

G. VOLUNTEER FIREFIGHTERS' RELIEF ORGANIZATIONS

A Second Look

by

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"Volunteer firefighters evoke Norman Rockwell images of smalltown camaraderie, and a 1993 study estimated that they save American communities \$36.8 billion a year. But despite national recruitment efforts and the modest new perks, their time may be slowly passing."

The Washington Post, Sunday, January 10, 1999, pg. A-1.

1. Overview

Many of us pay little attention to our local volunteer fire departments. We have no regular contact other than occasionally being inconvenienced by the siren of an emergency vehicle and the once a year solicitation for donations. Even this no longer arrives in the form of a fireman going door-to-door for donations but as an impersonal envelope mailed to every address in the service area. The fire department and other rescue services exist only on the periphery of our consciences unless or until we need their services. Will they be there when we need them?

This is a question currently being explored in many communities. According to the article in the Washington Post, cited above, today's modern living arrangements may be the death knell for traditional volunteer emergency services. The increasing suburbanization of America leaves mostly empty bedroom communities during the day. Our frenetic lifestyle, involving long commutes and little leisure time, has eaten into the supply of willing volunteers.

The cost of a career fire department, however, is substantial and may require a tax increase or reallocation of scarce funds. Communities wishing to defray such an expense are seriously looking at other options. Some fire departments have hired a few full-time firefighters to work alongside the volunteers. Many state and local governments are creating and funding benefits, from cash stipends to pension funds, as incentives to keep the volunteer force alive. Volunteer firefighters' relief organizations, last addressed in the 1996 CPE text, p. 349 - 364, are a popular first line of defense. Since 1996, we have seen growth in both the benefits being provided and the number of states providing benefits. With the number of relief organizations growing, this is a good time to take a second look at exemption issues.

2. The Road to Exemption

A. IRC 501(c)(3) & 501(c)(4)

The general rule is that mutual self-help organizations serve the private purpose of benefitting members and do not qualify for tax exemption under IRC 501(c)(3) or 501(c)(4). Rev. Rul. 81-58, 1981-1 C.B. 331, in discussing why an association of municipal police officers providing retirement and death benefits to its members failed to qualify for exemption under IRC 501(c)(4), explains that because the benefits are limited to members, the overall community benefit is merely incidental. This was the position taken by the court in Police Benevolent Association of Richmond, (PBA) v. U.S., 661 F. Supp. 765, (E.D.Va. 1987). The PBA argued that providing supplemental benefits to raise morale and retain officers lessened the burdens of government by reducing turnover in the police force and reducing the need to recruit and train new officers. Although the court acknowledged the government's legitimate concern in retaining public service employees, it held that providing such benefits on a voluntary basis, without the involvement of a governmental unit, to members of the organization primarily serves the private interests of the members. PBA did not qualify for exemption under IRC 501(c)(3) or 501(c)(4) because the private benefit received by the members in the form of supplemental pensions served a private rather than a public purpose.

Both Rev. Rul. 81-58 and Police Benevolent Association of Richmond involved organizations providing supplemental benefits to police departments made up of paid civil servants. Rev. Rul. 87-126, 1987-2 C.B. 150, involved a relief association paying pensions to paid firefighters. The organization differed from those the Service considered earlier in that it was not voluntary. Its funding, financing, and eligibility requirements were governed by a state law. Membership was mandatory and automatic. The state, when faced with low morale and increasing turnover of public service employees, found a way to offer the additional incentive of pension supplements to paid firefighters initially offered in the PBA case. And the Service, applying the analysis for determining if an organization is "relieving the burdens of government" in Rev. Ruls. 85-1, 1985-1 C.B. 177 and 85-2, 1985-1 C.B. 178, concluded that this relief association met the test.

Faced with similar pressures in the volunteer sector, many states have adopted statutory schemes to establish and fund a host of benefits to encourage membership and reduce turnover in volunteer fire departments. The usual method for funding the relief organizations is a 2 percent tax on foreign insurance premiums. The state law governs distribution of the funding, sets the mandatory and automatic eligibility requirements, and specifies the purposes for which the funds may be used. In 1996, we analyzed the Minnesota and Pennsylvania statutes. Statutes in other states, including New York, New Jersey, Florida, and Arkansas, to name just the few that we have seen, follow a similar theme. Close attention must be paid to the benefits permitted under the statute and to the interrelationship between the relief association and the local government. If the statutory

framework exists, and the relief association operates within it, then the organization is "lessening the burdens of government," an exempt purpose under IRC 501(c)(3) and an exempt activity under IRC 501(c)(4).

