

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Date:
August 09, 2024

Taxpayer =
State =
Statute =

Dear :

This letter responds to a letter from your authorized representative, dated February 9, 2024, and subsequent documentation dated June 4, 2024, and July 23, 2024, requesting a ruling that Taxpayer’s income is excludable from gross income under section 115(1) of the Internal Revenue Code (Code). Taxpayer represents the facts as follows.

FACTS

Statute authorizes public agencies in State to work together to perform any lawful activity. In accordance with Statute, certain school districts in State entered an Agreement to establish Taxpayer for purposes of self-insuring property belonging to the school districts. Taxpayer maintains that it helps the school districts protect against casualty and property risks at a cost that is less than the price of purchasing insurance from a commercial insurance company. To this end, Taxpayer maintains a self-funded risk sharing pool on behalf of participating school districts. Taxpayer also purchases commercial insurance to shield against excess risk.

A board of directors consisting of an administrator and at least five members governs Taxpayer. Each director must be a representative of a participating school district. The board of directors appoints officers to oversee Taxpayer’s activities.

The Agreement provides that no private interests can receive any net earnings or profit from Taxpayer’s operations, except as reasonable compensation for services rendered to or on behalf of Taxpayer. Upon dissolution, Taxpayer must distribute its remaining

assets to State, a political subdivision of State, or an entity whose income is excludable from gross income under section 115(1) of the Code.

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 governmental function and accruing to a state or any political subdivision thereof.

Rev. Rul. 77-261, 1977-2 C.B. 45, holds that income generated by an investment fund that is established by a state to hold revenues in excess of the amounts needed to meet current expenses is excludable from gross income under section 115(1) of the Code, because such investment constitutes an essential governmental function. The ruling states that the statutory exclusion is 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 an entity engaged in the operation of a public utility or the performance of some governmental function that accrues to either a state or political subdivision of a state. The ruling explains 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 that are within the ambit of a sovereign to conduct.

Rev. Rul. 90-74, 1990-2 C.B. 34, holds 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 section 115(1) of the Code, because the organization is performing an essential governmental function. The revenue ruling states that the income of such an organization is excludable from gross income so long as private interests do not participate in the organization or benefit more than incidentally from the organization. The benefit to the employees of the insurance coverage obtained by the member political subdivisions was deemed incidental to the public benefit.

In this case, school districts in State formed Taxpayer to administer a program of collective self-insurance to provide them with property and casualty insurance coverage. By providing such insurance to participating school districts, Taxpayer performs an essential governmental function. See Rev. Rul. 90-74.

Taxpayer's income accrues to State or political subdivisions of State. Private interests benefit only incidentally. In no event, including upon dissolution, will Taxpayer's assets be distributed to any entity that is not a state, a political subdivision of the state, or another entity the income of which is excludable from its gross income by application of section 115(1) of the Code.

RULING

Based on the information and representations submitted on behalf of Taxpayer, we conclude that, because Taxpayer derives its income from the exercise of an essential governmental function, and because Taxpayer's income accrues to a state or a political subdivision of a state, Taxpayer's income is excludable from gross income under section 115(1) of the Code.

The ruling contained in this letter is based on information and representations submitted by or on behalf of Taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party, and on the understanding that there will be no material changes in the facts described above. While this office has not verified any of the material submitted in support of the request for a ruling, the material is subject to verification upon examination. The Associate office will revoke or modify a letter ruling and apply the revocation retroactively if there has been a misstatement or omission of controlling facts; the facts at the time of the transaction are materially different from the controlling facts on which the ruling was based; or, in the case of a transaction involving a continuing action or series of actions, the controlling facts change during the course of the transaction. See Rev. Proc. 2024-1, section 11.05.

This letter does not address the applicability of any section of the Code or Treasury Regulations to the facts submitted other than with respect to the sections specifically described, and, except as expressly provided in this letter, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item of income discussed or referenced in this letter.

This ruling is directed only to Taxpayer. 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 Taxpayer's authorized representative.

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

Sincerely,

Kenneth M. Griffin
Chief
Exempt Organizations Branch 3
(Employee Benefits, Exempt Organizations,
and Employment Taxes)

cc: