



Department of the Treasury
Internal Revenue Service
Tax Exempt and Government Entities Division

Date:
December 23, 2013
Taxpayer identification number:

Form:

Tax year(s) ended:

Number: **201502015**
Release Date: 1/9/2015

Person to contact / ID number:

Contact numbers:

Telephone:

Fax:

Manager's name / ID number:

Manager's contact number:

UIL: 501.06-00

Response due date:

Certified Mail - Return Receipt Requested

Dear _____ :

Why you are receiving this letter

Enclosed is a copy of our report of examination explaining why revocation of your organization's tax-exempt status is necessary.

What you need to do if you agree

If you agree with our findings, please sign the enclosed Form 6018-A, *Consent to Proposed Action*, and return it to the contact at the address listed above. We'll send you a final letter revoking your exempt status.

If we don't hear from you

If we don't hear from you within 30 calendar days from the date of this letter, we'll process your case based on the recommendations shown in the report of examination and this letter will become final.

Effects of revocation

In the event of revocation, you'll be required to file federal income tax returns for the tax year(s) shown above. File these returns with the contact at the address listed above within 30 calendar days from the date of this letter, unless a request for an extension of time is granted. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

What you need to do if you disagree with our findings

If you disagree with our position, you may request a meeting or telephone conference with the supervisor of the contact identified in the heading of this letter. You also may file a protest with the IRS Appeals office by submitting a written request to the contact person at the address listed above within 30 calendar days from the date of this letter. The Appeals office is independent of the Exempt Organizations division and resolves most disputes informally.

For your protest to be valid, it must contain certain specific information, including a statement of the facts, the applicable law and arguments in support of your position. For specific information needed for a valid protest, please refer to page one of the enclosed Publication 892, *How to Appeal an IRS Decision on Tax-Exempt Status*, and page six of the enclosed Publication 3498, *The Examination Process*. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process. Please note that Fast Track Mediation referred to in Publication 3498 generally doesn't apply after we issue this letter.

If you and Appeals don't agree on some or all of the issues after your Appeals conference, or if you don't request an Appeals conference, you may file suit in United States Tax Court, the United States Court of Federal Claims, or United States District Court after satisfying procedural and jurisdictional requirements.

You may also request that we refer this matter for technical advice as explained in Publication 892. Please contact the person identified in the heading of this letter if you're considering requesting technical advice. If we send a determination letter to you based on a technical advice memorandum issued by the Exempt Organizations Rulings and Agreements office, then no further IRS administrative appeal will be available to you.

Contacting the Taxpayer Advocate Office is a taxpayer right

You have the right to contact the office of the Taxpayer Advocate Service (TAS). **TAS is your voice at the IRS. This service helps taxpayers whose problems with the IRS are causing financial difficulties; who have tried but haven't been able to resolve their problems with the IRS; and those who believe an IRS system or procedure is not working as it should. If you believe you are eligible for TAS assistance, you can call the toll-free number 1-877-777-4778 or TTY/TDD 1-800-829-4059. For more information, go to www.irs.gov/advocate.** If you prefer, you may contact your local Taxpayer Advocate at:

Internal Revenue Service
Office of the Taxpayer Advocate

For additional information

If you have any questions, please call the contact at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Nanette Downing
Director, EO Examinations

Enclosures:
Report of Examination
Form 6018-A
Publication 892
Publication 3498

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No.
		Year Ended December 31, 20XX

Issue

Whether the Internal Revenue Codes §501(c)(6) status of the organization should be retroactively revoked to January 1, 20XX based on the facts presented.

Facts

Current status of the Organization

In 20XX, the sole owner of (company) took over and business, in were closed as of August 31, 20XX, as a result of death on May 31, 20XX. has no office. It still had a website as of December 18, 20XX.

History of the Organization

() filed its application for exemption (Form 1024) with the Internal Revenue Service (IRS) on or about April 26, 19XX and received its 501(c)(6) exempt status in August 5, 19XX.

