

Internal Revenue Service

Department of the Treasury
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Date:
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LEGEND

Authority
State A

Dear

This is in reply to a letter dated May 8, 2000, requesting a ruling that the income of Authority is excludable from gross income under § 115 of the Internal Revenue Code.

FACTS

Authority is a nonprofit corporation organized under the provisions of the not-for-profit corporation law of State A. Authority was created to coordinate the operation of resources and the purchase and sale of on behalf of its members. The members of Authority each own and maintain facilities for the purpose of providing to consumers in its service area. The taxpayer represents that all current members are political subdivisions of states. All future members must be either political subdivisions or entities the income of which is excludable as gross income under § 115(1) of the Internal Revenue Code.

Authority is governed by a board of directors. Members are divided into Class A members and Class B members on the basis of size, as measured by the member's and capacity. Each Class A member

appoints three directors and each Class B member appoints one director. Each director is required to be an officer or employee of the member by which the director was appointed. Each member has the power to remove, with or without cause, any of the directors that it appoints.

Authority was formed to coordinate the operation of resources and the purchase and sale of on behalf of its members. In order to

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insure that an additional supply of _____ is available for its members in case of an unexpected event, and to promote cost effective participation by the members in the _____, Authority buys and sells _____ or _____ from other members or from third parties and enters into contractual relationships to buy or sell _____. Authority performs activities for its members on a consolidated basis which the members have historically performed for themselves. In order to provide financial support to Authority, each member is required to make a substantial capital commitment. In addition each member is required to provide a guarantee to Authority in the form of cash, trade guarantees and bank guarantees.

The net revenues of Authority are distributed monthly to the members less reasonable retention for working capital needs. Authority makes further distributions, typically quarterly but in no event less than annually, to the members to the extent that the retention amount is not required. The Articles of Incorporation provide that no income of Authority shall inure to the benefit of any director, officer or trustee of Authority or to any other private person. Upon the dissolution of Authority, any remaining assets will be distributed to the members in proportion to each member's capital account balance.

LAW AND ANALYSIS

Section 115(1) of the Code 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 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 of the Code. 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 ensuring the supply and efficient _____ of _____, a
, by _____, Authority performs an essential governmental function.

The net income of Authority accrues to its members (political subdivisions of a state or entities the income of which is excludable from gross income under § 115(1) of the Code) through monthly, quarterly, and/or annual payments. The income of Authority is used solely for purposes related to providing _____ to its members. No part of Authority's income will be distributed to any party other than a member of Authority. Upon the dissolution of Authority, its assets shall be distributed to its members.

Accordingly, the income of Authority 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).

CONCLUSION

The income of Authority is excludable from gross income for federal income tax purposes under § 115(1) of the Code.

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 representative.

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

Enclosures;
Copy of this letter
Copy for § 6110 purposes