



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Release Number: **201217025**
Release Date: 4/27/2012
Date: January 20, 2012

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Legend:

B = State
C = School

UIL Index:

6033.01-00
6033.00-00

Dear

We have considered your request for a ruling that you are not required to file annual information returns on Form 990, Return of Organization Exempt From Income Tax, pursuant to Rev. Proc. 95-48, 1995-2 C.B. 418. Based on the information provided, we have concluded that you do not meet requirements to be excepted from filing Form 990. The basis for our conclusion is set forth below.

Issue:

Do you meet the requirements to be excepted from filing Form 990 as a governmental affiliate? No, for the reasons explained below.

Facts:

You were incorporated under the laws of B. You subsequently filed an application with C School District to operate a charter school. Based on the information provided, you were recognized as a charter school exempt under code §501(3). You offer a full range of educational programs for basic kindergarten through twelfth grade as well as preschool,

special, vocational, gifted and talented programs, bilingual education and many other services and programs.

Each charter school in your district has a separate governing board; however, the Board of Education must approve all charter school applications and budgets. The charter schools are discretely presented components of the C School District's annual reports because the district is accountable for your financial reporting.

C School District approved your application to form and operate a charter school. Your governing body consists of five members elected by your school community. Section 7 of your charter contract indicates that your Board of Directors shall be accountable for the governance and operations of your school.

Section 7.9.1 of your charter contract provides that your Board of Directors have the authority to act independently when contracting for goods and services, selecting personnel, procuring equipment and furniture, and that you are to be solely responsible for purchases and/or financial agreements.

According to your school handbook, your board election procedures consist of an annual election held by your existing Board of Directors. You will send notices in your school handbook informing parents that a seat or seats are up for election at your annual meeting of members. A couple weeks prior to the election, information regarding voting will be distributed to parents. Candidates receiving the most votes at your annual meeting shall be elected.

Your budget is annually reviewed and approved by your School District. Your school is responsible for providing the school district with written revenue and expenditure reports in addition to annual financial statement that reports detailing the costs of administration, instruction and other spending categories, consistent with the format required by state law.

You stated that you do not have a ruling or determination letter from the Internal Revenue Service (Service) recognizing you as an affiliate of a governmental unit.

Law:

Section 501(a) of the Code provides, in part, that organizations described in section 501(c) are exempt from federal income tax. Section 501(c)(3) of the Code describes, in part, an organization which is organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purpose, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 6033(a)(1) of the Code generally requires the filing of annual information returns by exempt organizations.

Section 6033(a)(2)(A) of the Code provides certain mandatory exceptions to filing annual information returns.

Section 6033(a)(2)(B) of the Code provides discretionary exceptions from filing such returns where the Secretary "determines that such filing is not necessary to the efficient administration of the tax laws."

Rev. Proc. 95-48 provides an exception from filing for governmental units or affiliates of governmental units that are exempt from federal income tax under section 501(c)(3).

Section 4.02(a) of Rev. Proc. 95-48 provides that an organization will be treated as an affiliate of a governmental unit if it is described in section 501(c) and it has a ruling from the Service that:

- (1) Its exempt purpose income is excluded under section 115;
- (2) It is entitled to receive deductible contributions under section 170(c)(1) because the contributions are for the use of a governmental unit, or
- (3) It is a wholly owned instrumentality of a state or political subdivision for employment tax purposes; or (b) it meets the requirements of Section 4.02(b).

Section 4.02(b) of Rev. Proc. 95-48 provides the following criteria to be used to determine whether an organization meets the requirements of Section 4.02(b):

- (1) The organization is either operated, supervised or controlled (within the meaning of section 1.509(a)-4(g)(1)(i) of the regulations) by governmental units or by an organization's governing body that is elected by the public at large;
- (2) The organization possesses two or more affiliation factors listed under Section 4.03 of the revenue procedure; and
- (3) The organization's filing of Form 990 is not otherwise necessary to the efficient administration of the internal revenue laws.

Section 4.03 of Rev. Proc. 95-48 describes among the affiliation factors the following:

(a) the organization was created by one or more governmental units, organizations that are affiliates of governmental units, or public officials acting in their official capacity.

(b) The organization's support is received principally from taxes, tolls, fines, government appropriations, or fees collected pursuant to statutory authority. Amounts received as government grants or other contract payments are not qualifying support under this paragraph.

(c) The organization is financially accountable to one or more governmental units. This factor is present if the organization is:

- (i) required to report to governmental unit(s), at least annually, information

comparable to that required by Form 990; and

(ii) is subject to financial audit by the governmental unit(s) to which it reports. A report submitted voluntarily by the organization does not satisfy clause (i). Also, reports and audits pursuant to government grants or other contracts do not alone satisfy this paragraph (c).

