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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Number: **200621028**
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Date: 3/1/2006

Contact Person:

Identification Number:

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Employer Identification Number:

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By letter dated February 16, 2005, A ("Foundation") requests a ruling regarding approval of a proposed set-aside grant to be made to B (the "University Foundation") under the suitability test of Section 4942(g)(2) of the Internal Revenue Code of 1986, as amended . The University Foundation is a nonprofit corporation formed to support the C, a public university (the "University"). The University Foundation is tax-exempt pursuant to Section 501(c)(3) of the Code. The Foundation requests that the set-aside apply to the Foundation's fiscal year ended June 30, .

The Foundation proposes to set aside x (the "Grant") for the purpose of providing funding for a new E building for the University's D (the "Project"). The Project will provide a state-of-the-art facility for the D. The Project will provide facilities for all aspects of the college of E's programs. The Foundation plans to pay the Grant in five equal installments commencing June 1, , with a final payment scheduled for June 1, . If the Project is completed prior to June 1, , the Foundation will accelerate payment of the remaining installments to the completion date.

The Foundation does not anticipate that there will be any additions to the set-aside after its initial establishment.

The University has finalized the design and budget estimates for the Project and has concluded that it will cost approximately x. It is anticipated that approximately x of this amount will be provided from the State of F. The University expects to begin the design and planning phase by early 2006 and commence construction in 2007. The use of a set-aside is necessary to provide the University with a funding commitment, while permitting the Foundation to retain control over the distribution of its funds to ensure that (i) construction progresses as planned, (ii) funding is received from other sources, and (iii) contributions from the Foundation are used solely for the purpose of construction of the Project.

As provided in the proposed Grant Agreement , funding will be conditioned upon completion of progress reports by the University Foundation containing information regarding the progress of development and construction of the Project. The University Foundation must provide the Foundation with a progress report every six months until the University Foundation spends all grant funds. Although the Grant Agreement contains anticipated dates for the payment of the Grant, payment is contingent upon the University securing state funding, completion of the Project and the use of grant funds for the Project.

A set-aside is essential to ensure that the Foundation's committed support for the construction of the Project is used for that purpose. This is of particular importance for the Project because one-half of the funding required must be provided by the State of F and the availability of this amount is potentially subject to budgeting constraints. In the event the University is unable to go forward with construction, the Foundation does not want the funds it contributes to be spent for the general operating budget of the University Foundation or the University. The Foundation believes that a set-aside is the best mechanism to provide a funding commitment while ensuring the proper use of the Foundation's contributions.

The Project involves the construction of a new state-of-the-art building located on the University's campus to house the E. Its current facilities are outdated and of insufficient scope and size to fulfill current needs of students and faculty. In addition to classrooms and faculty and administrative offices, the new building will house a computer G writing and editing lab, library and reference room, and a career and student advice center. The University estimates that the Project will cost x. The University is seeking to raise x of the projected cost through private donations. The University has received commitments from other donors for x and grant applications are pending for the balance of the funds necessary to complete the Project.

Because construction of the Project has not yet commenced, the directors of the Foundation thought it would be prudent to commit to payments over a longer period of time than currently estimated for construction in case there are delays. It is anticipated that construction will commence in 2007. As indicated above, payment of the grant would be accelerated if amounts remain unpaid upon completion of construction. The x that will be set aside for purposes of the Project will actually be paid within the five-year payment period specified in the Grant Agreement. This payment period will end no later than 60 months after the date of the first set aside.

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) 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) and this paragraph are satisfied. The requirements of this paragraph (b) are satisfied if the private 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 is set-aside, and (i) 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, for example, a plan to erect a building to house a direct charitable, educational, or similar exempt activity of the foundation.

Section 53.4942(b)-1(b) of the regulations provides, in part, that any amount set-aside by a foundation for a specific project, such as the acquisition, restoration, or construction of additional buildings or facilities which are to be used by the foundation directly for the active conduct of the foundation's exempt facilities, shall be deemed to be a qualifying distribution expended directly for the active conduct of the foundation's exempt facilities if such amount has initially been shown to meet the set-aside requirements in section 53.4942(a)-3(b) of the regulations.

You have stated that your proposed set-aside will accomplish a purpose described in section 170 of the Code, specifically, providing funds for the construction of a new academic building on the campus of a state university. The subjects to be taught in such building are closely related to your tax-exempt purposes. The facility will be completed by approximately June 1, . which is within the 60 months from the date of the set-aside. The set-aside should satisfy the suitability test because the expenditures are to be used for the design and construction of the building, and could not be made in the taxable year ending June 30, as required under section 53.4942(a)-3(b)(2) of the regulations. Further, you have established to our satisfaction that the project is long-term in nature and is better accomplished by future expenditures than by current ones.

Based on the foregoing, we rule that the set-aside of x specifically devoted to the construction of the above described facility, meets the requirements of section 4942(g)(B)(i) of the Code and section 53.4942(a)-3(b)(2) of the regulations. Accordingly, the set-aside can be treated as a qualifying distribution expended directly for the active conduct of exempt activities for your taxable year ending June 30, .

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. 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).

Please keep a copy of this ruling in your organization's permanent records.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, Notice of Intention to Disclose. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

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,

Andrew F. Megosh, Jr.
Acting Manager
Exempt Organization Technical Group 2

Enclosure: Notice 437