

**Internal Revenue Service**

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Department of the Treasury

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Person To Contact:

, ID No.

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Refer Reply To:

CC:TEGE:EOEG:EO

PLR-138309-12

Date:

December 11, 2012

Entity:

Company:

State:

Jurisdiction:

Agreement:

Date:

Dear :

This letter responds to a letter from your authorized representative signed August 31, 2012, submitted on behalf of Entity and Company (the Taxpayers), requesting rulings that Company's income will be excluded from gross income under § 115 of the Internal Revenue Code. The Taxpayers represent the facts as follows.

**FACTS**

Entity was created and is operated under State law as an agency of State. Its purpose is to provide professional investment management of various trusts and operating funds established under the laws of State. Entity has broad authority to invest and reinvest, to collect income and rents, to acquire, manage, and sell real estate, and to employ outside counsel and contractors.

Entity formed Company on Date as a limited liability company under the laws of Jurisdiction. Entity is the sole member of Company. The Agreement provides that no person other than a state, a political subdivision of a state, or an entity whose income is excluded from gross income under § 115 may be admitted as a member of Company.

Entity is the initial manager of Company, with full and exclusive authority to handle Company's business affairs, in accordance with the Agreement. The manager may delegate any of its authority to another person, as long as the manager retains the power to direct and control the delegate. Entity may select any legal entity to serve as a successor manager under an advisory agreement to be reached between the successor and Company. Entity may remove a successor manager at any time, with or without cause.

Company's purpose, as stated in the Agreement, is to acquire, hold, and sell investments, and to engage in any lawful activity. Entity intends for Company to serve as an acquisition vehicle for its real estate investments. Company will enter into a loan facility with a third-party lender, allowing it to draw on funds to acquire real estate investments. Company will hold each investment in a separate, wholly-owned subsidiary, and will pledge its interests in these subsidiaries as security for the loan facility. The manager or an agent engaged by the manager will negotiate the loan facility and will identify, negotiate, and purchase real estate investments.

As the sole member of Company, Entity will be allocated all Company profits and losses and will receive all distributions from Company. Upon Company dissolution, and after the satisfaction of its legal obligations, all of Company's remaining assets will be distributed to Entity. Entity will bear all risk of loss from Company, limited to the amount of its capital contributions.

#### 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, was excludable from gross income for federal income tax purposes under § 115(1). The ruling indicated 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 utility 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 properly to conduct. In addition, pursuant to § 6012(a)(2) and the underlying regulations, the investment fund, being classified as a corporation that is subject to taxation under subtitle A of the Code, was required to file a federal income tax return each year.

In Rev. Rul. 90-74, 1990-2 C.B. 34, the income of an organization formed, funded, and operated by political subdivisions to pool various risks arising from their obligations regarding public liability, workers' compensation, or employees' health is excludable from gross income under § 115. In this ruling, private interests did not materially participate in the organization, nor did they benefit more than incidentally from the organization.

Company enables Entity to invest a portion of the trusts, operating funds, capital funds, and property of State and to engage in certain investment strategies, while limiting Entity's exposure to the risks of such investments. Providing such means for investing public assets and for limiting investment risk constitutes the performance of essential governmental functions. See Rev. Rul. 90-74 and Rev. Rul. 77-261.

All of Company's income accrues to Entity, an agency of State. Entity is allocated all Company profits and losses and receives all Company distributions. No private interests participate in, or benefit from, the operation of Company other than as providers of goods or services. The benefit to third-party lenders or to buyers and sellers in the real estate market is incidental to the public benefit. Upon Company's dissolution, no assets remaining after winding up will be distributed to any entity other than a state, a subdivision of a state, or an entity the income of which is excluded from gross income under § 115. See Rev. Rul. 90-74.

#### RULING

Based solely on the facts and representations submitted by the Taxpayers, we conclude that the income of Company is derived from the exercise of an essential governmental function and will accrue to a state or a political subdivision thereof for purposes of § 115(1). Consequently, we rule that Company's income is excludable from gross income under § 115(1).

Except for the specific ruling above, we express or imply no opinion concerning the federal tax consequences of the facts of this case under any other provision of the Code.

Under a power of attorney on file with this office, we are sending copies of this letter to your authorized representatives.

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

Sincerely,

SYLVIA HUNT  
Assistant Chief  
Exempt Organizations Branch  
Office of Division Counsel /  
Associate Chief Counsel  
(Tax Exempt & Government Entities)

enclosures: copy for § 6110 purposes