

Internal Revenue Service  
Director, Exempt Organizations

Department of the Treasury  
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4942.03.07

LEGEND

B= a state  
C= a city  
s= a dollar figure  
t= a dollar figure  
u= a number of acres  
v= a number of acres  
w= a dollar figure  
x= a number of acres  
y= a dollar figure

Dear :

By letter dated March 28, 2008, you requested a ruling that set-asides in the amounts of \$s and \$t meet the requirements of Section 4942(g)(2)(B)(i) and accordingly constitute qualifying distributions under section 4942(g) for the taxable years ending March 31, 20 and March 31, 20 , respectively.

FACTS

You are an irrevocable trust established under the laws of the State of B, exempt from federal income tax under section 501(c)(3) of the Code and classified as a private foundation under section 509(a) and as a private operating foundation described in section 4942(j)(3). You were formed to develop, construct and maintain a park for the benefit and enjoyment of the general public.

You were funded with an undivided one-half interest in approximately u acres of real property in C. You have entered into an agreement to sell approximately v acres to an unrelated developer for \$w. With the proceeds of the sale, you will buy out the owner of the other one-half interest of the remaining x acres for \$y. On the x acre parcel you will construct accommodations, facilities and amenities appropriate to a well appointed

public park, including lawns, paths, restrooms, playgrounds, picnic areas, and athletic fields. In addition, to the extent funds are available, the park may also include facilities such as a senior citizens' center, family recreational center, meditation garden and public library. The design phase began before the end of the first fiscal year, but construction is anticipated to begin in the latter part of the second fiscal year. Significant construction expenditures are not expected until calendar year 20 . Construction will be completed no later than March 31, 20 .

Upon completion of the public park, you will actively operate and maintain it until such time as it may be transferred to a governmental entity (probably the City of C or to another section 501(c)(3) charitable organization.

#### **LAW**

Section 509(a) of the Code describes organizations exempt from federal income tax under section 501(c)(3) of the Code that are private operating foundations subject to the private operating foundation provisions of IRC 4942(j)(3).

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 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 within one or more purposes of section 170(c)(2)(B) may be treated as a qualifying distribution if the amount meets the requirements of section 4942(g)(2)(B).

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 the amount set aside will be paid for the specific project within five years, and the specific project is one that can better be accomplished by the set-aside of income rather than by the immediate payment of funds (the "suitability test").

Section 4942(j)(3) of the Code requires that private operating foundations must spend at least 85% of its adjusted net income or its minimum investment return, whichever is less, directly for the active conduct of

its exempt activities (the income test) in order to remain a private operating foundation.

Section 53.4942(a)-3(a)(2)(iii) defines as a qualifying distribution any amount set aside within the meaning of paragraph (b) of section 3.

Section 53.4942(a)-3(b)(1) of the Foundation and Similar Excise Tax Regulations provides that the amounts of income set aside for a specific project for one or more of the purposes in section 170(c)(1) or 170(c)(2)(B) of the Code may be treated as qualifying distributions for the tax year(s) in which such amounts are set aside (but not in the tax year in which actually paid) if the requirements of section 4942(g)(2) and paragraph (b) are satisfied. The requirements of paragraph (b) are satisfied if the foundation establishes to the satisfaction of the Commissioner the amount set aside will be paid for the specific project within 60 months after it is set aside, and (i) the set-aside otherwise meets the suitability test of section 53.4942(a)-3(b)(2) or (ii) the foundation satisfies the cash distribution test.

Section 53.4942(a)-3(b)(2) of the regulations provides that the suitability test for a set-aside is met if the foundation establishes 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 erect a building to house a direct charitable, educational, or similar exempt activity of the foundation.

Section 53.4942(a)-3(b)(7)(i) provides that a private foundation must obtain Internal Revenue Service approval of its set-aside of income under the suitability test by applying before the end of the tax year in which the amount is set aside.

In Revenue Ruling 74-450, 1974-2 CB 388, an operating foundation's conversion of a portion of newly acquired land into an extension of an existing wildlife sanctuary and the remainder into a public park under a four year construction contract, under which payments were made mainly during the last two years, was held to constitute a specific project.

#### **ANALYSIS**

You have sought timely approval of your set-asides of income in accordance with Section 53.4942(a)-3(b)(7)(i).

As required by Section 4942(g)(2)(A) of the Code and Section 53.4942(a)-3(b)(1) of the Regulations, your proposed set-asides will be used to accomplish purposes described in section 170(c)(2)(B) of the Code, namely,

for the construction and operation of a public park (See, *Isabel Peters*, 21 T.C. 55 (1953), acq. 1950-2 C.B. 6).

You have credibly represented that the amounts set-aside for this specific project will be paid out within 60 months from the set-aside, as required by section 4942(g)(2)(B)(i) of the Code and section 53.4942(a)-3(b)(1) of the regulations.

Your project is one that can better be accomplished by the set-aside of income rather than by the immediate payment of funds. Many permits and approvals must be obtained prior to the construction of the public park. Moreover, as is customary and appropriate in the construction industry, payments will be made on an "as work is done" basis. The project is similar to the example from the Regulations cited above and to the project described in Revenue Ruling 74-450. Your project therefore satisfies the suitability test as set forth in Section 4942(g)(2)(B)(i) of the Code and Section 53.4942(a)-3(b)(2) of the Regulations.

#### **RULING**

Based on the foregoing, The set-asides of \$s and \$t for the taxable years ending March 31, 20 and March 31, 20 , respectively, meet the requirements of Section 4942(g)(2)(B)(i) and accordingly constitute qualifying distributions under section 4942(g).

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 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.

This ruling letter is directed only to the organizations that requested them. Section 6110(k)(3) of the Code provides that they may not be used or cited as precedent.

Please keep a copy of this ruling letter in your permanent records.

A copy of this letter has been sent to your authorized representative.

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,

Robert Choi  
Director, Exempt Organizations  
Rulings and Agreements