



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Release Number: **200832031**
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Date: May 12, 2008

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

UIL: 9100.00-00

Legend:

M

Year X

Year Y

Dear

You asked for discretionary relief under section 301.9100-3 of the Procedure and Administration Regulations for an extension of time to revoke your section 501(h) lobbying expenditure test election, effective for all tax years beginning after December 31, Year X.

FACTS

You are exempt from federal income tax as an organization described in section 501(c)(3) of the Internal Revenue Code (Code) and classified as a public charity under section 509(a)(1). You made a section 501(h) lobbying expenditure test election (the "lobbying election") several decades ago and have not revoked it.

Several years ago, you entered into discussions with M, which is also exempt from federal income tax as an organization described in section 501(c)(3) of the Code and classified as a public charity under section 509(a)(1). These discussions initiated a strategic alliance between the two organizations. You and M agreed to pursue a relationship that would allow you to maintain your distinct legal existence while joining M's family of organizations. During the following months, the parties conducted due diligence on each other's operations and held negotiations focused primarily on the terms of the alliance and how best to integrate your programs, activities, personnel, and governance structure with those of M.

In Year X, you and M entered into an asset acquisition agreement. Under the terms of the agreement, you retained your separate legal identity with responsibility for carrying out and expanding your "signature programs" and M agreed to provide ongoing operational assistance to support your activities.

When the agreement became effective on January 1, Year Y, M assumed control of you. You have represented that as of that date you became a member of an affiliated group with M within

the meaning of section 4911(f)(2) of the Code.

On December 31, Year X, one day before the agreement became effective, and without notice to you, M filed a Form 5768 revoking its section 501(h) lobbying election, effective for all tax years beginning after that date. Although M carefully reviewed this decision in the context of its own tax-exempt status, the impact such a revocation might have on you was not discussed.

Under a long-standing policy, M conducts virtually all of the lobbying activities on behalf of the entire group of affiliated entities, while the affiliates generally focus on non-lobbying, program activities. Thus, neither organization expected you to conduct any lobbying activities following the acquisition. This expectation was borne out by your subsequent conduct, as you drastically reduced your lobbying expenditures to less than 1% of your exempt purpose expenditures. In fact, following the acquisition, the combined lobbying expenditures of M and all of its affiliated organizations, including you, declined.

Eighteen months later, an accounting firm, which had been engaged to prepare your Year Y Form 990, discovered the unintended consequence of your failure to timely revoke your section 501(h) election. Under section 4911(f)(2) of the Code, you became the sole electing member of the affiliated group, potentially liable for all of the excess lobbying expenditures of the group. The firm's calculation of the excise tax that could be imposed on you was more than 20 times your actual lobbying expenditure for the year and put you at risk of losing your tax-exempt status.

You immediately conducted an internal review of this matter and retained the accounting firm and outside legal counsel to assist in preparing a request for discretionary relief under section 301.9100 of the regulations. You included as part of your Form 990 for Year Y, a schedule A, Part VI-A, with a note that although you had not revoked your election for that year, you filed the Schedule A as though you had because you intended to seek discretionary relief. You then filed this request before the Internal Revenue Service (the "Service") initiated any examination or discovered this matter.

You had relied on a qualified attorney for legal advice on all aspects of the acquisition, including the impact of the acquisition on your tax-exempt status. Your attorney did not inform you that you would be subject to the affiliation rules of section 4911(f) of the Code as a result of this transaction, nor did he advise you to revoke your lobbying election to avoid the adverse consequences of that Code section. Had you done so by the effective date of the acquisition, you would not have incurred any tax liability under section 4911.

Granting your request will eliminate a tax liability that arose as a result of your inadvertent failure to revoke your lobbying election. It will not result in a lower tax liability than was applicable at the time you should have revoked your lobbying election.

Based on the above facts, you requested the following ruling:

An extension of time to retroactively revoke your lobbying election to be effective for all tax years beginning after December 31, Year X.

LAW

Section 501(c)(3) of the Internal Revenue Code exempts from federal income tax entities organized and operated exclusively for charitable, educational and other exempt purposes, provided, in relevant part, that "no substantial part of [the organization's] activities [may consist of] carrying on propaganda, or otherwise attempting to influence legislation (except as otherwise provided in subsection (h))."