By determination letter issued August 5, 19XX, was recognized by the Internal Revenue Service (IRS) as a tax-exempt organization described in § 501(c)(6). After that date, changed its name to (). In 20XX, changed its name to () and later changed it back to . The articles of incorporation of were accepted by the on November 24, 19XX.

Article three of its Articles of Incorporation stated that was organized for the following purposes:

A. To promote the development and growth of the life sciences, biotechnology, computer sciences, telecommunications and related technologies in the . For the purposes of these Articles, the “ ”, shall mean

B. To promote the common business interest of in the

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C. To monitor state and federal legislation which may affect _____ located in the _____ and to advocate statutes, regulations and government policies which foster the growth and development of _____.

D. To improve business conditions for _____ in the _____.

The Form 1024 stated that _____ would spend approximately 0% of its time monitoring state and federal legislation affecting the industry, 0% of its time providing information on various topics of interest related to the industry via newsletters and seminars, and 0% of its time representing its members in negotiating special deals with providers of services commonly purchased by its members. In 19XX, annual membership fee was \$0.

One of the benefits offered by _____ to its members was group health insurance at a discounted rate. _____ members grew until 19XX, when the State of _____ passed legislation prohibiting employers who had 0 or less employees from accessing health insurance for their employees via a trade association group plan. One of the primary reasons for members to join _____ was seriously diluted because every member was forced to buy health insurance which was priced based solely on the company's demographics and the member could not participate in _____ large group association pool. By 19XX, because of this legislation, membership in _____ dwindled to the point that all the other packaged benefits could not be supported due to the inability to maintain the critical mass for the primary member benefit offerings. Attempts were made by _____ to create new offerings.

In 20XX, _____ () (a trade association with like member profiles) partnered with _____ to have a group benefits program offered to its members, even though there was no pricing advantage. The purpose for this partnering was to expand member offerings. The initiative had fits and starts due to staff turnover, loss of leadership and continuing coordination with _____. By 20XX the participation in the offerings did not allow for continuation of the program.

In 20XX _____, the sole owner of _____ (company) offered to take over _____. The company only sold life insurance products and did not sell annuities or mutual funds. The company was also involved in marketing Section 419 plans, also known as Insured Security Plans (ISP), Section 419 Severance Pay Plans (SPP) and a plan offered by _____.

¹ _____ had a royalty agreement with _____. The ISP plan was also known as the _____. As of October 17, 20XX, the ISP plan was terminated and it ceased to be marketed, (after _____ became aware of Notice 2007-83 and that this plan was considered a listed transaction).

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held licenses that covered the sale of fixed and variable life insurance and annuities.
 was also the owner of a company known as

The administration, operation and bank accounts of were transferred to . However, was advised by counsel to keep the same corporate name rather than incorporate a new entity in , since was formed in . In order to keep a corporate presence in , one of the board members, , who lived in , agreed to stay on the board of directors and maintain the corporate office in . The administration of was handled in , but mail was received and handled in . The bank accounts of were in

board meetings were held regularly. board of director attended by phone and was the host and they discussed membership initiatives, business exit planning, and merger advice. had a tax and legal newsletter. The minutes were kept by , since he was the Secretary.

Between October 17, 20XX and December 31, 20XX, established the “ ” (“ ”). The was also marketed under other names including the following:

used the life insurance plans as a magnet to obtain membership. In 20XX, had approximately 0 member employers. Of the 100 member employers, for which partial information was available, over 85% were located outside of the area. Numerous employers participating in the were interviewed by the IRS and questioned concerning the value of their membership. Most replied that the only value of their membership was access to the

The main purpose of became the offering of to its members. provided other nominal benefits in the form of newsletters and two books. However, all of these benefits of membership were available through other sources at much less cost.

During the examination of the books and records, a copy of a adoption agreement was reviewed. The agreement indicated that (called the in the adoption agreement) obtained an interest in the term life insurance policies insuring the lives of the eligible plan participants who applied for and obtained life insurance. The agreement required the employer to have each eligible participant execute a co-ownership agreement and an assignment of policy for collateral security which related to the interest in the life insurance policies which were used as a funding source for

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plan death benefits. The plan only provided death benefits through the . The co-ownership agreement indicated that the total premium, referred to as the "planned annual premium" paid on any particular employee owned policy consisted of the annual premium, a policy owner's annual premium, and the participation premium.

The adoption agreement defined the term assignment of policy for security to mean grants to the of an interest in a policy and policy proceeds as security for payment to the of the total death benefit. In the event of the death of an employee, the insurer would pay the benefit to the , which in turn would pay the benefit to the employee's beneficiary.

The adoption agreement defined the term co-owner as the to the extent of its interest identified in the co-ownership agreement, which was defined to mean that with respect to the insured death benefit, an agreement between the policy owner and the (at the direction of the contract administrator), whereby the two parties agreed to define and limit the extent of the assigned interest in the policy and the policy proceeds.

The employer made "contributions" to which was used primarily as premium payments on one or more insurance policies issued by an insurer. The adoption agreement provided that the contributions were intended to meet the "deductibility limits of Section 79 of the Code." The adoption agreement provided that the contributions to the were made solely for the purpose of funding the benefits provided and that the employer and the plan participants did not have any rights, title or interest in the contributions. It also provided that the would have no liability to pay any plan participant, beneficiary or payee with respect to any shortfall in benefits provided.

filed its first Form 990 for the 20XX year on or about September 25, 20XX.
received substantial commissions from its insurance activities.

The Form 990 for the 20XX year used a address. This return indicated that was doing business as " ," which had a separate EIN. In Parts I and III of the 20XX Form 990, stated that it had the following mission: "To promote the closely held business as a favorable structure to conduct business in the United States. The goal is to improve the business conditions of the member companies through its specific activities." Part III, 4a of the 20XX Form 990 stated the following:

The is a forum for the exchange of information that will improve the profitability and longevity of a business and improve conditions in each line of business represented by members. The retains a tax attorney/lobbyist to monitor and report monthly in a members' newsletter titled " ' on federal legislation that could affect the fringe benefits and business conditions of the industries represented by the members. This activity is important

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because under current law, a closely held business can offer tax advantaged benefits to the owners that the owners could not obtain as individuals. In addition, the provides material for the members to educate them on planning for business continuation, business valuation issues and business exit planning strategies. All of this material is designed to strengthen the viability of the business and hence the overall strength of the members' industry. A close-held business is exempt from significant government reporting required of public companies. Companies that are private do not have to worry about meeting expectations from Wall Street every quarter and can concentrate on long-term goals. The , through its various activities, promote these advantages to its members et al.

The information in the following table was taken from filed Forms 990 for the tax years 20XX through 20XX. The 20XX and 20XX tax years were not audited but is shown for comparative purposes only.

Revenue Description	20XX	20XX	20XX
Contributions	-0-	-0-	\$0
Program Service	\$0	\$0	-0-
Other revenue	\$0	\$0	\$0
Total Revenue	\$0	\$0	\$0

During the year of examination, 20XX, the organization did not receive any program service revenue; due to the discontinuation of activities. The 20XX Form 990 indicated that the organization had no contributions or program revenue in the prior year (20XX) and that it received \$0 in program revenue in 20XX. Per the tax preparer, no membership fees were reported in any tax year. Part VIII, response to question #2 stated that the \$0 in program revenue was received from insurance commissions. The response to question #34 in Part IV stated that the organization was not related to any tax-exempt or taxable entity. The responses to questions #3a and 5a stated that the organization did not have any unrelated business gross income of \$1,000 or more and that it was not a party to a prohibited tax shelter transaction. signed this return as the Secretary of and Part VI, question #20 indicated that possessed all the books and records of

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The Form 8868, *Application for Extension of Time to File an Exempt organization Return*, stated that the delay in filing the return was due to the “ .” The extension request was executed by .

The origins of the funds reported on Form 990 for 20XX were insurance commissions collected by . However Form 990 for 20XX, filed on or about January 5, 20XX, indicated “program revenue” of only \$0 . The 20XX Form 990 indicated that this program revenue was from insurance commissions. Like the 20XX Form 990, this return used a address and it was signed by as the secretary of . The last Form 990 filed by was for the 20XX year.

