

26 CFR 601.201: Rulings and determination letters.
(Also section 115.)

Rev. Proc. 2003-12

SECTION 1. PURPOSE

This Revenue Procedure provides guidance on dissolution provisions for any organization described in § 501(c)(3) and exempt from federal income tax under § 501(a) of the Code that requests a letter ruling that its income is excluded from gross income under § 115(1).

SECTION 2. BACKGROUND

.01 Section 115(1) of the Code provides that gross income does not include income that is (i) derived from a public utility or from the exercise of any essential governmental function (the “essential government function test”), and (ii) accruing to a State, any political subdivision thereof, or the District of Columbia (the “accrual test”). An entity is not required to obtain a ruling from the Service to claim an exclusion from gross income under § 115(1).

.02 One aspect of the accrual test of § 115(1) is that assets of the organization must be distributed upon the organiza-

tion’s dissolution to one or more States, political subdivisions thereof, the District of Columbia, or to other organizations the income of which is excluded from gross income under § 115(1) (the “distribution of assets upon dissolution requirement”). The assets of an entity described in § 115(1) may not be distributed upon dissolution (or at any other time) to the United States government. *See* Rev. Rul. 90-74, 1990-2 C.B. 34; Rev. Rul. 77-261, 1977-2 C.B. 45; Rev. Rul. 71-589, 1971-2 C.B. 94. An organization seeking a ruling under § 115(1) will not be found to satisfy the distribution of assets upon dissolution requirement of the

§ 115(1) accrual test if its articles of organization fail to limit distribution of all the organization's assets upon dissolution to one or more States, political subdivision(s) thereof, the District of Columbia, or to other organizations whose income is excluded from gross income under § 115(1).

.03 An organization may be described in § 501(c)(3) of the Internal Revenue Code and its income may also be excluded from gross income under § 115(1). *See* Treas. Reg. § 1.6033-2(g)(1)(v) (a state institution exempt from taxation under § 501(a) the income of which is excluded from gross income under § 115(a) (now § 115(1)) is not required to file an annual information return on Form 990, *Return of Organization Exempt From Income Tax*); *see also* Rev. Proc. 95-48, §§ 3.01, 4.02, 1995-2 C.B. 418.

.04 To qualify as an organization described in § 501(c)(3) and exempt from federal income tax under § 501(a), an organization must meet the requirements of the organizational test of § 501(c)(3). One requirement of the organizational test is that the assets of the organization be dedicated to an exempt purpose. Treas. Reg. § 1.501(c)(3)-1(b)(4).

.05 A § 501(c)(3) organization's articles of organization must contain a dissolution clause that satisfies the organizational test of § 1.501(c)(3)-1(b)(4) of the Treasury Regulations, unless the organization is organized under State laws that satisfy the distribution of assets upon dissolution provisions of § 1.501(c)(3)-1(b)(4). *See* Treas. Reg. § 1.501(c)(3)-1(b)(4); Rev. Proc. 82-2, 1982-1 C.B. 367.

SECTION 3. APPLICATION

A § 501(c)(3) organization can satisfy the organizational test of § 1.501(c)(3)-1(b)(4) of the Treasury Regulations by reason of its articles of organization or by operation of law. However, for purposes of obtaining a § 115(1) ruling, a § 501(c)(3) organization will not satisfy the "distribution of assets upon dissolution requirement" of § 115(1) unless its articles of organization also limit distribution of assets on dissolution (to the extent consistent with § 1.501(c)(3)-1(b)(4)) to one or more States, political subdivisions of States, the District of Columbia, or other organizations the income of which is excluded under § 115(1). For purposes of obtaining a § 115(1) ruling, the organization may not

rely on a provision of state law to satisfy the distribution of assets upon dissolution requirement of § 115(1).

SECTION 4. EXAMPLES

.01 Organization A is exempt from federal income tax under § 501(a) as an organization described in § 501(c)(3). Organization A has a dissolution clause in its articles of organization that satisfies Treas. Reg. § 1.501(c)(3)-1(b)(4). Organization A's articles state that, upon dissolution, any assets remaining after the payment of debts and the satisfaction of liabilities are to be distributed (1) to an organization described in § 501(c)(3) for one or more exempt purposes, or (2) to the United States government, or to a State or local government, for a public purpose. Organization A requests a letter ruling that its income is excluded from gross income under § 115(1). Although the dissolution clause in the articles of Organization A meets the organizational requirements of § 501(c)(3), the dissolution clause allows for distribution to entities to which distributions may not be made under § 115(1). The dissolution clause, therefore, fails to satisfy the distribution of assets upon dissolution requirement of the accrual test of § 115(1). In these circumstances, a favorable ruling on § 115(1) would not be issued.

.02 Organization B is exempt from federal income tax under § 501(a) as an organization described in § 501(c)(3). Organization B has a dissolution clause in its articles of organization that satisfies Treas. Reg. § 1.501(c)(3)-1(b)(4). Organization B's articles state that, upon dissolution, any assets remaining after the payment of debts and the satisfaction of liabilities are to be distributed either (1) to a State or political subdivision thereof for a public purpose or (2) for one or more exempt purposes to an organization described in § 501(c)(3) and whose income is also excludable from gross income under § 115(1). Organization B requests a letter ruling that its income is excluded from gross income under § 115(1). The dissolution clause in the articles of Organization B meets the requirements of the organizational test of § 501(c)(3) and also satisfies the distribution of assets upon dissolution requirement of the accrual test of § 115(1).

.03 Organization C is exempt from federal income tax under § 501(a) as an organization described in § 501(c)(3). Upon

dissolution, Organization C's remaining assets will be distributed by operation of the law of Organization C's state of incorporation to a political subdivision of the state for a public purpose. Organization C requests a letter ruling that its income is excluded from gross income under § 115(1). Although state law provides a dissolution distribution scheme that meets the organizational test of Treas. Reg. § 1.501(c)(3)-1(b)(4), the state's dissolution provision fails to satisfy the accrual test of § 115(1) for purposes of obtaining a § 115(1) letter ruling. In these circumstances, a favorable ruling on § 115(1) would not be issued. To receive a favorable § 115(1) letter ruling, Organization C must have articles of organization that contain a provision satisfying the distribution of assets upon dissolution requirement for the § 115(1) accrual test.

SECTION 5. DRAFTING INFORMATION

The principal author of this revenue procedure is Sara T. S. Wolff of the Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). For further information regarding this revenue procedure, contact Ms. Wolff at (202) 622-6080 (not a toll-free call).