Section 501(h) of the Code sets out an alternative to the "no substantial part" limitation on expenditures made for the purposes of influencing legislation. This section permits an organization to elect to be governed by mechanical rules that set ceilings on the permissible lobbying expenditures it may make during a taxable year.

Section 501(h)(3) of the Code delegates to the Secretary the responsibility for setting the specific time and manner in which the lobbying election should be made.

Section 501(h)(6)(A) of the Code provides that an organization's election under section 501(h) is effective for all taxable years which end after the date the election is made.

Section 501(h)(6)(B) of the Code provides that an organization's election under section 501(h) continues to be effective for all taxable years which begin before the date the election is revoked by the organization.

Section 1.501(h)-2(a) of the Income Tax Regulations provides that an election under section 501(h) is made by filing a completed "Form 5768, Election/Revocation of Election by an Eligible Section 501(c)(3) Organization to make Expenditures to Influence Legislation...." This section also provides that the election remains in effect for each succeeding taxable year for which the organization is an eligible organization and which begins before a notice of revocation is filed under paragraph (d) of section 1.501(h)-2 of the regulations.

Section 1.501(h)-2(d)(1) of the regulations provides that an organization may voluntarily revoke a lobbying election by filing a Form 5768.

Section 4911(f)(1)(A) of the Code provides that when two or more organizations are affiliated, and at least one has made an election under 501(c)(3)(h), the determination as to whether excess lobbying expenditures have been made and the expenditure limits of 501(h)(1) have been exceeded, shall be made as though the affiliated organizations are one organization.

Section 4911(f)(2) of the Code defines membership in an affiliated group, for the purposes of the preceding paragraph: when the governing instrument of one organization requires it to be bound by the decisions of another on legislative issues, or the governing board of one organization includes persons who are either specifically designated representatives or members of the governing board, officers, or paid executive staff of another organization; and who by aggregating their votes have sufficient power to cause or prevent action on legislative issues by the first organization.

Section 301.9100-1(c) of the Procedure and Administration Regulations gives the Commissioner discretion to grant a taxpayer a reasonable extension of time to make a

regulatory election.

Section 301.9100-1(b) of the regulations defines a regulatory election as an election the due date of which is prescribed by a regulation published in the Federal Register, revenue ruling, revenue procedure, notice, or announcement published in the Internal Revenue Bulletin.

Section 301.9100-3(a) of the regulations provides that requests for extensions of time to file regulatory elections when the taxpayer provides the evidence to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and the grant of relief will not prejudice the interests of the Government.

Section 301.9100-3(b)(1) of the regulations provides that a taxpayer will be deemed to have acted reasonably and in good faith if the taxpayer:

- i. Requests relief before the failure to make the regulatory election is discovered by the Service;
- ii. Failed to make the election because of intervening events beyond the taxpayer's control;
- iii. Failed to make the election because, after exercising reasonable diligence, the taxpayer was unaware of the necessity for the election;
- iv. Reasonably relied on the written advice of the Service; or
- v. Reasonably relied on a qualified tax professional who failed to make, or advise the taxpayer to make, the election.

Section 301.9100-3(b)(3) of the regulations provides that a taxpayer will not be considered to have acted reasonably and in good faith if the taxpayer:

- i. Seeks to alter a return position for which an accuracy related penalty could be imposed under section 6662 of the Code at the time the taxpayer requests relief and the new position requires a regulatory election for which relief is requested;
- ii. Chooses not to make the election, being fully informed of the required election and related consequences; or
- iii. Uses hindsight in requesting relief. If specific facts have changed since the original deadline that makes the election advantageous to a taxpayer, the Service will not ordinarily grant relief.

Section 6662 of the Code imposes an accuracy related penalty for any underpayment of tax required to be shown on a return, if that underpayment is attributable to one of several different actions.

Section 301.9100-3(c)(1) of the regulations states that the interests of the Government are prejudiced when:

- i. Granting relief would result in a taxpayer having a lower tax liability in the aggregate for all taxable years affected by the election than the taxpayer would have had if the

election had been timely made. Similarly, if the tax consequences of more than one taxpayer are affected by the election, the Government's interests are prejudiced if there is a resulting decrease in the aggregate tax liability for all affected taxpayers.

- ii. If the taxable year in which the regulatory election should have been made, or any taxable years that would have been affected by the election had it been timely made, are closed by the period of limitations on assessment under section 6501(a) of the Code before the taxpayer's receipt of a ruling granting relief under this section, the Government's interests are ordinarily prejudiced.

Section 6501(a) of the Code provides that, in general, the amount of any tax imposed must be assessed within 3 years after the return was filed.

Rev. Rul. 83-74, 1983-1 C.B. 112, granted relief under section 301.9100-1 of the regulations to a homeowner's association seeking to revoke its section 528 election. The Service reasoned that the situation of a taxpayer seeking relief to revoke an election is analogous to one where a taxpayer is seeking relief to make an election, and thus the provisions of section 301.9100-1 of the regulations are applicable.

ANALYSIS

A taxpayer may seek relief under section 301.9100-3 of the regulations for an extension of time to file a regulatory election. An election whose due date is published in the Federal Register is considered a regulatory election under section 301.9100-1(b). The due dates for making and revoking lobbying elections under section 501(h) of the Code were published in the Federal Register. Therefore, the section 501(h) lobbying election is a regulatory election within the meaning of section 301.9100-1(b).

A taxpayer seeking relief to revoke an election is in a position analogous to one seeking relief to make an election, and thus the provisions of section 9100 of the Code are applicable. (Rev. Rul. 83-74, *supra*) Because you are seeking relief to revoke an election, Rev. Rul. 83-74 allows you to seek relief under the provisions of section 301.9100-1 of the regulations.

Relief may be granted if the taxpayer establishes to the satisfaction of the Commissioner that he acted reasonably and in good faith, and that the relief will not prejudice the interests of the Government. (Section 301.9100-3(a) of the regulations, *supra*.) A taxpayer may demonstrate that he has acted reasonably and in good faith by requesting relief before the Service discovers his failure to make the regulatory election, among other methods. (Section 301.9100-3(b) of the regulations, *supra*.) You filed a Schedule A, Part VI-A for your 990 return for year Y as if you had properly revoked your election, with a note alerting the Service to your intent to seek 9100 relief on this matter. You also made this request before the Service discovered your failure to revoke the election. Therefore, you will be deemed to have acted reasonably and in good faith, provided that none of the situations in section 301.9100-3(b)(3) of the regulations apply.

Section 301.9100-3(b)(3) of the regulations sets out three circumstances which show that a taxpayer has not acted reasonably or in good faith, but none apply to you. You are not seeking to alter a return position for which an accuracy related penalty could be imposed because revocation of the lobbying election solely affects the way lobbying expenditures are reported.

You were not informed of the consequences of not revoking the election. You are not using hindsight in requesting relief because no facts have changed since the due date of the revocation that would make the revocation more advantageous. Therefore, you are deemed to have acted reasonably and in good faith within the meaning of section 301.9100-3(b)(3).

For relief to be granted, a taxpayer must also establish that an extension of time would not prejudice the interests of the Government. (Section 301.9100-3(a) of the regulations, *supra*.) The interests of the Government would be prejudiced if granting relief would result in the taxpayer having a lower tax liability than the taxpayer would have had if the election had been timely made. (Section 301.9100-3(c)(1)(ii), *supra*.) If you make a retroactive revocation of your lobbying election, your tax liability, and that of your affiliates, will be the same as it would have been if you had made the revocation during your tax Year X, before the merger took effect. Therefore, the interests of the Government will not be prejudiced because you have a lower tax liability.

The interests of the Government could also be prejudiced if the taxable year in which the regulatory election should have been made, or any taxable years that would have been affected by the election had it been timely made, are closed by the period of limitations on assessment under section 6501(a) of the Code. (Section 301.9100-3(c)(1)(ii) of the regulations, *supra*.) The revocation of your election will only affect years after Year X: Year Y and succeeding years. Three years have not passed since the date you filed your Form 990 return for X Year, nor any of the subsequent years that would be affected. Therefore the year in which the election should have been made and the years which the revocation would affect are still open, and the interests of the Government will not be prejudiced in this manner. (Section 6501(a), *supra*.)

Based on all of the facts and information submitted and the representations made, it is our determination that you acted reasonably and in good faith and granting the requested relief will not prejudice the interests of the Government.

RULING

You are granted an extension of time of 30 days from the date of this letter ruling to file a revocation of your lobbying election, to be effective for all tax years beginning after Year X. You should attach this letter to your amended return.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

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

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes in these facts. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept 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,

Marvin Friedlander, Manager
EO Technical

Enclosure
Notice 437