The website of , as it existed on December 18, 20XX, stated that had the following purpose:

The purpose of the of (“ ”) is to promote the closely held business as a favorable structure to conduct business in the United States. The goal is to improve the business conditions of the industries of the member companies through its specific activities.

The is a forum for exchange of information that will improve the profitability and longevity of a business and improve conditions in each line of business represented by the members.

The retains a tax attorney/lobbyist to monitor and report monthly in a members’ newsletter titled “ ” on federal legislation that could affect the fringe benefits and business conditions of the industries represented by the members. This activity is important because under current law, a closely held business can offer tax advantaged benefits to the owners that the owners could not obtain as individuals.

In addition, the provides material for members to educate them on planning for business continuation, business valuation issues and business exit planning strategies. All this material is designed to strengthen the viability of the business and hence the overall strength of the members’ industry.

A closely-held business is exempt from significant government reporting required of public companies. Companies that are private don’t have to worry about meeting expectations from Wall Street every quarter and can concentrate on long-term goals.

The , through its various activities, will promote these advantages to its

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members and others.

The website indicated that these purposes would be accomplished through education.

The third paragraph of the Internal Revenue Service original determination letter reads as follows:

“If your sources of support, or your purposes, character, or method of operation change, please let us know so we can consider the effect of the change on your exempt status. In the case of an amendment to your organizational documents or bylaws, please send us a copy of the amended document or bylaws. Also, you should inform us of all changes in your name or address.”

_____ did not notify the IRS of the changes that he made in _____ purposes, character and method of operation. The IRS was never provided with amended articles of incorporation or amended bylaws. _____ did not file a separate application for exemption.

LAW

The Internal Revenue Code § 501(c)(6) provides that certain organizations are exempt from paying federal income taxes. Those organizations include:

Business leagues, chambers of commerce, real-estate boards, boards of trade, or professional football leagues (whether or not administering a pension fund for football players), not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Treas. Regulations § 1.501(c)(6)-1 defines a business league as follows:

A business league is an association of persons having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried on for profit. It is an organization of the same general class as a chamber of commerce or board of trade. Thus, its activities should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons. An organization, whose purpose is to engage in a regular business of a kind ordinarily carried on for profit, even though the business is conducted on a cooperative basis or produces only sufficient income to be self-sustaining, is not a business league. An association engaged in furnishing information to prospective investors, to enable them to make sound investments, is not a business league, since its activities do not

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further any common business interest, even though all of its income is devoted to the purpose stated. . . .

Based on the above quoted regulation, a business league has the following characteristics:

- (1) an organization of persons having a common business interest;
- (2) whose purpose is to promote the common business interest;
- (3) not organized for profit;
- (4) that does not engage in a regular business of a kind ordinarily conducted for profit;
- (5) whose activities are directed to the improvement of business conditions at one or more lines of a business as distinguished from the performance of particular services for individual persons; and
- (6) of the same general class as a chamber of commerce or a board of trade.

The regulation also states that an association engaged in furnishing information to prospective investors, to enable them to make sound investments, is not a business league, since its activities do not further any common business interest, even though all of its income is devoted to the purpose stated.

In order to qualify for a business league classification, each and every requirement of § 1.501(c)(6) must be met. Failure to meet one of the six requirements results in the organization not being qualified under § 501 (c)(6). The Engineers Club of San Francisco v. United States, 791 F.2d 686 (9th Cir. 1986); North Carolina Association of Insurance Agents, Inc. v. United States, 739 F.2d 949 (4th Cir. 1984); ABA Retirement Funds v. United States, 2013 WL 1788297, 111 AFTR2d 2013-1815, 2013 U.S. Dist. Lexis 60086 (N.D. Ill. 2013)

In The Engineers Club of San Francisco, *supra*, the court stated that the Club's performance of particular services (chiefly food and beverage service) for its members distinguished it from a board of trade or chamber of commerce. Prominent among the characteristics of boards of trade and chambers of commerce is the emphasis on improving trade and commerce by activities which serve business people and members of the community in common, not individually. One key characteristic of a business league is that it also provides a benefit to non-members.

