



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

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

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U.I.L. Nos.  
501.03-00  
501.03-33

Employer Identification Number:

LEGEND:

M =

N =

X =

x =

y =

Dear \_\_\_\_\_ :

This is in response to a letter dated March 11, 2004, from your authorized representative requesting a series of rulings on your behalf regarding the tax consequences associated with the transactions described below. In a letter dated December 1, 2005, you amended your ruling request.

You were incorporated in the state of M. You have been recognized as an organization exempt from federal income taxation under sections 501(a) of the Internal Revenue Code and section 501(c)(3) of the Code.

You are a membership organization open to political subdivisions in the greater N metropolitan area. Most of your member jurisdictions are relatively small cities, townships and villages near N.

You operate under the direction of a fulltime, elected, volunteer Board of Trustees. You

were incorporated to promote cooperation and collaboration among local governments primarily in the greater N area by means of data collection, analysis and dissemination, education and consulting services. You seek to accomplish this mission through information exchange, cost reductions, shared resources, interjurisdictional collaboration, and the development of new approaches to finance capital acquisitions.

You offer your members a variety of collaborative programs and training, including information services; training and development; judgment use of force training for police officers at a firearms training simulator you own; mutual aid pacts for public works coordinated and maintained by you; and, a training program for disaster preparedness. You fund your programs through a combination of membership dues and fees charged to members participating in some of your collaborative projects.

Member jurisdictions are required to purchase or construct capital assets and improvements such as fire trucks, police cruisers, fire stations, police stations, other municipal vehicles and buildings, and road improvements. You state that because many of the jurisdictions are small, their borrowing needs are commensurate with their size. As a result, when acting alone, the jurisdictions are forced to engage in relatively expensive financing programs.

Your members requested that you look into the feasibility of offering, sponsoring, administering or coordinating a capital asset financing program. In response, you established a capital asset financing program ("Program") in the form of a loan pool which would allow your members to pool their anticipated borrowing needs. From the loan pool, participating jurisdictions issue "fractionalized interest" general obligations bonds which represent the amount of general obligation bonds that each would have otherwise issued. The liability of each participating jurisdiction is limited to the fractionalized interest. You state that by permitting the jurisdictions to pool their borrowing needs and issue bonds as a part of a larger pool, the participating jurisdictions realize substantial savings in the form of (1) credit enhancements on the larger borrowing; (2) lower interest rates; and, (3) lower administrative costs of issuance.

You further state that a bond issuance fully achieved the Program objectives of lowering interest rates and administrative costs for participants. To preserve the economies of scale and cost savings produced by the Program, you determined that each of the loan pools that you had scheduled for the following year would require a minimum issue of \$x million of bonds. After canceling the first of several planned loan pools because of insufficient demand, you realized that the size of your membership and their respective financial demands would prevent you from offering the loan pool as regularly as your members desired. You further determined that the participation of nonmember jurisdictions would increase the benefits received by your members as you would be able to offer loan pools several times a year, making the Program available to members when they need it. You state that larger bond pools should result in even lower interest rates and administrative savings for all participants, including your members. You explain that offering the program to both your members and non-members is a natural extension of your mission of assisting municipalities and townships to operate in the most efficient manner possible.

You anticipate that any future bond issues under the Program will be on substantially

similar terms and conditions as the \_\_\_\_\_ issue, for which you received a fee of \$y from the bond proceeds for administering, implementing and coordinating the initial bond issue under the Program. The fee to be received for future bond issues is undetermined at this point. However, you state that it would likely be proportionate on a percentage basis to the fee received in the issue and negotiated at arms-length with the underwriter.

You have requested the following rulings:

1. The proposed transactions described herein will not jeopardize the tax-exempt status of X as an organization described in section 501(c)(3) of the Code.
2. Fees received by X for administering, implementing and coordinating the future issuance of general obligation bonds by both member and non-member jurisdictions under guidelines that are substantially similar to those of the Program to finance the acquisition of capital assets: (i) will not constitute unrelated business taxable income within the meaning of section 512 of the Code; and (ii) will not be subject to the tax on unrelated business income imposed by section 511 of the Code.

Section 501(c)(3) of the Internal Revenue Code exempts from federal income tax organizations organized and operated exclusively for charitable, educational, and other purposes, provided that no part of the organization's net earnings inures to the benefit of any private shareholder or individual.

Section 511 of the Code imposes a tax on the unrelated business taxable income of organizations described in section 501(c)(3).

Section 512(a) of the Code defines unrelated taxable business income as the gross income derived from any unrelated trade or business regularly carried on by the organization.

Section 513(a) of the Code defines "unrelated trade or business" as any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under section 501.

Section 1.501(c)(3)-1(c)(1) of the Income Tax Regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(2) of the regulations defines "charitable" in its generally accepted legal sense and includes, among other things, the erection or maintenance of public buildings, monuments, or works, and the lessening of the burdens of government.

Section 1.513-1(d)(2) of the regulations provides that a trade or business is related to exempt purposes only where the conduct of the business activity has substantial causal relationship to the achievement of exempt purposes. Thus, for the conduct of a trade or business from which a particular amount of gross income is derived to be substantially related to the purposes for which exemption is granted, the production or distribution of the goods or performance of the services from which the gross income is derived must contribute importantly to the accomplishment of those purposes.

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. 70-583, 1970-2 C.B. 114, holds that an organization furthers the charitable purpose of lessening the burdens of government by operating a community correctional center that rehabilitates prisoners selected by the courts or governmental custodial agencies.

Rev. Rul. 74-361, 1974-2 C.B. 159, holds that a nonprofit organization that was organized and operated as a volunteer fire company to provide fire protection and ambulance and rescue services to a community qualifies for exemption as a charitable organization under section 501(c)(3) of the Code.

X was formed to promote cooperation and collaboration among local governments. Cost reductions, shared resources, interjurisdictional collaboration, and the development of new approaches to finance capital acquisitions are some of the ways in which X seeks to accomplish its exempt purposes. X's membership is comprised mostly of relatively small cities, townships and villages. One of the activities in which X has been engaged is the establishment of a Program under which its members can pool their resources in order to finance the acquisition of capital assets through the issuance of general obligation bonds. X has determined that by including nonmember political subdivisions in the Program, both the member and nonmember jurisdictions would benefit from economies of scale that would not otherwise be available to them, reducing the costs of financing projects for all the participants.

Through the Program, X would further the charitable purpose of lessening the burdens of government as set forth in Rev. Rul. 85-1 and Rev. Rul. 85-2. Furthermore, the fees received by X in connection with the issuance of the general obligation bonds, an activity that is

substantially related to X's exempt purpose, would not be subject to the tax imposed under section 511 of the Code.

Based on the information submitted and assuming your organization will operate as stated above, we rule as follows:

1. The proposed transactions described herein will not jeopardize the tax-exempt status of X as an organization described in section 501(c)(3) of the Code.
2. Fees received by X for administering, implementing and coordinating the future issuance of general obligation bonds by both member and non-member jurisdictions under guidelines that are substantially similar to those of the Program to finance the acquisition of capital assets: (i) will not constitute unrelated business taxable income within the meaning of section 512 of the Code; and (ii) will not be subject to the tax on unrelated business income imposed by section 511 of the Code.

This ruling applies the applicability of sections 511-513 to the facts represented above. We express no opinion as to the tax consequences of the transaction under any other provisions of the Code.

This ruling is directed only to X. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Because this letter could help resolve any future questions about tax consequences of your activities, you should keep a copy of this ruling in your permanent records.

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 Organizations  
Technical Group 2