B. Other Issues to Consider

i. General Fund/Restricted Fund

In determining qualification for tax exemption for many firefighters' relief associations, determining that the restricted fund relieves the burdens of government does not end the inquiry. Many organizations also have a general fund that is not funded and controlled by the state. The general fund is supported primarily by member dues and contributions. The funds are often used to purchase supplies, provide training, and otherwise assist the fire department in doing its job. In some cases, however, general funds are used to provide additional supplemental benefits to the members. These benefits must be considered when analyzing tax exemption.

The type of benefits we have seen most often include vision services, dental services, and payment of deductible amounts under a health insurance policy. Some relief associations also supplement the pensions provided under the state statute. These are personal and private benefits identical in nature to the pension benefits offered in Police Benevolent Association of Richmond, supra. These benefits, whether in conjunction with the state supported benefits described above or standing alone, jeopardize exemption under IRC 501(c)(3).

In evaluating a relief association's qualification for exemption under IRC 501(c)(4), any benefits paid out of the general fund must be considered. In some older associations, the general fund may be the larger fund and benefits paid out of it may dwarf the activity of the restricted fund. The payment of these benefits may, in fact, be the organization's primary activity. A thorough facts and circumstances analysis must be conducted to determine the nature and extent of this activity. A determination that the payment of personal benefits is the primary activity of the association will preclude exemption under IRC 501(c)(4).

ii. IRC 501(m) -- "Commercial-Type Insurance"

The 1996 CPE raised a question as to whether the pensions provided for under many state statutes were similar to life insurance benefits and might be subject to IRC 501(m). The benefits we were concerned with are similar to those provided by the organization described in Rev. Rul. 87-126, supra, which was published after IRC 501(m)'s enactment. The IRS has no current plans to revoke Rev. Rul. 87-126, and has decided not to raise IRC 501(m) as a bar to exemption in the volunteer firefighters' relief association context.

It is no longer necessary to refer applications presenting this issue to Headquarters. The Internal Revenue Manual has been amended to remove this as a reserved issue.

iii. Charitable Gaming

In states where charitable gaming is legal, some firefighters' relief organizations have an additional restricted fund for gaming proceeds. The 1996 CPE discussed this issue with particular mention of the sale of state regulated pull-tabs. In considering whether a fire relief association is described in IRC 501(c)(3) or 501(c)(4), it is necessary to consider the effect of this activity.

The sale of pull-tabs is ordinarily unrelated trade or business. Because it is labor intensive, analysis of the facts and circumstances may show that gaming is a relief association's primary activity. If so, exemption under IRC 501(c)(4) is inappropriate.

"Relieving the burdens of government," however, is a basis for exemption under both IRC 501(c)(4) and 501(c)(3). Because IRC 501(c)(3) applies a "purpose" test rather than an "activity" test, the conduct of an extensive unrelated trade or business will not usually jeopardize exemption. If appropriate, an association should be permitted to amend its organizational documents to satisfy the organizational test under IRC 501(c)(3) and submit Form 1023. If the facts do not show any private benefit or inurement from the conduct of this activity, a firefighter relief organization with substantial unrelated business income will qualify for exemption under IRC 501(c)(3).

One issue mentioned in the 1996 CPE that should raise a red flag is the use of funds from the gaming account, as well as the general fund, to supplement relief benefits paid from the restricted account. This kind of private benefit is inconsistent with exemption under IRC 501(c)(3). Exemption under IRC 501(c)(4) may be precluded because of the extensiveness of the unrelated business activity. Under these circumstances, exemption must be denied and the organization treated as a mutual self-help organization serving the private purpose of benefiting its members. See, Police Benevolent Association of Richmond, *supra*.

As of January 1, 1997, applications from organizations conducting gaming activities were no longer reserved for National Headquarters review.

3. Conclusions

Because of the increasing pressure on the volunteer sector, the growth of state supported incentives being administered by volunteer firefighters' associations through the use of restricted funds has been remarkable. Many of these organizations will qualify for exemption under IRC 501(c)(3) or 501(c)(4) because they are "relieving the burdens of government" by implementing the provisions of the state statutes. Some associations will, however, continue to be taxable because of the payment of member-supported mutual benefits.

Relief associations failing to qualify for exemption under IRC 501(c)(3) or 501(c)(4) may wish to consider the other routes to exemption described in 1996 CPE 362.