In ABA Retirement Funds v. United States, *supra*, the Court granted the IRS summary judgment and held that the ABA Retirement Funds (ABRA) did not qualify as a business league under § 501(c)(6). The ABRA was incorporated by the American Bar Association (ABA) for the purpose of promoting and facilitating the operation and use of tax-qualified retirement plans for members of the ABA and their employees. ABRA had the authority under the qualified retirement plans to engage, monitor, and replace vendors and it was responsible for the design and maintenance of the plan documents. It also obtained tax qualifications for the plans. The plans paid ABRA a fee based on the total percentage of

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total assets invested. The court held that ABRA failed the following tests: (1) its activities were not directed to the improvement of a line of business, instead it was providing services for individuals. A business league must not only improve the conditions of a line of businesses but must do so in a way different from simply supplying products or services to its individual members; (2) its activities failed to promote a common business interest; (3) it was engaged in a regular business of a kind ordinarily conducted for profit. The fact that the ABRA contracted with a third party vendor to perform certain administrative services for the plans did not change the conclusion that ABRA was engaged in a trade or business.

As an additional ground for denying the exemption, the court stated that the organization was not exempt under § 501(c)(6) because it provided information to enable prospective investors to make sound investments. The court stated that this prohibition covered a substantially broader range of activities than providing specific advice about particular investments. The activities of the ABRA violated this provision to the extent that it promoted, advertised or advised concerning the retirement plans. ABA Retirement Funds v. United States, *supra*.

In MIB, Inc. v. Commissioner, 734 F.2d 71(1st Cir, 1984), the court upheld the IRS' determination that MIB was not entitled to exempt status under § 501(c)(6) as a business league because it provided a particular service to its members. MIB's membership was basically open to all life insurance companies incorporated in the United States or Canada, and almost all companies in the United States were members. MIB responded to a member's request for information about a named applicant for insurance by transmitting whatever information that it had about that person to the requesting member. The main function of the information circulated by MIB was to "alert" members to possible omissions or misstatements in current applications. These services benefitted the businesses of the individual members. The court also stated that a major factor in determining whether services are "particular" is whether they are supported by fees and assessments in "approximate proportion to the benefits received." In the MIB case, over 91 % of MIB's total dues and assessments were related directly to MIB's principal activity, the information exchange. Of this amount, over half -- 47 % of total dues and assessments -- was received in direct exchange for information through service charges based upon the number of information requests processed.

In North Carolina Association of Insurance Agents, Inc. v. United States, *supra*, the Court held that the organization was not entitled to exempt status under § 501(c)(6) because when it acted as the state's insurance agent, it wrote policies in much the same way as any other insurance broker. It was engaged in a regular business of a kind ordinarily conducted for profit. The court also stated that the non-exempt business activities were not incidental to the organization's exempt activities because the activities generated between 95-98% of the organization's gross revenues and its administration of the state insurance program occupied approximately 60% its employees' time.

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In Rev. Rul. 81-175, 1981-1 C.B. 337. the organization was formed for the purpose of, and had as its sole activity, regularly engaging in the business of insurance as a reinsurer. Even though the organization's reinsurance business may not have created a profit, it was the nature of the activity that determined whether the activity is a business ordinarily carried on for profit. Since reinsurance is a business ordinarily carried on by commercial insurance companies for profit, the organization was not exempt under § 501(c)(6). See also Rev. Rul. 81-174, 1981-1 C.B. 335.

Rev Rul. 74-81, 1974-1 C.B. 135 stated that by providing group workmen's compensation insurance for its members, the organization relieved the members of obtaining this insurance on an individual basis, resulting in a convenience in the conduct of their businesses. Since the principal activity of the organization was rendering particular services for individual members as distinguished from the improvement of business conditions in the contracting and related industries generally, it was not entitled to exemption under § 501(c)(6).

Government's Position

The Internal Revenue Service has held for an organization to be exempt under §501(c)(6) the organization needs to be formed as a association of persons, including legal entities such as trusts and corporations, having a common business interest. Its purpose is to promote the common business interest and not to engage in a regular business if a kind ordinarily carried on for profit.