(d) One or more governmental units, or organizations that are affiliates of governmental units, exercise control over, or oversee, some or all of the organization's expenditures (although it is not financially accountable to governmental units as described in paragraph (c) of this section).

(e) If the organization is dissolved, its assets will (by reason of a provision in its articles of organization or by operation of law) be distributed to one or more governmental units, or organizations that are affiliates of governmental units within the meaning of section 4 of this revenue procedure.

Section 4.04 of Rev. Proc. 95-48 provides that in making a ruling or determination whether the organization's filing of Form 990 is otherwise necessary to the efficient administration of the internal revenue laws under section 4.02(b)(iii), all relevant facts and circumstances shall be considered.

Relevant facts and circumstances suggesting that filing is necessary for efficient tax administration include the extent to which the organization has taxable subsidiaries or participates in joint ventures with non-exempt entities; whether it engages in substantial public fund-raising efforts; and whether its activities provide significant benefits to private interests.

Application of Law:

Based on the information you submitted, and for the reasons explained below, we have concluded that it is not in the interest of sound tax administration to approve your request for exception from filing Form 990 as a governmental affiliate.

In order to qualify for the exception from the 990 filing requirement, you must demonstrate that you are:

1. A governmental unit, or
2. Closely affiliated with a governmental unit.

You are not a governmental unit, so we have considered whether you are closely affiliated with a governmental unit. Section 4.02(a) and 4.02(b) of Rev. Proc. 95-48 provide the circumstances under which an organization will be treated an affiliate of a governmental unit.

Section 402(a) requires that you have a ruling or determination from the Service that you are "an affiliate of a governmental unit." You do not have the necessary ruling.

You, also, do not meet the exception provided by Section 4.02(b) because:

- (i) Your officers, directors or trustees are not appointed or elected by a governmental unit or the public at large.
- (ii) You do not possess more than 2 of the affiliation factors under section 4.03:
 - You were not created by a governmental unit, affiliate or public official;
 - The payments you receive from the school district are based on contractual obligation rather than statutory authority;
 - The annual reports you provide to the school district are provided pursuant to your contract, not statutory financial accountability to the school district; and
 - There is no evidence that any governmental unit has the right to exercise control over your expenditures beyond the terms of your contract with the school district.
 - Finally, the fact that your assets will be distributed to a governmental unit on your dissolution is a single factor that is not sufficient to ensure that your current operations are subject to the supervision and control of C School District.
- (iii) The Service has not found that the efficient administration of the internal revenue laws will be promoted if you or similar organizations are granted relief from the Form 990 requirement.

Applicant's Position:

You assert that your charter contract shows that you are operated, supervised or controlled (within the meaning of section 1.509(a)-4(g)(1)(i) of the regulations) by governmental unit(s) or by an organization's governing body that is elected by the public at large. You assert that the school district you are affiliated with has the authority to terminate your charter contract for non-compliance under any of its terms.

Service's Response to Applicant's Position:

Your organization is not operated, supervised or controlled (within the meaning of section 1.509(a)-4(g)(1)(i) of the regulations) by governmental units or by an organization's governing body that is elected by the public at large. Your annual election is restricted to parents of your student body and is not open to the public at large. Your affiliated governmental unit does not exercise the control and discretion over your governing body comparable to that of a parent and subsidiary.

Conclusion:

Based on the information you submitted and in accordance with Rev. Proc. 95-48, we deny your request for exception from filing Form 990 as a governmental affiliate as it is not in the interest of sound tax administration.

As explained above, you are not a government unit, and you are not closely affiliated with a governmental unit.

Accordingly, we conclude it is not in the interest of sound tax administration to grant your request for exception from filing Form 990 as a government affiliate.

Filing Penalties and Revocation of Tax-Exempt Status:

If a Form 990 or Form 990-EZ is not filed, the IRS may assess penalties on the organization of \$20 per day until it is filed. This penalty also applies when the filer fails to include required information or to show correct information. The penalty for failure to file a return or a complete return may not exceed the lesser of \$10,000 or 5 percent of the organization's gross receipts. For an organization that has gross receipts of over \$1 million for the year, the penalty is \$100 a day up to a maximum of \$50,000. The IRS may impose penalties on organization managers who do not comply with a written demand that the information be filed.

Section 6033(j) of the Code provides that failure to file Form 990, Form 990-EZ, or Form 990-n for 3 consecutive years results in revocation of tax-exempt status as of the filing due date for the third return. An organization whose exemption is revoked under this section must apply for reinstatement by filing a Form 1023 and paying a user fee, whether or not the organization was originally required to file for exemption. Reinstatement of exemption may be retroactive if the organization shows that the failure to file was for reasonable cause. Information with respect to the implementation of Section 6033(i) is available at www.irs.gov/eo.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Lois G. Lerner
Director, Exempt Organizations

Enclosure: Notice 437

A redacted copy of this letter