

Tax Law Change Needed To Protect Electric Co-op Tax-Exempt Status

Key Findings

- Recent changes to the Internal Revenue Code created an unintended consequence for rural electric cooperatives. Government grants are now considered non-member income.
- As community-focused, member organizations, electric cooperatives must comply with the 85 percent-15 percent income test. No more than 15 percent of gross income may come from non-member sources.
- Congress should take action to amend Section 501(c)(12) to retain the tax-exempt status of nearly 900 rural electric co-ops. This will allow the full use of federal, state or local grants to benefit their members.

Most of America's electric cooperatives are tax exempt organizations under Internal Revenue Code (IRC) Section 501(c)(12). In order to maintain tax exempt status, an electric cooperative must receive at least 85 percent of all income from its members. P.L. 115-97 amended Section 118 of the IRC to provide that contributions to a corporation by a non-shareholder government entity or civic group is no longer considered capital. Under prior tax law, such contributions were capital and excluded from the income of a corporation.

If a government grant or reimbursement is not a capital contribution, then the grant may be considered non-member income and could jeopardize a cooperative's tax-exempt status. This would have a profound impact on the cooperative and its member-consumers. Historically, electric cooperatives have received grants from a variety of federal, state and local governments to assist in providing services to their members for purposes such as renewable energy development, energy efficiency and conservation, economic development, storm restoration or rural broadband initiatives.

Current Tax Law Could Jeopardize Storm Recovery Efforts

Electric cooperatives belong to the communities they serve and operate at cost. The treatment of government grants as income may impair their ability to use the full value of the grant to benefit their members. Moreover, it means that an electric cooperative struck by disaster may have to consider whether it can afford to use FEMA's Public Assistance Program to help restore power to its community. In essence, co-ops could be forced to choose between maintaining their tax-exempt status or accepting FEMA assistance when recovering from a major storm or other disaster.

Congress must act now to correct this unintended consequence and protect the tax status of electric co-ops. In doing so, Congress would preserve the full value of government grants that deliver societal benefits to the communities served by electric cooperatives, many of which are located in persistent poverty counties.

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