The regulations define a business league as an association of persons, including legal entities such as trusts and corporations, having a common business interest. Its purpose is to promote the common business interest and not to engage in a regular business of a kind ordinarily carried on for profit. Its activities are directed to the improvement of business conditions of one or more lines of business rather than the performance of particular services for individual persons.

- b. It must not be organized for profit. engaged in a regular business of a kind ordinarily conducted for profit. Selling life insurance is a "for profit" activity and realized substantial revenues from this activity.
- c. It must be a membership organization and have a meaningful extent of membership support. did not prove to be organized as a membership organization since realized substantial revenues from selling life insurance and failed to show any membership fees as a meaningful extent of membership support. There are no dues or membership fees reported on any filed Form 990.
- d. No part of its net earnings may inure to the benefit of any private shareholder or individual. The audit did reveal inurement for the benefit of the private shareholder/individual. An analysis of the bank records of for 20XX indicated that \$0 in checks were written to The origins

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of these funds were insurance commissions collected by . However Form 990 for 20XX, filed on or about January 5, 20XX, indicated "program service revenue" of only \$0. The 20XX Form 990 indicated that this program revenue was from insurance commissions. He used the organization as a marketing tool to sell his group term life insurance.

e. Activities must be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons. Performance of particular services by an organization for its members or others is not an IRC §501(c)(6) activity. While such activities, in and of themselves, do not preclude exemption, an organization whose primary activity is performing particular services is not exempt under IRC §501(c)(6). received contributions from its members (employer) which were used primarily as premium payments on one or more insurance policies issued by an insurer.

f. Its purpose must not be to engage in a regular business of a kind ordinarily carried on for profit, even if the business is operated on a cooperative basis or produces only sufficient income to be self-sustaining. Whether an organization's purpose is primarily to engage in business is thus a question of fact. An organization engaging in business activities is exempt under IRC 501(c)(6) only when it can be determined that such activities do not constitute its primary activity. Selling life insurance is "for profit" activity and realized substantial revenues from this activity.

g. It must be primarily engaged in activities or functions constituting the basis for exemption. Exemption was granted as a 501(c)(6) organization. does not meet the definition of an association of persons, including legal entities having a common business interest and not to engage in a regular business of a kind ordinarily carried on for profit. was providing life insurance products to its members, and received substantial commissions from selling life insurance policies. The organization's activities do not support the basis to be exempt as a 501(c)(6) organization, but rather performs a for profit/regular business.

h. Its primary activity cannot be performing particular services for members. was providing life insurance products to its members, as distinguished from the improvement of business conditions received substantial commissions from selling life insurance policies.

Based on the above, 's § 501(c)(6) exempt status should be revoked for the following reasons: (1) it was rendering particular services for individual members by providing life insurance products to its members, as distinguished from the improvement of business conditions; (2) it was engaged in a regular business of a kind ordinarily conducted for profit. Selling life insurance is a for profit activity and realized substantial revenues from this activity; (3) closely held corporations is not an industry or a line of business; and (4) to the extent that life insurance can be considered an investment, it was providing investment advice.

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Retroactive Revocation

Under § 7805(b)(8), the Commissioner has broad discretion to make retroactive determinations. See also §§601.201(l)(1); 601.201(l)(5); 601.201(n)(3)(ii).

Treas. Reg. § 1.501(a)-1(a)(2) provides that an organization that has been determined to be exempt under section 501(a) may rely upon such determination so long as there are no substantial changes in the organization's character, purposes, or methods of operation.

operated substantially differently from the representations made in application for exemption. The character, purposes, methods of funding and methods of operation of were substantially different from . Therefore, retroactive revocation is appropriate.

Taxpayer's Position

Unknown. , the former director, has passed away, and no one has stepped forward to take his place.

Conclusion

Based on the forgoing reasons, it is the Government's position that the organization no longer meets the requirements for exemption under Internal Revenue Code §501(c)(6) and Treasury Regulation 1.501(c)(6)-1. It is recommended that the exempt status of this organization be revoked as of January 1, 20XX.