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

200216037

JAN 23 2002

Date:

Contact Person:

S.I.N. 0501.03-00, 0501.03-26, 0513.00-00

Telephone Number:

T:EO:B4

Legend
M =
S =
T =
U =
V =
Agreement =
Date 1 =
Date 2 =

Employer Identification Number:

Dear Sir or Madam:

We have considered M's ruling request dated September 28, 2001, submitted by its authorized representative. Based on the information submitted, we have decided to rule favorably on the rulings requested.

FACTS

M is an unincorporated membership organization consisting of S (the "Members"). M was formed on Date 1, with seven original members entering into the Agreement, pursuant to which the Members control M's operations. M performs accounting and administrative functions for the Members, and performs other functions that would otherwise be performed by the Members. By performing the functions needed to operate some of the Members' T activities, M helps the Members fulfill their statutory responsibilities. Participation in the Agreement is explicitly authorized by the statutes creating some of the Members.

By letter dated Date 2, the Service recognized M as exempt from federal income taxation under section 501(a) of the Internal Revenue Code, as an organization described in Code section 501(c)(3). This letter further classified M as a non-private foundation, as a supporting organization described in section 509(a)(3).

Some of M's Members have expressed an interest in offering a new U as a means to generate additional revenues for designated governmental activities funded by the proceeds of the Members' T activities. Participating Members and T organizations located outside V ("non-V T") would sell these new products within their own jurisdictions or in other places where it was

209

legally permissible to do so. M will be retained to perform functions with respect to these new U, similar to those that M performs for existing T. M will be paid a fee for its services. The non-V T organizations will not become M's members, and will thus not control M or play any role in its governance; M's governance structure will be unchanged after it begins offering this new U.

LAW AND ANALYSIS

Section 501(c)(3) of the Internal Revenue Code describes organizations, exempt under section 501(a), that are organized and operated exclusively for charitable and certain other purposes.

Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations further delineates purposes considered "charitable" within the meaning of Code section 501(c)(3), stating that the term "charitable" is used in its generally accepted legal sense, and includes "lessening of the burdens of Government".

The criteria the Service uses to determine if an organization's activities further the charitable purpose of lessening the burdens of government are contained in Rev. Rul. 85-1, 1985-1 C.B. 141, and Rev. Rul. 85-2, 1985-1 C.B. 141. The criteria are, first, that a governmental unit considers the organization's activities to be its burden and second, that the activities actually lessen the burden.

Rev. Rul. 85-1 further states:

> An activity is a burden of government if there is an objective manifestation by the governmental unit that it considers the organization's activities to be its burden. The interrelationship between the governmental unit and the organization may provide evidence that the governmental unit considers the activity to be its burden. Whether the organization is actually lessening the burdens of government is determined by considering all of the relevant facts and circumstances.

Rev. Rul. 87-126, 1987-2 C.B. 150, holds that an organization that provides government-funded retirement benefits for volunteer firefighters qualifies for exemption as a social welfare organization under section 501(c)(4) of the Code. The organization provides a benefit of a type and in an amount that the local government deems to be in the public interest and recognizes as a legitimate function of government, as evidenced by the state government's willingness to fund the association and by the establishment of a civil service retirement program to provide comparable benefits. Thus, it lessens the burdens of government, a charitable purpose under section 1.501(c)(3)-1(d)(2) of the regulations, and a social welfare purpose under section 1.501(c)(4)-2(i) . *See also* Rev. Rul. 74-361, 1974-2 C.B. 159, which holds that a nonprofit volunteer fire company qualifies for exemption under section 501(c)(3) because providing fire and rescue services for a community lessens the burdens of government; and Rev. Rul. 71-99, 1971-1 C.B. 151, which holds that an organization that provides food and drink to emergency personnel at the scene of major disasters lessened the burdens of government by helping the workers conduct governmental functions.

Rev. Rul. 81-276, 1981-2 C.B. 128, holds that a professional standards review organization designated by the Department of Health and Human Services to review professional activities of health care providers performed for patients under the Medicare and Medicaid programs qualifies for exemption under section 501(c)(3) as an organization that lessens the burdens of government. The organization performs part of the government's statutory responsibilities under the statutes creating these programs. *See also* Rev. Rul. 85-2, *supra* (legal requirement that the government provide services of the type provided by the organization demonstrates existence of governmental burden).

Rev. Rul. 76-418, 1976-2 C.B. 145, holds that an organization lessens the burden of government where it performs services for the government – traffic control and safety - that are the government's recognized responsibility. In the ruling, the relationship between the organization and the government help indicate that the organization's activities are part of the government's burden, in that governments asked the organization to perform certain services and it performs those services free of charge, deriving its operating income from public contributions.

In Rev. Rul. 78-68, 1968-1 C.B. 149, an organization qualifies for exemption as a charitable organization under section 501(c)(3) where it operates a governmental program under the authority of the federal and state governments. In contrast, in Rev. Rul. 74-117, 1974-1 C.B. 128, an organization that conducts activities associated with the inauguration of a new state governor does not further charitable purposes where the state had never provided similar services, and thus had not recognized the activities as a governmental function.

