

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:ITA:B01

PLR-107043-14

Date:

May 30, 2014

Legend

Taxpayer =

Foundation =

State =

Member 1 =

Member 2 =

Facility 1 =

Facility 2 =

Facility 3 =

Certificate =

Commissioner =

Services =

Condition 1 =

Condition 2 =

Condition 3 =

a =

b =

c =

d =

e =

f =

g =

h =

Dear _____ :

This responds to your letter dated February 7, 2014, requesting rulings on behalf of Taxpayer. Taxpayer requests a ruling on the proper treatment of certain payments made to charitable organizations under §§ 162 and 170 of the Internal Revenue Code.

RULINGS REQUESTED

- (1) Taxpayer's payments, which are required by law to be made to charitable organizations, including payments made to Foundation, are not deductible under § 170.
- (2) These payments are deductible ordinary and necessary business expenses under § 162(a).

FACTS

Taxpayer is a State Limited Liability Company treated as a partnership for federal income tax purposes. Taxpayer began operating in 2010 as a joint venture between Member 1 and Member 2. Member 1 is a nonprofit corporation exempt from taxation under § 501(c)(3) and owns a% of Taxpayer. Member 2 is a professional corporation that owns the remaining b%. Taxpayer offers Services at three facilities: Facility 1, Facility 2, and Facility 3.

In State, owners and sponsors of identified facilities like that of Taxpayer are required to obtain a Certificate from the Commissioner. The Commissioner is authorized to impose three conditions on the recipient of a Certificate in order for the recipient to continue to operate: (1) Condition 1; (2) Condition 2; and (3) Condition 3. When a service provider's Certificate is subject to Condition 3, the provider may satisfy its conditions with direct payments to organizations approved by Department to receive and distribute contributions satisfying Certificate conditions.

Taxpayer is subject to Condition 1 and Condition 3. Together, the combined value of satisfying both conditions for Facility 1 must equal at least c% of gross revenue derived from operating specific equipment at that Facility covered by the Certificate. For Facility 2, the combined value must equal at least d%, and for Facility 3, the combined value must equal at least e%. Taxpayer's annual shortfall between the required percentage and its actual services provided to satisfy the conditions varies from year to year. To make up for the shortfall and satisfy the conditions placed on its Certificate, Taxpayer makes cash contributions to qualified § 501(c)(3) organizations. For 2010, Taxpayer paid \$f in qualifying cash contributions; for 2011, it paid \$g; and for 2012, it paid \$h. The

majority of these cash contributions were paid to Foundation, a non-stock, not-for-profit corporation that is also the parent of Member 1.

LAW AND ANALYSIS

Section 170(a) of the Code provides, subject to certain limitations, a deduction for contributions and gifts to or for the use of organizations described in § 170(c), payment of which is made within the taxable year.

A contribution for purposes of § 170 of the Code is a voluntary transfer of money or property that is made without receipt or expectation of financial or economic benefit commensurate with the amount of the transfer. Transfers of property that bear a direct relationship to the taxpayer's trade or business and that are made with a reasonable expectation of financial return commensurate with the amount of the transfer may constitute allowable deductions under § 162 as trade or business expenses. See § 1.170A-1(c)(5) of the Income Tax Regulations and H.R. Rep. No. 1337, 83 Cong., 2d Sess. A44 (1954).

Section 162(a) of the Code allows a deduction for all the ordinary and necessary expenses of carrying on a trade or business. See also § 1.162-1(a) of the Income Tax Regulations. Section 162(b) provides that a deduction will not be permitted under § 162(a) for a contribution or gift that would be allowed as a charitable deduction were it not for the limitations of § 170.

Section 1.162-15(a)(2) of the regulations states that the limitation provided in § 162(b) of the Code applies to payments which are, in fact, contributions or gifts to organizations described in § 170 of the Code.

Rev. Rul. 72-314, 1972-1 C.B. 44, provides that whether payments to a charitable organization are deductible pursuant to § 170 or pursuant to § 162 depends upon whether the payments are completely gratuitous or whether they bear a direct relationship to the taxpayer's business and are made with a reasonable expectation of a financial return commensurate with the amount of the payment. See also Rev. Rul. 77-124, 1977-1 C.B. 39, and Rev. Rul. 63-73, 1963-1 C.B. 35.

Taxpayer's contributions, which it makes to satisfy the conditions of its Certificate under the law of State, are not deductible under § 170(a). The payments are not voluntary, nor are they completely gratuitous. As a provider of Services in State, Taxpayer is subject to the regulatory authority of the Commissioner, and must satisfy the conditions of its Certificate to continue to operate. The payments are no more than c% of Taxpayer's gross revenue, and are made annually in order to comply with rules of the governmental entity regulating Taxpayer's right to conduct its business operations in State. Failure to make those payments could jeopardize Taxpayer's continued business operations in State. The payments therefore bear a direct relationship to the taxpayer's

business and are made with a reasonable expectation of financial return commensurate with the amount spent.

Accordingly, we conclude that the contributions are ordinary and necessary business expenses that are deductible under § 162.

CONCLUSIONS

- (1) Taxpayer's payments, which are required by law to be made to charitable organizations, including payments made to Foundation, are not deductible under § 170.
- (2) These payments are deductible ordinary and necessary business expenses under § 162(a).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code 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 your authorized representatives.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Lewis K. Brickates
Chief, Branch 1
Office of Associate Chief Counsel
(Income Tax & Accounting)