal Revenue Service dated _____, 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 _____, 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 _____, several of C's relatives filed an equity complaint with E. The claimants challenged (i) the validity of Wills executed by C in _____ and _____, 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 _____ hearing, a preliminary injunction was issued to the same effect. In late _____, 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 assets, including principal and income. B appealed the preliminary injunction. That appeal was denied.

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

Based on the assumption that B is entitled to retain all property that it has received pending the ongoing litigation, B's estimated distributable amount for income earned in 2002(as defined in section 4942(f) of the Code) that must be distributed by _____ 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, 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) of the succeeding 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. B states that the litigation continues to be unresolved.

Based on the foregoing, we rule that B can make a contingent set-aside for the tax year ending . The amount to be set-aside is equal to the entire portion of B's 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.

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 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 must be taken into account in determining the private 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) of the regulations.

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

This ruling letter is directed only to M. 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,

Joseph Chasin
Manager, Exempt Organizations
Technical Group 2