

INTERNAL REVENUE SERVICE
District Director

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Dear Sir or Madam:

This letter responds to your request for information concerning your federal income tax status.

No provision of the Internal Revenue Code imposes a tax on the income of governmental units (such as states and their political subdivisions). It has, therefore, long been the position of the Service that income of governmental units is not generally subject to federal income tax. If, however, an entity is not itself a governmental unit (or an "integral part" thereof) its income will be subject to tax unless an exclusion or exemption applies.

One such exclusion is provided by section 115(1) of the Code, which excludes from gross income, (a) income derived from the exercise of any essential governmental function, and (b) income accruing to a state or political subdivision.

Your income may not be subject to tax, either because you are a governmental unit (or an "integral part", thereof) or because your income is excluded under section 115. In addition, you may also be eligible to receive charitable contributions which are deductible for federal income, estate, and gift tax purposes, and you are probably exempt from many federal excise taxes.

You may obtain a letter ruling on your status under section 115 following the procedures specified in Rev. Proc. 94-1, 1994-1 I.R.B. 10, or its successor (the first Revenue Procedure published each year). You must also pay a user fee as described in Rev. Proc. 94-1.

You may also qualify for exemption from federal income tax as an organization described in section 501(c)(3) of the Code. If you are an entity separate from the state, county, or municipal government, and you do not have powers to tax or to exercise enforcement or regulatory powers, you would qualify under section 501(c)(3). To apply for exemption, you would need to complete Form 1023 and pay the required user fee.

Sometimes governmental units are asked to provide proof of their status as part of a grant application. If you are applying for a grant from a private foundation, it may be requesting certain information from you because of the restrictions imposed by the Code on such foundations. One such restriction imposes a tax on private foundations that make any "taxable expenditures". Under section 4945(d) and (h) of the Code, "taxable expenditures" include (1) any grant to an organization (unless excepted), unless the foundation exercises "expenditure responsibility" with respect to the grant; and, (2) any expenditure for non-charitable purposes. Under section 4942 of the Code, private foundations must also distribute certain amounts for charitable purposes each year--"qualifying distributions" include certain amounts paid to accomplish charitable purposes.

Private foundation grants to governmental units for public or charitable purposes are not taxable expenditures under these provisions, regardless of whether the foundation exercises "expenditure responsibility". Under section 53.4945-5(a)(4)(ii) of the Foundation and Similar Excise Tax Regulations, expenditure responsibility is not required for grants for charitable purposes to governmental units (as defined in section 170(c)(1) of the Code). Similarly, grants to governmental units for public purposes are "qualifying distributions" under section 53.4942(a)-3(a) of the regulations and, if they are for charitable purposes, will not be taxable expenditures under section 53.4945-6(a) of the regulations. Most grants to governmental units will qualify as being for charitable (as well as public) purposes.

Because of these restrictions, some private foundations require grant applicants to submit a letter from the Service determining them to be exempt under section 501(c)(3) and classified as a non-private foundation. Such a letter, or an underlying requirement that a grantee be a public charity, is not legally required for an organization to be relieved from the restrictions described above, when the prospective grantee is a governmental unit and the grant is for qualifying (public or charitable) purposes.

We believe this general information will be of assistance to you. This letter, however, is not a ruling and may not be relied on as such. If you have any questions, please feel free to contact the person whose name and telephone number are listed in the heading of this letter.

Sincerely,



B. Grout, #75-13540
EO Quality Review