



Lessening the Burdens of Government as a Basis for Tax Exemption under IRC Section 501(c)(3)

Issue Title:

Lessening the Burdens of Government as a Basis for Tax Exemption under IRC Section 501(c)(3)

Description:

Whether an organization is lessening the burdens of government is determined by considering all relevant facts and circumstances. First, it is necessary to identify whether an organization is conducting activities that a governmental unit considers to be its burden, and, second, whether such activities actually lessen the governmental burden.

IRC Section and Treas. Regulation:

IRC Section 501(c)(3) Tax-exempt organizations

Treas. Reg. Section 1.501(c)(3)-1(d)(2): the term "charitable" includes "lessening the burdens of government."

Resources (Court Cases, Chief Counsel Advice, Revenue Rulings, Internal Resources):

Court Cases:

Columbia Park & Recreation Assn. v. Commissioner, 88 T.C. 1 (1987), aff'd. without published opinion, 838 F. 2d 465 (4th Cir. 1988): The Tax Court held that the mere assertion that, in petitioner's absence, government would have had to assume the activities in question did not mean the activities were, in fact, the burdens of government.

Indiana Crop Improvement Association, Inc. v. Commissioner, 76 T.C. 394 (1981), acq., 1981-2 C.B. 1: The Tax Court held an association whose primary activity was the certification of crop seed under State and Federal law was exempt under section 501(c)(3). The association was specifically delegated these functions in accordance with State law.

Quality Auditing Company, Inc. v Commissioner, 114 T.C. 498 (2000): The Court determined that the organization did not lessen the burdens of government, and that even if it did lessen the burdens, the organization more than incidentally served private interests of the owners and developers. See also Asmark Institute v. Commissioner, T.C. Memo 2011-20, aff'd. 2012 WL 2550474 (6th Cir. 2012)

Public Industries, Inc. v. Commissioner, T.C. Memo 1991-3: Citing Federal and State law, the court concluded that neither the Federal government nor the government of the state of petitioner's incorporation viewed petitioner's activity – purchasing prison-made goods for sale to the private sector - as a proper governmental function.

Revenue Rulings:

Rev. Rul. 85-1 holds that lessening the burdens of government occurs only if the governmental unit formally recognizes the activities of the organization to be its burden. This objective manifestation may be evident in the interrelationship between the organization and the governmental unit. The organization's activities were an integral part of a larger governmental program and the organization funded governmental expenses.

The fact that a governmental unit expresses approval of an organization's activities doesn't establish that the organization is lessening the burdens of government.

Rev. Rul. 85-2 sets forth two requirements for an organization to qualify for exemption under IRC section 501(c)(3) by lessening the burdens of government. These requirements are:

- 1) An organization's activities must be activities that a governmental unit considers to be its burdens, **and**
- 2) The activities of the organization must actually lessen such governmental burdens.

Analysis:

Issue: Is an organization tax-exempt under IRC § 501(c)(3) because it is lessening the burdens of government?

The organization has the burden of proof to demonstrate that it lessens the burden of government.

Based on all the facts and circumstances, an organization must demonstrate that a governmental unit considers the organization to be acting on the government's behalf. "Acting on the government's behalf" means the activities of the organization free up governmental assets (such as human, material or fiscal) that would otherwise have to be devoted to that activity if carried out by the governmental unit itself.

Refer to Rev. Ruls. 85-1 and 85-2 for the following relevant factors:

- 1) Identify activities that constitute the burdens of government.
- 2) Determine under what conditions an organization's activities actually lessen such burdens.

In the Columbia Park case, the petitioner provided a wide range of services and facilities to the residents of a large private real estate development. Petitioner argued that its activities lessened the burdens of government because the local or state government would have to provide these services if petitioner did not. The Tax Court rejected the petitioner's argument, and said that the organization had to demonstrate that the government accepted the activities conducted by the petitioner as its responsibility and recognized petitioner as acting on its behalf. In addition, the organization had to establish that its activities actually lessened the burden of the state or local government.

Even if you conclude that an organization is charitable because it does lessen the burdens of government, remember that it must also satisfy the other requirements of IRC § 501(c)(3), including that it not serve private interests more than incidentally. In Quality Auditing, the organization was formed to audit structural steel fabricators pursuant to its own certification program. The Court held that even if it concluded that the organization lessened the burdens of government, it would not be exempt because it was operated for the benefit of private interests of the steel industry. In the Indiana Crop case, the Court concluded that the

organization lessened the burdens of government, and also rejected an argument made by the Commissioner that the organization more than incidentally served the interests of commercial seed producers and commercial farmers.

Issue Indicators or Audit Tips:

As with any facts and circumstances test, cases will arise in which the correct conclusion is unclear. In that situation focus on:

- the statute creating or authorizing the organization
- the control exerted by governmental units over the organization's activities
- the interrelationship between the governmental unit and the organization
- the organization's funding
- whether the organization's activities defray general or specific expenses of the governmental unit
- whether the governmental unit has previously engaged in the same activity prior to the organization taking over such activity
- whether the activity is one which the governmental unit may, under state or local law, conduct itself
- In addition, other facts and circumstances may be relevant and should be considered.

Once the relevant facts are ascertained, weigh the facts and determine whether the organization has made the requisite showing of an objective manifestation by a governmental unit that the organization's activities constitute a burden of government, and that the activities actually lessen such burden.

Remember to also check for the other 501(c)(3) organizational/operational considerations

- Organizational Test (Purpose Clause; Dissolution Clause)
- Private Benefit/Inurement
- Unrelated Business Activity
- Commercial Purpose

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