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Date:
July 25, 2024

LEGEND

Authority	=
State	=
State Law	=
County	=
City	=
Date	=
X	=
Y	=

Dear :

This letter ruling responds to a letter from your authorized representatives dated January 26, 2024, and supplemental documentation dated March 22, 2024, requesting rulings under sections 115 and 170 of the Internal Revenue Code.[1]

FACTS

Authority is a State corporation, incorporated pursuant to State Law by County and City, political subdivisions of State. State Law specifically authorizes State political subdivisions to incorporate organizations such as Authority that, in addition to complying

[1] Unless otherwise noted, all section references are to the Internal Revenue Code of 1986, as amended (the "Code").

with other requirements provided in State Law, have as their purpose the undertaking or support of infrastructure projects that mitigate the effects of climate change. Infrastructure projects include financing the capital costs associated with flood barriers, green spaces, building elevation, and stormwater remediation technology.

State Law permits Authority to assume costs incurred for the acquisition, design, construction, renovation, and expansion of these projects. Authority is tasked with acting as the "general contractor" for these projects, ensuring they are satisfactorily completed according to the terms of the grants they receive for these projects. Upon completing its responsibilities regarding these projects, Authority transfers any ownership and control it assumed back to County and City.

County and City established Authority by, as directed by State Law, adopting enabling legislation describing Authority and its powers. The enabling legislation included Authority's articles of incorporation, which were subsequently adopted on Date and then submitted by County's Executive to, and accepted by, State's Tax Department, as required by State Law. Upon this acceptance, State considers Authority to be a "body politic… and instrumentality" of City and County.

Authority's articles of incorporation limit its purpose to "undertake and support projects in [City] and in [County] that mitigate the impact of climate change[.]" Authority has only those powers granted to it by State Law and City and County law and is not authorized to issue stock. Only County, with the consent of City, may amend Authority's articles of incorporation. State Law, the County and City enabling legislation, and Authority's organizing documents establish that, except as necessary to pay any debt service or implement its public purpose, Authority's net earnings may only benefit City and County and prohibit more than incidental benefits to private persons and interests. Authority represents that, consistent with these requirements, it ensures that private interests do not benefit more than incidentally from Authority's activities. If Authority is terminated, State, County, and City law require that all Authority property be transferred to County and City.

Authority is governed by a 12-member board entirely appointed by County and City. Board members are (i) uncompensated for their efforts, (ii) must be residents of City or County, (iii) demonstrate relevant subject-matter experience, (iv) annually certify a conflict-of-interest statement, and (v) take no financial interest in any Authority project. Before undertaking their responsibilities, each Authority board-member is required to swear a constitutional oath of office before a County court clerk. Authority's board is aided by a Director appointed by County's Executive, who will also serve as a County employee and also may not take any financial interest in any Authority project, as well as an advisory committee comprised of County and City officers with relevant subject-matter portfolios.

State law vests authority in County and City to determine Authority's sources of revenue. Authority's organizing activity is funded by initial grants from County totaling $X. Authority may, and has, raised additional revenue by way of project-specific grants from government entities including the federal government. To date Authority has received project-specific grants from State, County, and federal agencies including the Departments of Energy and Transportation and the National Parks Service. The grants total $Y for projects such as floodplain restoration, coastal erosion restoration and beach renourishment, roadway protection, and motor-vehicle electric charging infrastructure support.

Authority is enabled to issue bonds to finance projects but has not done so and has not indicated any plans to do so in the future. Any bonds issued by Authority will be (i) determined appropriate by County, with advice of City, (ii) issued subject to standard operating procedures and associated with specific projects to be financed, and (iii) not backed by the credit of County or City.

Authority will provide annual written reports on its activities and audited financial statements to State, County, and City, as required by State, County, and City law. Authority is also required to make its books and other records available to County and City officials for inspection as County and City deem appropriate.

RULINGS REQUESTED

1. Authority's income is excludable from gross income pursuant to section 115(1) because Authority's income is derived from its performance of an essential government function and accrues to County and City; and

2. Contributions to Authority are deductible under section 170 because Authority meets the instrumentality criteria provided in Rev. Rul. 57-128 for the purposes of section 170(c)(1).

LAW AND ANALYSIS

Ruling 1

Law

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

Rev. Rul. 77-261, 1977-2 C.B. 45, holds that the income from an investment fund, established pursuant to state law for the temporary investment of cash balances of a State and its participating political subdivisions, is excludable from gross income under

section 115. The ruling explains that section 115(1) represents the desire of Congress to not restrict in any way the ability of a State (or, by implication, its political subdivisions) to participate in enterprises useful in carrying out those projects desirable to the State in their exercise of sovereign powers. Section 115(1), therefore, refers to the income of any State or municipality resulting from a corporation engaged in public utilities or some other government function that accrues to the State or its political subdivisions. The ruling concludes that the investment fund is a separate entity from the State and its political subdivisions but the income from its investment activity was income from the exercise of an essential governmental function, and since the State and its participating political subdivisions had an unrestricted right to their proportionate share of the investment fund's income, the fund's income accrued to them.

Rev. Rul. 90-74, 1990-2 C.B. 34, holds that income of an organization formed, operated, and funded by political subdivisions of a State to pool their casualty risks is excluded from gross income under section 115(1). In this ruling, the political subdivisions were authorized by state law to form and become members of these pools as long as the governing body of the participating political subdivision authorized the political subdivision's participation and appointed individuals to represent the political subdivision in the governing affairs of the pools. Members funded the pools with general revenue. Upon dissolution, all pool assets would be distributed to member political subdivisions. The ruling states that the determination as to whether a function is an essential government function depends on the facts and circumstances of each case. In addition to benefitting the political subdivisions by protecting their financial integrity, the ruling cites the significant involvement of the political subdivisions in the formation and operation of the pools to conclude they are an essential government function. Finally, the ruling concludes, as evidence that the activity is the exercise of an essential government function, that private interests do not, except for incidental benefits to employees of the participating State and political subdivisions, participate in or benefit from the organizations.

Rev. Rul. 71-589, 1971-2 C.B. 94, holds that income from property willed by an individual to be held in trust by a political subdivision as a fund to be used for certain enumerated charitable purposes was excluded from gross income under section 115(1). Although neither the assets or income of the trust accrued directly to the political subdivision, the fact that the gift of the trust was accepted and used by the political subdivision's board of commissioners for designated public purposes ordinarily recognized as municipal functions was sufficient to conclude that the trust's income accrued to the political subdivision.

Analysis

Authority represents that County and City are political subdivisions of State. To the extent that Authority generates income from the exercise of any essential government

function of County or City that accrues to County or City, that income is not includable in Authority's gross income pursuant to section 115(1).

Authority's activities constitute the exercise of an essential government function of County and City. Rev. Rul. 77-261 explains that section 115(1) allows for States and political subdivisions to participate in income-generating enterprises useful and desirable to those entities in exercising their sovereign powers. State passed State Law to specifically authorize political subdivisions such as County and City to form organizations like Authority to further the purposes identified by State in State Law. County and City did so, complying with all requirements under State Law, engaging in significant control of Authority and direction of its activities. City and County expressly provided Authority's power to pursue its mission, control its organizing documents, appoint Authority's board and Director, and have oversight over its financial books, records, and instruments. Authority provides ongoing reporting to County, City, and State. County provided initial funding for Authority's operations and Authority has subsequently been entirely funded by grants from County, City, State, and the federal government. County, City, and State have all demonstrated that Authority is useful and desirable to their exercising of their sovereign powers.

Rev. Rul. 90-74 holds that the determination as to whether an activity is an essential government function depends on all the facts and circumstances. As discussed, County and City's significant involvement in Authority demonstrates their intent to exercise an essential government function through Authority's activities. This involvement is consistent with the facts provided in Rev. Rul. 90-74. Rev. Rul. 90-74 also concludes that an essential government function requires that private interests do not, except for more than incidentally, benefit from the activities. Authority assumes oversight of projects funded by County, City, and other public entities, transferring ownership and control of these projects to these entities upon completion. Authority adheres to strict rules, either by law or its own organizing documents, including conflicts-of-interest statements and requirements that limit the ability of Authority insiders and other persons to privately benefit from Authority's activity. If Authority is terminated, title to all Authority property transfers to County and City. County, City, and State directly benefit from Authority's exercise of the functions delegated to it. Any private interests benefit from Authority's activity only incidentally, either in their capacity as project contractors, or members of the general public.

Authority's income related to its exercise of essential government functions accrues to County and City. Rev. Rul. 71-589 explains that income accepted and used by an entity for an essential government function is income that accrues to political subdivisions. County and City control and direct authority's activities furthering the specific purpose identified by State in State Law. County and City law and Authority's organizing documents require it to be organized and operated exclusively to further the essential government functions identified by County and City as the purpose of Authority. Authority's net earnings are prohibited by State, County, and City law from being used

to benefit private interests. In these circumstances, Authority's income accrues to political subdivisions.

Authority's income is excludable from gross income under section 115(1) because it is derived from its performance of an essential government function and accrues to County and City.

Ruling 2

Law

Section 170(a)(1) of the Code provides that there shall be allowed as a deduction any charitable contribution (as defined in section 170(c)) payment of which is made within the tax year.

