

An organization otherwise exempt from Federal income tax under section 501(a) of the Internal Revenue Code of 1954 as an agricultural organization described in section 501(c)(5) thereof, is subject to tax under section 511 of the Code on the unrelated business income resulting from services rendered to certain insurance companies and from the performance of property management services.

Advice has been requested whether an organization, exempt from Federal income tax as an agricultural organization described in section 501(c)(5) of the Internal Revenue Code of 1954, is taxable under section 511 of the Code on income received from services rendered to certain insurance companies and from property management services, under the circumstances set forth below.

The instant organization was formed for the advancement and improvement of agriculture. It was granted exemption from Federal income tax under section 501(a) of the Code as an agricultural organization described in section 501(c)(5) thereof.

In addition to its usual activities in the furtherance of agriculture, it conducts educational programs and organizational work for the purpose of promoting wider insurance coverage among its members and other local farmers. The insurance programs include life, casualty and fire insurance.

A part of the organization's administrative and secretarial staff is assigned to such work. Insurance policies are written for the benefit of the several insurance companies cooperating in the program. The organization does not represent insurance companies as agent in connection with the promotion of insurance programs, nor does it receive a direct commission for services performed in that connection. However, it does receive an over-all fee from the insurance companies for office and other services rendered them in connection with its insurance programs.

Under a property management contract, the organization also manages an office building for one of the insurance companies participating in its farm insurance program. The contract provides for the payment to the life insurance company of a specified percentage of its investment in the building. The balance of the rentals, less expenses, are retained by the organization as its operating profit.

Section 511(a) of the Code imposes a tax on the unrelated business taxable income of certain organizations, including agricultural organizations, which are otherwise exempt from tax under section 501(a) of the Code.

Section 1.513-1 of the Income Tax Regulations provides, in part, that the income of an exempt organization is subject to tax on unrelated business income only if two conditions are present

with respect to such income. The first condition is that the income must be from a trade or business regularly carried on by the organization. The second condition is that the trade or business must not be substantially related (aside from the need of the organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable or other purpose or function constituting the basis for its exemption from tax.

The regulations further provide that a trade or business is regularly carried on when the activity is conducted with sufficient consistency to indicate a continuing purpose of the organization to derive some of its income from such activity. Ordinarily, a trade or business is substantially related to the activities for which an organization is granted exemption if the principal purpose of such trade or business is to further, other than through the production of income, the purpose for which the organization was granted exemption.

Services of the type herein considered rendered in connection with insurance programs and property management are activities which constitute businesses of a kind ordinarily carried on for profit. Such activities are not usually associated with the functions of an agricultural organization and normally would not be carried on by such an organization in the furtherance of its exempt purposes. Therefore, these activities are not related to the organization's exempt purposes other than through the use it makes of the net earnings received therefrom.

It is concluded, therefore that such activities constitute unrelated trades or businesses within the meaning of section 513 of the Code. Accordingly, it is held that the instant organization is subject to the tax under section 511 of the Code on the unrelated business taxable income, as defined in section 512(a) of the Code, which it derives from services rendered in connection with the insurance programs and from the performance of property management services.