Rev. Rul. 74-246, 1974-1 C.B. 130, holds that an organization that provides funds with which a police department could provide rewards for information leading to the apprehension of persons engaged in criminal activities lessens the burdens of government because it gratuitously performs services for government.

Rev. Rul. 71-29, 1971-1 C.B. 150, holds that a section 501(c)(3) organization's expenditure to provide funds to a city transit authority to ensure that city bus service is continued furthers the charitable purpose of lessening the burdens of government.

Thus, the Service has considered a variety of factors in deciding whether an activity is a governmental burden, including the following:

1. The organization's interrelationship with governmental unit(s), or with governmental officials acting in their official capacity
2. Whether the organization conducts activities previously conducted by governmental unit(s)
3. The organization's payment of governmental expenses
4. The sources of the organization's funding
5. Whether the activities could be performed directly by governmental units
6. Whether a statute requires of the type performed by the organization

Section 511 of the Code imposes a tax on the unrelated business taxable income, as defined in section 512, of organizations exempt from tax under section 501(a).

Section 512(a) of the Code defines unrelated business taxable income as the gross income derived from any unrelated trade or business, as defined in section 513) regularly carried on, with certain deductions and modifications.

Section 513(a) of the Code defines unrelated trade or business as a trade or business the conduct of which is not substantially related to the organization's exercise or performance of the purpose or function forming the basis for its exemption under section 501(a).

Section 1.513-1(d)(2) of the regulations provides that trade or business is "related" to exempt purposes only where the conduct of the business activities has a causal relationship to achieving exempt purposes; and it is "substantially related" only if the causal relationship is a substantial one. The regulation states that for the conduct of trade or business from which a particular item of gross income is derived to be substantially related to exempt purposes, producing or distributing the goods or services from which the income is derived must contribute importantly to accomplishing those purposes.

Section 509(a) of the Code provides that a section 501(c)(3) organization is a private foundation unless it is described in section 509(a)(1), (2), (3), or (4).

Section 509(a)(1) of the Code provides that organizations described in section 170(b)(1)(a)(i) - (vi) are not private foundations.

Section 170(b)(1)(A)(v) of the Code describes governmental units, which are not private foundations under section 509(a)(1).

Section 509(a)(3) of the Code provides that an organization is not a private foundation if it meets three requirements:

(1) It is organized and operated exclusively for the benefit of, to perform the functions of, or to carry out the purposes of organizations described in section 509(a)(1) or (2);

(2) It is operated, supervised, or controlled by or in connection with organizations described in section 509(a)(1) or (20; and

(3) It is not controlled, directly or indirectly, by disqualified persons (as defined in section 4946) other than foundation managers and section 509(a)(1) or (2) organizations.

Section 1.509(a)-4(e)(1) of the regulations provides that a supporting organization will be regarded as operated exclusively to support publicly supported organizations only if it engages solely in activities that support or benefit the supported organizations. Under section 1.509(a)-4(e)(2) of the regulations, a supporting organization may satisfy the operational test by carrying on an independent activity or program that supports or benefits the supported organizations. A supporting organization may also engage in fund raising activities to raise funds for permissible beneficiaries.

Here, M's activities are a burden of government, as evidenced by the following facts and

circumstances:

1. M was created by official action of its governmental Members, some of whom are statutorily authorized to participate in M; its activities are controlled by its Members, with whom it has a close working relationship.
2. The functions M provides its Members are necessary to their performance of their governmental responsibilities.
3. M conducts activities its Members would otherwise conduct, and pays expenses the Members would otherwise pay.

The new U to be conducted by M's Members, with M's administrative support, does not differ in substance from the existing V-based T. M's administrative support will assist the Members in carrying out their statutorily authorized functions, by performing functions necessary for the Members to perform their governmental responsibilities, conducting activities the Members would otherwise conduct, and paying expenses the Members would otherwise pay. As such, the new U and M's administrative support promote section 501(c)(3) purposes and are substantially related for purposes of the section 511 through 513 unrelated business income tax provisions.

For similar reasons, the new U will not adversely affect M's status as a supporting organization under section 509(a)(3). Because conducting the T will help the Members perform their governmental responsibilities and all of the profits will be distributed to the Members pursuant to the Agreement, the activity supports and benefits the Members.

Accordingly, based on the facts and information submitted and representations made, we rule as follows:

1. M's provision of accounting and administrative services to its Members participating in the U and receipt of fees for such services from participating Members will not adversely affect M's status as an organization exempt under section 501(c)(3) of the Code.

2. M's provision of accounting and administrative services to non-V T organizations participating along with Members in the U and receipt of fees for such services from the non-V T organizations will not adversely affect M's status as an organization exempt under section 501(c)(3) of the Code.

3. M's receipt of fees for providing accounting, administrative, and other services to non-V T organizations participating along with Members in the non-V T will not be classified as income from an unrelated trade or business under section 513 of the Code.

4. M's provision of accounting and administrative services to non-V T organizations, and receipt of fees for such services, will not adversely affect M's status as a supporting organization under section 509(a)(3) of the Code.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Internal Revenue Code provides that it may not be used or cited by others 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,

(signed) Gerald V. Sack

Gerald V. Sack
Manager, Exempt Organizations
Technical Group 4

214