

Internal Revenue Service

Department of the Treasury

Washington, DC 20224

199916053

Contact Person:

Telephone Number: U.I.L:  
501.06-00  
In Reference to: 513.00-00

Date: JAN 26 1999

Employer Identification Number:  
Key District:

Legend:

M =  
N =  
O =  
P =  
Q =  
R =

Dear Applicant:

This letter is in reply to the letter from your authorized representative dated July 29, 1998, in which M, N, O, P, Q, and R requested rulings with respect to the tax consequences of a proposed merger as described below.

M, N, O, P, and Q are organizations recognized by the Internal Revenue Service as exempt from federal income tax as business leagues under section 501(c)(6) of the Internal Revenue Code. R is an organization recently recognized by the Service as exempt from federal income tax as a business league under section 501(c)(6) of the Code.

A chamber of commerce in a particular area, along with local business leaders, decided that the then existing methods and practices for recruiting and bringing industry to the area were insufficient to develop the economic growth and base they desired. The method they developed to recruit industry to the area involved the creation of an entity that would qualify as an exempt organization under section 501(c)(6) of the Code. This entity would negotiate with the recruited industry to furnish it with facilities tailored to the recruited industry's needs. A lease agreement would be entered into upon favorable financial terms to the recruited industry.

Traditional financing from local banks would be the primary source of funding used by the organization exempt under section 501(c)(6) of the Code for its incentive packages to bring the recruited industry into the area, including the purchase of real

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estate and the building of plants and facilities. The local bank lending limits, however, did not allow for more than one substantive project. The solution was to create identical, but separate, section 501(c)(6) entities for different industrial recruitment projects, enabling full use of the bank lending limits. M, N, O, P, and Q were created for this reason.

M, N, O, P, and Q were each organized with an economic development vision to seek and establish an industrial park by offering an incentive package and creating a team for ongoing community development in the area. The boards of directors for M, N, O, P, and Q are identical, but each board acts separately and independently. Because of the bank lending limits, there existed a good business purpose for forming the organizations. Currently, however, the banks are no longer requiring the application of their lending limits. The practical problems and administrative costs associated with the numerous entities have led to a desire and a valid business purpose to consolidate all industrial recruitment for the area into one entity. In addition, the costs associated with having separate accounting and the filing of separate tax returns has become impractical and costly.

The organizations propose to alleviate the practical problems and artificial costs associated with M, N, O, P, and Q by creating R and consolidating the organizations into the new entity. M, N, O, P, and Q have all adopted plans of consolidation under state law.

Section 501(c)(6) of the Code provides for the exemption from federal income tax of business leagues, chambers of commerce, real-estate boards, or boards of trade, not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(c)(6)-1 of the Income Tax Regulations provides that 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.

Section 511(a) of the Code imposes a tax on the unrelated business taxable income of organizations described in section 501(c).

Section 512(a)(1) of the Code defines the term "unrelated business taxable income" as the gross income derived by any organization from any unrelated trade or business regularly carried on by it, less certain allowable deductions and modifications.

Section 513(a) of the Code defines the term "unrelated trade or business" as any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of the function constituting the basis of its exemption.

Section 1.513-1(d)(2) of the regulations provides that trade or business is "related" to exempt purposes, in the relevant sense, only where the conduct of the business activities has causal relationship to the achievement of exempt purposes; and it is "substantially related" only if the causal relationship is a substantial one. The regulation continues that for the conduct of trade or business from which a particular amount of gross income is derived to be substantially related to purposes for which exemption is granted, the production or distribution of the goods or the performance of the services from which the gross income is derived must contribute importantly to the accomplishment of those purposes.

Rev. Rul. 70-81, 1970-1 C.B. 131, holds that the acquisition, development, and sale of industrial sites in the manner described are conducted in a manner designed to attract industry to the community and is not an activity of a kind ordinarily carried on for profit. The revenue ruling concludes that the activity is in furtherance of the chamber's purpose of improving the general business conditions of the community, and accordingly, holds that the chamber's exemption from federal income tax under section 501(c)(6) of the Code is not adversely affected by engaging in this activity.

Subsequent to the proposed reorganization, R will carry on activities within the meaning of section 501(c)(6) of the Code. The transfers and movements described, in and of themselves, will have no adverse effect on a determination of exempt status. Further, the proposed merger of M, N, O, P, Q, and R does not involve the regular carrying on of unrelated trade or business within the meaning of section 513 of the Code.

Accordingly, based on the facts and circumstances concerning the reorganization and related transactions as stated above, we rule as follows:

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(1) The proposed consolidation of M, N, O, P, and Q into R does not create a taxable event for the organizations which would subject them to any federal income tax, including unrelated business income tax.

(2) The proposed consolidation of M, N, O, P, and Q into R does not effectuate a revocation of the tax exempt status of M, N, O, P, or Q prior to the termination of their separate existences.

(3) The proposed consolidation of M, N, O, P, and Q into R does not violate or otherwise jeopardize R's status as an organization described in section 501(c)(6) of the Code.

These rulings are based on the understanding that there will be no material changes in the facts upon which they are based. Any such change should be reported to the Ohio EP/EO key district office. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept in your permanent records. A copy of this ruling is being forwarded to the Ohio EP/EO key district office.

Except as we have specifically ruled herein, we express no opinion as to the consequences of these transactions under the cited provisions or under any other provisions of the Code.

This ruling is directed only to the organization that requested it. Section 6110(j)(3) of the Code provides that it may not be used or cited as precedent.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely yours,

(signed) Garland A. Carter

Garland A. Carter  
Chief, Exempt Organizations  
Technical Branch 2

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