Section 170(c)(1) states that, for purposes of section 170, the term "charitable contribution" means a contribution or gift to or for the use of a state, a possession of the United States, or any political subdivision of any of the foregoing, or the United States or the District of Columbia, but only if the contribution or gift is made for exclusively public purposes.

The determinative question as to whether an entity has the status of a political subdivision is whether it has been delegated any of a state's sovereign powers. The three generally acknowledged sovereign powers are the police power, the power to tax, and the power of eminent domain. Estate of Shamberg, 3 T.C. 131, 143, aff'd, 144 F.2d 998 (2d Cir.), cert. denied, 323 U.S. 792 (1944). It is not necessary that all three of these powers be delegated in order to treat an entity as a political subdivision for purposes of the Internal Revenue Code. Id.

Section 170(c)(1) does not refer to instrumentalities of a political subdivision. However, the long-standing position of the Internal Revenue Service is that contributions or gifts to an instrumentality of a state or an instrumentality of a political subdivision are considered to be "for the use of" of a state or a political subdivision rather than gifts "to" a state or political subdivision. The significance of this distinction is that a gift "for the use of" a state or political subdivision is subject to the 30-percent limitation of section 170(b)(1)(B). See Rev. Rul. 75-359, 1975-2 C.B. 79.

Rev. Rul. 57-128, 1957-1 C.B. 311, provides that, in cases involving the status of an organization as a wholly-owned instrumentality of a state or political subdivision, the following factors are considered —

(1) whether the organization is used for a governmental purpose and performs a governmental function;

(2) whether the organization's function is performed on behalf of a state or political subdivision;

(3) whether any private interests are involved, or whether a state or political subdivision has the powers and interests of an owner;

(4) whether the control and supervision of the organization is vested in a public authority;

(5) whether express or implied statutory or other authority is necessary for the creation or use of the organization, and whether such authority exists; and

(6) the degree of the organization's financial autonomy and the source of its operating expenses.

Rev. Rul. 75-359, 1975-2 C.B. 79, found that a voluntary association of counties was separate from its member counties and qualified as a wholly-owned instrumentality of those counties, which were political subdivisions, and that it was formed and operated exclusively for the public purposes of the member counties. Therefore, the ruling held that contributions to the association were deductible as contributions for the use of political subdivisions, subject to the limitation of section 170(b)(1)(B).

Rev. Rul. 69-453, 1969-2 C.B. 182, applied the six factors of Rev. Rul. 57-128 to hold that a soil and water conservation district formed as a private non-stock corporation by private individuals was not an instrumentality of the state. The ruling found that the state had no authority or control over the district's expenditures, that it had no authority to remove any member of the district's board, and that the district funded its operations through fees that it charged landowners for work done for the purpose of soil conservation. The ruling noted that the state had no claim to the district's assets after the district's dissolution.

Rev. Rul. 65-196, 1965-2 C.B. 388, held that a sports area commission formed pursuant to an agreement (which was authorized by the enactment of a state law legalizing such agreements) among a city and two villages to erect and operate an athletic stadium was an instrumentality of political subdivisions of the state. The commission was composed of members appointed by the councils of the city and the villages as their representatives. Each member was required to be a citizen and resident of the state and could not be a member of the governing body of the city or the villages. The sole source of financing for the commission came from bonds issued by the city; the city was authorized to issue bonds upon the request of the commission to fund the athletic stadium. The ruling found that the commission was an instrumentality of the city and the two villages by whose agreement it was formed, because it met substantially all of the Rev. Rul. 57-128 factors: the commission was created by the city and the villages as their instrumentality, and validated by state law; the commission members were

delegated certain authority under the terms of the agreement among the city and the villages; control and supervision of the assets of the commission were in the hands of the city and the villages; there were no private interests involved; and the city, upon the commission's direction, was responsible for the project's finances.

Analysis

As stated above, section 170(c)(1) generally defines the term "charitable contribution," for purposes of section 170(a)(1), to include a contribution or gift to or for the use of a state or any political subdivision of the state, provided the contribution or gift is made for exclusively public purposes.

Authority is not itself a political subdivision of State. Therefore, contributions to Authority cannot constitute charitable contributions to a political subdivision of State for purposes of section 170(c)(1). However, pursuant to Rev. Rul. 75-359, contributions to Authority may constitute charitable contributions for the use of a political subdivision of State, which are deductible under section 170(a), subject to the limitation of section 170(b)(1)(B), if Authority qualifies as a separate, wholly-owned instrumentality of one or more political subdivisions of State. Whether Authority is a wholly-owned instrumentality of a state or political subdivision of a state is determined by applying the six factors of Rev. Rul. 57-128.

