

Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply to:
CC:TE/GE:EO2 - PLR-165808-02
Date:
March 5, 2003

LEGEND

Corporation =

State A =

Dear :

This is in reply to a letter dated November 18, 2002, requesting a ruling that the income of Corporation is excludable from gross income under § 115(1) of the Internal Revenue Code.

FACTS

Corporation is organized under the not-for-profit corporation law of State A. Its purpose is to improve the operations of the utility businesses to be owned or operated by its members. Corporation will operate electricity generating facilities and provide planning and purchasing services in connection with members' electricity generating functions. Any member may elect to participate in some of Corporation's projects and not participate in others.

The taxpayer represents that each of the current members is a political subdivision of a state for federal income tax purposes. All future members must be either political subdivisions of a state or entities the income of which is excludable as gross income under § 115(1). If a member ceases to be a political subdivision of a state or an entity the income of which is excludable as gross income under § 115(1), it

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shall cease to be a member of Corporation. Currently, Corporation has four members. Corporation is governed by a board of directors. Each member appoints one director and has the power to remove, with or without cause, the director it appoints. A director must be an officer or employee of the appointing member.

Each new member will be assessed an appropriate capital contribution. Each member will also make annual contributions to Corporation based on Corporation's operating budget, as determined by its board. Corporation is required to submit to each member an accrual basis balance sheet together with an accrual basis profit and loss statement monthly. Within 120 days after the end of its fiscal year, Corporation is required to have its independent certified public accountant provide each member full, detailed, certified financial statements showing the assets, liabilities, properties, net worth, net revenues, net expenses and net income for the fiscal year.

Corporation's articles of incorporation provide that no part of its net earnings will inure to the benefit of any private person. If a member voluntarily withdraws, Corporation is required to return the amount contributed by the departing member plus such departing member's share of margins and other revenue recognized, less its fair share of liabilities and expenses, and less all amount previously distributed to it. In the event Corporation dissolves, any assets remaining after Corporation satisfies its obligations will be distributed to its members.

LAW AND ANALYSIS

Section 115(1) provides that gross income does not include income derived from any public utility or the exercise of any essential government function and accruing to a state or any political subdivision thereof.

In Rev. Rul. 77-261, 1977-2 C.B. 45, income from an investment fund, established under a written declaration of trust by a state, for the temporary investment of cash balances of the state and its participating political subdivisions, is excludable from gross income for federal income tax purposes under § 115(1). The ruling indicates that the statutory exclusion was intended to extend not to the income of a state or municipality resulting from its own participation in activities, but rather to the income of a corporation or other entity engaged in the operation of a public utilities or the performance of some governmental function that accrued to either a state or municipality. The ruling points out that it may be assumed that Congress did not desire in any way to restrict a state's participation in enterprises that might be useful in carrying out projects that are desirable from the standpoint of a state government and which are within the ambit of a sovereign to properly conduct.

In Rev. Rul. 90-74, 1990-2 C.B. 34, the Service determined that the income of an organization formed, funded, and operated by political subdivisions to pool various risks (casualty, public liability, workers' compensation, and employees' health) is excludable from gross income under § 115(1). In Rev. Rul. 90-74, private interests neither materially participate in the organization nor benefit more than incidentally from the organization.

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By facilitating the cost effective production and transmission of electrical power, a basic utility, by public utilities, Corporation performs an essential governmental function.

The net income of Corporation accrues to solely to entities that are political subdivisions of a state or to entities the income of which is excludable from gross income under § 115(1). Other than incidentally, as compensation for goods and service, no part of Corporation's income will be distributed to any party other than a political subdivision of a state or an organization the income of which is excluded from gross income under § 115(1). Upon the dissolution of Corporation, its assets shall be distributed to its members.

The income of Corporation is derived from an essential governmental function and accrues to a political subdivision of a state or to an entity the income of which is excludable from gross income under § 115(1). Accordingly, the income of Corporation is excludable from gross income for federal income tax purposes under § 115(1).

CONCLUSIONS

Corporation's income is excludable from gross income under § 115(1).

Except as specifically provided otherwise, no opinion is expressed on the federal tax consequences of any particular transaction.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that this ruling may not be used or cited as precedent.

In accordance with a Power of Attorney on file, we are sending a copy of this letter to your representatives.

Sincerely,

Elizabeth Purcell, Chief
Exempt Organizations
Branch 2
Division Counsel/Associate
Chief Counsel
(Tax Exempt and Government
Entities)

Enclosures;