The first factor under Rev. Rul. 57-128 is whether Authority is used for a governmental purpose and performs a governmental function. Authority was created by County and City, which are political subdivisions of State, as authorized by State Law, to undertake or support infrastructure projects that mitigate the effects of climate change in City and County. Thus, State, through its legislature, has identified the development of this infrastructure as a legitimate function of the counties and cities within State. Accordingly, we conclude that Authority is used for a governmental purpose and performs a governmental function.

The second factor under Rev. Rul. 57-128 is whether the performance of Authority's function is on behalf of a state or political subdivision. Authority's board is appointed by County and City and its Director is appointed by the County Executive pursuant to County and City law as authorized by State Law. Therefore, Authority's function is carried out on behalf of County and City for the general purpose of mitigating the effects of climate change to individuals living in County and City. Consequently, we find that Authority's function is performed on behalf of County and City, which are political subdivisions of State.

The third factor under Rev. Rul. 57-128 is whether any private interests are involved, or whether a state or political subdivision has the powers and interests of an owner. State County, and City law provide that except as necessary to pay debt service or implement the public purposes or programs of County or City, the net earnings of Authority may

benefit only County and City and may not benefit any person. Authority represents that no private interests will participate in, or benefit from Authority except in a manner incidental to the public benefit provided by Authority. Annually, Authority's board members are required to execute a statement affirming whether or not they have an interest that is or may be perceived to be an actual or possible conflict of interest.

Additionally, State, County, and City law provides that if Authority ever terminates, title to all Authority's property shall be transferred to County and City and all Authority's obligations shall be transferred to and assumed by County and City.

Consequently, we conclude that no private interests are involved in Authority. Rather, we find that political subdivisions of State have the powers and interests of an owner with respect to Authority.

The fourth factor under Rev. Rul. 57-128 is whether the control and supervision of Authority is vested in a public authority. County and City created Authority as authorized by State, County, and City law. Authority is governed by the board, the members of which are appointed by County and City. Authority is required by law to provide State, County, and City with an annual report and audited financial statements. Therefore, we conclude that the control and supervision of Authority is vested in a public authority.

The fifth factor under Rev. Rul. 57-128 is whether express or implied statutory or other authority is required to create or use Authority, and whether such authority exists. Pursuant to State Law, a local government may create an authority by local law. Accordingly, County's Executive formed Authority by filing articles of incorporation with State's Tax Department. County, with the concurrence of City, can set or change the powers, structure, organization, procedures, programs, or other activities of Authority. Consequently, we conclude that express statutory authority is necessary for the creation and use of Authority and that such authority does exist.

The sixth factor under Rev. Rul. 57-128 is the degree of Authority's financial autonomy and the source of its operating expenses. Authority has represented that its activities are financed by State, County, and U.S. federal grants. The financial affairs of Authority are managed by the board, which is appointed by County and City, and supervised by State, County, and City officials. Therefore, we find Authority is not financially autonomous from any political subdivision of State.

For the reasons stated above, application of the factors set forth in Rev. Rul. 57-28 weigh in favor of a finding that Authority is a wholly-owned instrumentality of one or more political subdivisions of State, specifically, County and City. Therefore, contributions made to Authority exclusively for a public purpose may be deductible by donors as charitable contributions under section 170(c)(1) to the extent otherwise provided under section 170.

CONCLUSIONS

Therefore, we rule that:

1. because Authority's income is derived from its performance of an essential government function and accrues to County and City, it is excludable from gross income under section 115(1); and

2. Because Authority is an instrumentality for purposes of section 170(c)(1), contributions to it are deductible to the extent otherwise allowable by section 170.

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The rulings contained in this letter are based upon information and representations submitted by or on behalf of Authority and accompanied by penalties of perjury statements executed by an individual with authority to bind Authority and upon the understanding that there will be no material changes in the facts. *See* Rev. Proc. 2024-1 § 7.01(16), 2024-1 I.R.B. 1. This office has not verified any of the material submitted in support of the request for this ruling, and such material is subject to verification on examination. The Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes) will revoke or modify a letter ruling and apply the revocation retroactively if: 1) there has been a misstatement or omission of controlling facts; 2) the facts at the time of the transaction are materially different from the controlling facts on which the letter ruling was based; or 3) the transaction involves a continuing action or series of actions and the controlling facts change during the course of the transaction. *See* Rev. Proc. 2024-1 § 11.05, 2024-1 I.R.B. 1.

This letter does not address the applicability of any section of the Code or Treasury regulations other than those sections specifically described. Except as expressly provided herein, no opinion is expressed or implied concerning the federal tax consequences of any fact or issue discussed or referenced in this letter.

This letter is directed only to Authority. Section 6110(k)(3) provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to Authority's authorized representatives.

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.
Senior Tax Law Specialist
Exempt Organizations Branch 2
(Employee Benefits, Exempt Organizations, and Employment Taxes)

cc: