

**Office of Chief Counsel
Internal Revenue Service
memorandum**

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subject: IRC 501(c)(6)¹ Organizations Providing Pension and Health Benefits

The purpose of this memorandum is to provide updated information on IRC 501(c)(6) business leagues that provide pension and health benefits to their members. This document may not be used or cited as precedent.

BACKGROUND

This memorandum addresses a 2012 private letter ruling (PLR), PLR 201246039, (the 2012 PLR)². The 2012 PLR was issued by the Internal Revenue Service (IRS) prior to a significant court case on the issue and does not reflect the current position of our office.

In the PLR, dated August 21, 2012, the IRS issued a favorable ruling to an IRC 501(c)(6) Business League that provided pension and health benefits to its eligible members.

¹ The Internal Revenue Code (Title 26 of the United States Code) is referenced herein as "IRC." Similarly, the Treasury Regulations (Title 26 of the Code of Federal Regulations) are referenced as "Reg." IRC 501(c)(6) provides for the exemption from Federal income taxation of business leagues, chambers of commerce, real-estate boards, boards of trade, or professional football leagues, not organized for profit and no part of the net earnings of which inure to the benefit of any private shareholder or individual. Specifically, this memorandum deals with business leagues.

² PLRs are not precedential and can only be relied upon by the taxpayer to whom the PLR was issued.

The 2012 PLR stated that: 1) providing pension and health benefits in the manner described will not result in private inurement as described in IRC 501(c)(6), and 2) providing the proposed benefits will not adversely affect the organization's IRC 501(c)(6) status. Although the 2012 PLR stated in its initial paragraph that the organization was also requesting ruling(s) with regard to unrelated business income tax (UBIT), the PLR did not issue a UBIT ruling and did not explain why one was not issued.

Based on our analysis, the 2012 PLR has been called into question because of the reasons cited in this memorandum, including a subsequent court case involving the provision of retirement benefits by an IRC 501(c)(6) organization to its members.

No opinion is expressed regarding the provision of pension and health benefits to employees or other service providers of any IRC 501(c)(6) organization, including the IRC 501(c)(6) organization that was the subject of the 2012 PLR.

ISSUES

1. Whether providing pension and health benefits to members furthers IRC 501(c)(6) business league purposes.
2. Whether providing pension and health benefits for members in the manner described will create unrelated business income within the meaning of IRC 512.

CONCLUSIONS

1. A business league's activity of providing pension and health benefits to its members does not further IRC 501(c)(6) business league purposes.
2. The activity of providing pension and health benefits to members is unrelated to the purpose or function constituting the basis for exemption of an IRC 501(c)(6) business league and results in unrelated business income within the meaning of IRC 512.

FACTS

In the 2012 PLR, an IRC 501(c)(6) Business League was a potential distributee from a State fund; the funds were earmarked for pension and health benefits of members, their families, and employees. The Business League planned to use the funds to purchase pension and health benefits for its eligible members. The Business League represented that, per State statute, all funds would be used to provide such benefits and to pay for the reasonable costs of providing such benefits. Also, the Business League would not use any such funds for general purposes. The Business League sought rulings that the

provision of such benefits was not “private inurement” and that participation in the program would not jeopardize its exempt status. The facts provided in the PLR were as follows.

A State statute provided for the establishment of a Development Fund within State's Treasury. State made distributions from the Development Fund to certain types of organizations, including the Business League. The Business League was required to use the distributions to fund health and pension benefits to its members, their families, employees, and others in accordance with the Business League's rules and eligibility requirements, as approved by a State Commission.

The Business League's website stated that its members in good standing and their dependents were eligible for the Business League's Health Care Plan and Pension Plan. In addition, full-time employees of the Business League's members were eligible for the Business League's Pension Plan. The Business League stated that it interviewed insurance providers and administrators and selected the plan features to be provided as well as the provider. The Business League paid the premiums as they became due based on a billing from the provider.

The Business League described its eligibility guidelines as straightforward and easily administered. One of the Business League's employees tracked the eligibility standards for each member. When an individual achieved the required eligibility standards, the individual's name was added to the monthly roster sent to the provider. Based on this record, the provider's representative notified each member of the benefit program and the member's eligibility date.

The Business League represented that it did not receive any fees for particular services. Amounts the Business League received from the Development Fund under the State formula for purposes of providing health and pension benefits were used exclusively for providing for such benefits and for the reasonable administrative costs of providing such benefits, not to exceed an amount specified by the statute. No amount received from the Development Fund for the purpose of providing health and welfare benefits was returned to the Business League for the Business League's own use.

The Business League stated that it was reimbursed from the Development Fund for a portion of the Business League's controller's compensation. Controller was a part-time employee whose primary responsibility was the Development Fund, including general accounting and internal controls of the Development Fund monies, financial reporting to the State Control Board, working directly with the auditors for the State Control Board, the State Department of Agriculture, and the Business League, and working with the pension fund actuaries and other professionals.

The Business League was required to file an annual audit of funds received from the

Development Fund with the State Control Board. The expense of this audit was paid from Development Fund funds. Furthermore, the State Department of Agriculture engaged an auditing firm to conduct an independent audit of all expenditures of all organizations similar to the Business League that received Development Fund funds. The State Department of Agriculture allocated the expense of this audit among the organizations, and the Business League paid this expense out of Development Fund funds, not out of the Business League's general account. The Business League engaged and paid for an independent certified public accountant to audit the Business League and its related entities.

The Business League stated that, in summary, no funds received from the Development Fund for the purpose of providing pension, health, and welfare benefits were used for the Business League's general purposes, but were used as set forth in the State statute establishing and governing the Development Fund. Any amounts received from the Development Fund for such benefits were used solely for providing the benefits and for the reasonable administrative expenses of paying such benefits. The reasonable administrative expenses included the controller's allocable expense directly related to the benefits programs. The Business League did not charge and did not pay a fee for services related to provision of benefits.

LAW

IRC 501(c)(6) provides for the exemption from federal income tax of business leagues not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

IRC 511 imposes a tax on the unrelated business taxable income of certain organizations, including those organizations described in IRC 501(c)(6).

IRC 512(a)(1) defines the term "unrelated business taxable income" as the gross income derived by any organization from any unrelated trade or business (as defined in IRC 513) regularly carried on by it, less deductions computed with the modifications provided in IRC 512(b).

IRC 513(a) provides that the term "unrelated trade or business" means, in the case of any organization subject to the tax imposed by IRC 511, any trade or business the conduct of which is not substantially related (aside from the need of such organization for the income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its exempt functions.

IRC 513(c) states, in part, that for purposes of that section, the term “trade or business” includes any activity which is carried on for the production of income from the sale of goods or the performance of services.

Section 1.501(c)(6)-1 of the Income Tax Regulations defines a business league as 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 business ordinarily carried on for profit. The activities of the business league should be directed towards the improvement of business conditions in 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 tax-exempt business league. In considering whether the organization in ABA Retirement Funds v. United States, 759 F.3d 718 (7th Cir. 2014), aff’g 2013-1 U.S. Dist. LEXIS 60086 (N.D. Ill. 2013), was a business league for purposes of section 501(c)(6), the court looked for guidance in section 1.501(c)(6)-1.

Paraphrased, the regulation provides that an organization qualifies as a business league if and only if it is an association (1) “of persons having some common business interest;” (2) “the purpose of which is to promote such common interest;” (3) that is not organized for profit; (4) that does not “engage in a regular business of a kind ordinarily carried on for profit;” (5) whose activities are “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,” and (6) that is “of the same general class as a chamber of commerce or board of trade.” See section 1.501(c)(6)-1.

Reg. 1.513-1(b) provides that for purposes of IRC 513, the term “trade or business” has the same meaning it has in IRC 162, and generally includes any activity carried on for the production of income from the sale of goods or performance of services.

Reg. 1.513-1(d)(1) provides that gross income derives from “unrelated trade or business,” within the meaning of IRC 513(a), if the conduct of the trade or business which produces the income is not substantially related (other than through the production of funds) to the purposes for which exemption is granted.

Reg. 1.513-1(d)(2) provides that a 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 (other than through the production

of income); and it is “substantially related,” for purposes of IRC 513, only if the causal relationship is a substantial one.

Rev. Rul. 65-164, 1965-1 C.B. 238, held that a nonprofit association of employers in a particular industry whose activities consisted of the negotiation of written collective bargaining labor contracts, the interpretation of such contracts, and the adjustment of labor disputes, qualified for exemption under IRC 501(c)(6). In Rev. Rul. 65-164, the organization was a nonprofit corporation without capital stock. Its membership was made up of individuals, partnerships, firms, and corporations engaged in a particular industry. Each of the foregoing entities was allowed one membership. The purposes of the organization were to conduct collective bargaining with employees and labor groups on behalf of its members generally; to promote the fulfillment of such bargaining agreements; to promote the settlement of labor disputes; to promote the prevention of strikes, lockouts, and industrial strife; to hold meetings of members for the interchange of views for their mutual benefit; promotion of their trades and industrial harmony and prevention of labor disputes; to conduct investigations toward the promotion of industrial harmony for settlement of labor disputes; and to promote a spirit of cooperation among members and between members and labor groups and employees. The organization's only activities consisted of negotiation of written collective bargaining labor contracts, the interpretation of such contracts, and the adjustment of labor disputes on an industrywide basis. Interpretation of contracts and adjustments of labor disputes were incidental to its primary activity of negotiating collective bargaining agreements. Rev. Rul. 65-164 noted that these activities ‘further the common purpose with respect to the common labor problems of the business group and do not represent services to individual members which they could purchase elsewhere.’ This ruling was in accord with the decision in the case of Associated Industries of Cleveland v. Commissioner, 7 T.C. 1449 (1946), in which the Commissioner acquiesced. C.B. 1947-1, 1. The avowed labor purpose of the organization in that case was to secure and perpetuate for employers and employees freedom of contract, and, in general, its purpose was to provide the means whereby the executive heads of the industries engaged in Cleveland and vicinity may meet to discuss, for the benefit of all engaged in industry, the various problems of common interest, and to promote a better understanding concerning subjects of material interest, particularly those relating to labor, production, and finance. In actual operation the organization was an employers’ association which primarily backed the “open shop” principle. The organization participated in labor contract negotiations and in settling labor disputes; it advised its members with respect thereto and furnished general labor information. The Tax Court held that the organization was held exempt from Federal income tax as a business league under section 101(7) of the 1939 Code (corresponding to section 501(c)(6) of the 1954 Code).

In support of its conclusion that the organization was exempt, the Tax Court stated, in part, as follows:

“* * * (I)t is clear that the real business interest which petitioner's members have in common is the desire to establish what the members consider to be ‘industrial peace and sound industrial relations in the community’ by advancing and maintaining the ‘open shop’ principle in the industry. The members have endeavored to establish employment and labor conditions which are stable and desirable from their standpoint. They wanted a readily available labor market from which they could obtain skilled labor upon such terms and conditions as they considered most favorable to themselves. To develop and insure the labor conditions which they deemed desirable they banded together to form the petitioner association.”

It was specifically noted in Rev. Rul. 65-164 that the functions of a labor or personnel department would not be activities consistent with exemption for an association under IRC 501(c)(6) because it would be permitting benefits to inure to the membership.

Rev. Rul. 66-151, 1966-1 C.B. 152, describes a business league exempt under IRC 501(c)(6) whose principal activity is to represent member firms in all matters pertaining to their relationship with labor unions. The organization also regularly manages a health and welfare plan for its members. It receives a fee for each employee covered by the plan. In the context of “unrelated trade or business,” Rev. Rul. 66-151 holds that the management of health and welfare plans, including the performance of services connected therewith, constitutes a business that is not substantially related to the basis for which exemption is granted under IRC 501(c)(6). Therefore, the management of the health and welfare plans by the organization constitutes the conduct of an unrelated trade or business within the meaning of IRC 513, and the organization is subject to the tax imposed by IRC 511, as computed under IRC 512, on the income from such activity.

Rev. Rul. 67-176, 1967-1 C.B. 140, held that an organization formed to provide an emergency loan plan, practice loan plan, hotel discounts, and car leasing plan to serve primarily as a convenience and economy to members in providing financial aid in completing their professional studies and establishing themselves in practice performed particular services for members as opposed to improvement of a line of business. Therefore, the organization did not qualify for exemption from federal income tax under IRC 501(c)(6).

Rev. Rul. 67-251, 1967-2 C.B. 196, considered the exemption of a business league which extends financial aid and welfare services to its members; the ruling held that the organization does not qualify under IRC 501(c)(6) since part of its net earnings inure to the benefit of private individuals. The IRS found that the organization benefited private individuals by providing financial aid and welfare services to its members. Therefore, the business league was not exempt under IRC 501(c)(6), even though its financial aid to

members is minor in relation to its other activities which are directed to improvement of business conditions in a line of business.

Rev. Rul. 71-155, 1971-1 C.B. 152, provides that an organization composed of licensed insurance companies that was designed to make insurance available to persons who are in high-risk categories and are not otherwise able to obtain coverage qualifies for exemption under IRC 501(c)(6). The organization was formed to distribute high risk policies among all members. The IRS found that the organization promoted the common business interests of members because spreading high risk policies among members provides insurance to persons who would normally be unable to obtain insurance and decreased public criticism of the industry. Accordingly, the organization conducted activities that improved business conditions of one or more lines of business as distinguished from the performance of particular services for members.

Rev. Rul. 73-452, 1973-2 C.B. 183, holds that an organization created under State statute to pay claims against insolvent fire and casualty insurance companies qualifies for exemption as a business league under IRC 501(c)(6). The ruling holds that by assuring the payment of claims and providing a means for their orderly liquidation, the organization is serving a quasi-public function imposed by law which is directed at relieving a common cause of hardship and distress of broad public concern in the field of insurance protection. The function serves an important common business interest of the industry by meeting a widespread need which is incident to the field of insurance, could not be effectively met in the ordinary course of the individual insurance businesses of the members, and does not directly enhance the profitability of such individual businesses.

Rev. Rul. 74-81, 1974-1 C.B. 135, holds that a nonprofit organization formed to promote the business welfare and interests of persons engaged in the contracting trade and related industries and whose principal activity is to provide its members with group workmen's compensation insurance is rendering a particular service to members and is not entitled to exemption under IRC 501(c)(6).

Rev. Rul. 76-410, 1976-2 C.B. 155, provides that a nonprofit organization composed of insurance companies operating within a state and created under the state's no-fault insurance statute to provide personal injury protection benefits for residents of the state who sustain injury in situations where the injuring party is unknown or has very limited or no liability insurance coverage qualifies for exemption under IRC 501(c)(6). The IRS found that the organization's activities "promote the common business interests of its members by fulfilling an obligation that the state has imposed upon the insurance

industry as a prerequisite for doing business within the state and by enhancing the image of the industry.” Also, because all insurance companies operating in the state were required to be members, the ruling found that there was no competitive edge gained by any of the members of the organization. The IRS found that all of these activities indicate that the organization was formed to improve business conditions of one or more lines of business rather than to perform particular services for individual members.

Rev. Rul. 81-174, 1981-1 C.B. 336, holds that a nonprofit association of insurance companies, created by an act of the State legislature, that provides medical malpractice insurance to health care providers is not exempt under IRC 501(c)(6). The organization charges fees, issues policies, and performs administrative services typical of insurance companies’ normal operation, and it is the nature of this activity that determines whether it is a business ordinarily carried on for profit. The revenue ruling concludes that the organization is operating in a manner similar to a business ordinarily carried on for profit and, equally important, since its method of operation involves it in its member companies’ insurance business, and since its insurance activities serve as an economy or convenience in providing necessary protection to its policyholders, the organization is performing particular services for its member companies and policyholders. The revenue ruling distinguishes Rev. Rul. 71-155, a state-mandated association composed of all insurance companies writing a specified type of insurance in a given state that was formed for the purpose of making insurance available to all persons in high-risk categories. The organization in Rev. Rul. 71-155 operated by accepting applications, and then assigning them to a member company, that performed the actual insurance functions. Unlike the organization in this case, the organization described in Rev. Rul. 71-155 did not assume the risk on a policy, and therefore was not itself engaged in the insurance business.

Rev. Rul. 81-175, 1981-1 C.B. 337, holds that a nonprofit association of automobile insurance companies that accepts for reinsurance high-risk customers who would ordinarily be turned down by member companies is not exempt under IRC 501(c)(6). The organization was created by an act of the State legislature for the purpose of guaranteeing the availability of automobile insurance to persons who are in high-risk categories and cannot otherwise obtain coverage. The organization assures the availability of this insurance by accepting for reinsurance high-risk customers that member companies would ordinarily turn down. The revenue ruling concludes that since reinsurance is a business ordinarily carried on by commercial insurance companies for profit, the organization is not operated as a business league within the requirements of Reg. 1.501(c)(6)-1. The revenue ruling distinguishes Rev. Rul. 71-155

in the same way that Rev. Rul. 81-174 distinguished that ruling, by noting that the organization in Rev. Rul. 71-155 did not assume the risk on the policy.

In Southern Hardwood Traffic Association v. United States, 411 F.2d 563 (6th Cir. 1969), the plaintiff provided its members with a variety of services, such as the collection of freight claims and the preparation of bills of lading. In holding that the plaintiff was not a “business league” entitled to tax exempt status, the court stated:

Any particular activity or service performed, which does not ... benefit ... all of its members generally and which would otherwise have to be done by or for the members in order for him to properly perform his business, must be classified as an individual service.

Similarly, in Associated Master Barbers & Beauticians of America, Inc. v. Commissioner, 69 T.C. 53 (1977), the court sustained the revocation of the petitioner’s exempt status under IRC 501(c)(6) because of the extensive services provided to members. The court stated:

Because these activities serve as a convenience or economy to petitioner’s members in the operation of their business, we think they constitute “particular services” as proscribed by the regulation. By providing insurance or textbooks for its members, the petitioner relieves its members of obtaining insurance or textbooks on an individual basis from a nonexempt commercial business. If the petitioner did not provide these goods and services, its members would have to obtain them from nonexempt businesses at a substantial increased cost. Thus, the organization is rendering “particular services” for the individual members as distinguished from an improvement of business conditions in barbering and beautician professions generally.

In Indiana Retail Hardware Association v. United States, 366 F.2d 998 (Ct. Cl. 1966), the court held that an association which performed managerial services, weekly bookkeeping services, quarterly audits, annual preparation of federal income tax returns and other services for its members was engaged in particular services for its members and was not exempt.

As to the industry-wide nature of services provided, in MIB, Inc. v. Commissioner, 734 F. 2d 71, 78 (1st Cir. 1984), the court stated that although “industry-wide participation defeats the inference that some members have been treated specially or given competitive advantages, it does not resolve the nature of the services received.” Thus, the court found that a non-profit organization that provides a databank and an exchange

for confidential life insurance information was providing particular services to its members and was denied exemption under IRC 501(c)(6).

In Steamship Trade Association of Baltimore, Inc. v. Commissioner, 757 F.2d 1494 (4th Cir. 1984), aff'g 81 T.C. 303 (1983), the appeals court found that the organization's activities were not related to its exempt trade or business and, therefore, the income was derived from non-tax-exempt activities. Steamship Trade Association of Baltimore, Inc. (STA)'s primary activity was negotiating collective bargaining agreements on behalf of its members, who were businesses associated with the maritime industry in the Port of Baltimore. The collective bargaining agreements provided, among other things, that STA's employer members would pay a vacation benefit and a guaranteed annual income to their employees. The calculation to provide these benefits for each employee was based on the number of hours worked. STA assisted members by collecting members' information regarding the number of hours each employee worked, computing the assessment rate that members must pay to support the vacation and annual income accounts, collecting the assessments, paying the proper benefits to the eligible employees and reporting to the union about these activities. STA was paid fees for administering the vacation pay and guaranteed annual income assessment benefits. The appeals court found that STA was engaged in a trade or business by performing comprehensive and essential business services in return for a fixed fee. The court also found that while negotiating, interpreting the collective bargaining agreement, and resolving disputes was an exempt function, administering the vacation pay and guaranteed annual income funds was not substantially related to STA's performance of its exempt functions. Consequently, the court upheld the district court and ruled that the organization owed tax under IRC 511(a) on income derived from administering its members' benefit plans.

In ABA Retirement Funds v. United States, 759 F.3d 718 (7th Cir. 2014), aff'g 2013-1 U.S. Dist. LEXIS 60086 (N.D. Ill. 2013), an appeals court upheld a district court's ruling that an organization formed to create and maintain retirement plans for adoption by lawyers and law firms was not a tax-exempt "business league" under IRC 501(c)(6). ABA Retirement entered into a contract with State Street Bank and Trust to be the trustee and ABA Retirement became the plan fiduciary. In its role as plan fiduciary, ABA Retirement had a variety of duties, such as vendor oversight, negotiating contracts, reviewing and approving the marketing plan, and recommending ways to grow its participant list and assets. ABA Retirement assisted State Street in its marketing efforts by publicizing and mailing promotional materials about its retirement plans to attorneys, sections of the ABA, and others engaged in the legal profession. Although State Street was

authorized to hire and fire investment consultants, ABA also had input in the investment decisions. ABA was authorized to fire State Street.

The Plan paid ABA Retirement for the expenses incurred in providing administration, marketing and other services related to the retirement program. The fee was based on a percentage of all the investments. In considering whether ABA Retirement was a business league for purposes of section 501(c)(6), the court looked for guidance in section 1.501(c)(6)-1 of the Treasury regulations, specifically, the six points enumerated earlier. The court stated:

"ABA Retirement fails every necessary condition for business league status. Because the district court's opinion is thorough, we focus on just two of the reasons why ABA retirement is not a business league: 1) its activities are not directed to the improvement of business conditions for the legal field generally; and 2) it engages in a business ordinarily conducted for profit. "

The appeals court agreed with the district court that an organization that engages in business activities incidentally will not lose its tax exemption. However, in this case, both courts found that:

"the association's insurance activities were directed towards providing benefits to individuals within the industry and those activities were substantial."

The court found that ABA Retirement's activities were not directed to the improvement of business conditions of one or more lines of business because it carried on substantial activities directed towards promoting its own retirement plan, rather than promoting general retirement savings in the legal profession. The court stated that while retirement planning is a business, it provides benefits to individual persons, not to an entire field of commerce, and doesn't qualify ABA Retirement for exempt status. The court found that ABA Retirement was engaged in business ordinarily conducted for profit because ABA Retirement was not just a sponsor of the retirement plan, it provided a service in connection with the retirement program for which it was paid a program expense fee based on a percentage of the total assets. Accordingly, the court concluded that ABA Retirement was not exempt from federal income tax under IRC 501(c)(6).

ANALYSIS

Issue 1: Whether Providing Pension and Health Benefits to Members Furthers an IRC 501(c)(6) Business League Purpose.

To determine whether an activity is furthering an organization's exempt purpose, one has to first determine what constitutes an organization's exempt purpose. IRC 501(c)(6) provides for the exemption from Federal income taxation of business leagues not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.³ One of the requirements of a business league is that its 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. Reg. 1.501(c)(6)-1. The question then is whether, in the 2012 PLR, the Business League's provision of pension and health benefits is directed to the improvement of one or more lines of business or whether it is the performance of particular services for individual persons. Reg. 1.501(c)(6)-1.

The 2012 PLR is silent regarding the Business League's specific line of business that its activities seek to promote. The implication is that the provision of pension and welfare benefits to members, regardless of the line of business, would improve business conditions of any line of business.

The 2012 PLR stated, "Like the insurance activities described in Rev. Rul. 71-155, using State funds to procure health and pension benefits for your members and their employees is a way of providing insurance to persons who would normally be unable to obtain such benefits, thereby improving the image of the industry. By using State funds to provide health and pension benefits to your members, you are serving a function imposed by law which is directed at relieving a cause of hardship and distress in a particular industry in State. Rev. Rul. 73-452 and Rev. Rul. 76-410. You are complying with a legal mandate that will improve business conditions in your members' line of business rather than performing particular services for individual members. Consequently, such activities are considered to be substantially related to your exempt purposes and would not affect your recognition under section 501(c)(6)."

However, the PLR failed to distinguish Rev. Rul. 81-174 and Rev. Rul. 81-175, in which organizations created by state mandate to provide insurance were denied tax exempt status under IRC 501(c)(6) because they were found to be operating in a manner similar to a business ordinarily carried on for profit as distinguished from the improvement of business conditions in a particular industry. The PLR also failed to distinguish Rev. Rul. 66-151, Rev. Rul. 67-251, and Rev. Rul. 74-81; these organizations provided services

³ The existence of *any* private inurement will jeopardize the tax-exempt status of an organization under IRC 501(c)(6) even if the activity resulting in private inurement is considered minor in relation to the organization's overall exempt activities. Rev. Rul. 67-251. Determination of private inurement is based on the organization's specific facts and circumstances at issue.

to individuals with respect to financial aid, health and welfare plans, and workman's compensation insurance, which resulted in either UBIT or the denial of exemption.

Rev. Rul. 73-452, and Rev. Rul. 76-410, illustrate two of the very few exceptions to state-created organizations that qualify as business leagues, and they are very narrowly drawn. Rev. Rul. 73-452 describes an organization aiding the policyholders covered by insolvent member fire and casualty insurance companies, thus serving an important common business interest of the insurance company members. The organization gives assurance to the public that its insurance company members will provide insurance, even in insolvency, thus improving the public's perception of the insurance industry as a whole. Rev. Rul. 76-410 describes an organization required by the state's no-fault insurance law to provide personal injury protection benefits for residents who are injured by unknown parties or by parties with limited or no liability coverage. The ruling found that the organization enhanced the image of the industry and promoted the common business interests of its members by fulfilling an obligation that the state imposed upon the insurance industry as a prerequisite for doing business within the state. Also, because every insurance company operating in the state was required to be a member, there was no competitive edge to being a member of the organization.

The Business League's activities are distinguishable from the activities described in Rev. Rul. 73-452 and Rev. Rul. 76-410, because the Business League's activities are not directed at enhancing the public's perception of an industry nor fulfilling a state imposed obligation specific to a particular industry.

If a particular activity or service performed by an organization relieves the member of the necessity of securing the service commercially (or performing the service on an individual basis) in order to properly conduct the member's business, resulting in a convenience or economy to the member, the activity or service will be classified as a 'particular service' for purposes of Reg. 1.501(c)(6)-1. Rev. Ruls. 67-176, 74-81, 81-174, and 81-175.

Additionally, in a later case, ABA Retirement Funds, the court found that an organization that was engaged in the business of providing retirement plans, a business ordinarily conducted for profit, failed to qualify for tax exemption under IRC 501(c)(6).

In ABA Retirement Funds, the appeals court considered an organization that provided members with retirement plans. The court held that the organization was not a tax-exempt business league under IRC 501(c)(6) because its activities were not directed to the improvement of business conditions for the legal field generally. The organization contended that:

“[L]awyers secure in their retirement are happy, confident lawyers, and this is reflected in the general satisfaction quotient for the profession as a whole.”

The court, however, stated:

“That may be true: we do not doubt that retirement planning is good for the legal profession generally (as it is for everyone else), but ABA Retirement furnished that benefit almost exclusively by providing a particular service to particular persons, namely, retirement plans for those who signed up for its program.”

Applying the law in ABA Retirement to the current case in the 2012 PLR, the Business League’s activity of providing pension benefits is not an activity that improves a line of business; rather, it is providing a particular service to its members, and possibly their families, employees, and others.⁴ This is also consistent with the holding in Rev. Rul. 67-251, 1967-2 C.B. 196, where a business league that extended financial aid and welfare services to its members did not qualify under IRC 501(c)(6) since part of its net earnings inured to the benefit of private individuals; this was so, even though its financial aid to members was minor in relation to its other activities which were directed to improvement of business conditions in a line of business. See also, Rev. Rul. 67-176, 1967-1 C.B. 140 (providing an emergency loan plan, practice loan plan, hotel discounts, and a car leasing plan is tantamount to performing particular services for members as opposed to improvement of a line of business.)

Providing members with a variety of services, such as the collection of freight claims and the preparation of bills of lading, is the performance of individual services rather than benefiting the membership as a whole. Southern Hardwood Traffic Association v. United States. In providing insurance or textbooks for members, an organization is relieving its members of obtaining insurance or textbooks on an individual basis from a nonexempt commercial business; thus, the organization is rendering “particular services” for the individual members as distinguished from an improvement of business conditions. Associated Master Barbers & Beauticians of America, Inc. v. Commissioner. Finally, an association that performed managerial services, weekly bookkeeping services, quarterly audits, annual preparation of federal income tax returns and other services for its members was engaged in particular services for its members. Indiana Retail Hardware Association v. United States. Contrast an association whose activities

⁴ Although it is unclear whether any benefits are provided to family members or employees of the business league’s members, the facts provided by the PLR indicate that benefits may be provided to family members, employees, or others. Benefits to family members, employees, and others are clearly services to particular individuals rather than improvement of business conditions.

consisted of the negotiation of written collective bargaining labor contracts, the interpretation of such contracts, and the adjustment of labor disputes; these activities further the common purpose with respect to the common labor problems of the business group and do not represent services to individual members that they could purchase elsewhere. Rev. Rul. 65-164, 1965-1 C.B. 238.

The PLR's conclusion that the Business League's pension and health activities confer a benefit to the industry as a whole is similar to an argument made by the appellant in MIB, Inc. v. Commissioner. MIB asserts that by maintaining an information data bank and distributing information as requested by members, it prevents fraudulent claims by insureds and claimants who may leave out or conceal information needed by insurance company members to assess risks. The court concludes that while the operation of an information exchange may provide a benefit to all the members and act to deter fraud, MIB is still performing particular services for individual persons. Like the organization in MIB, Inc. v. Commissioner, the Business League's pension and health administration activities may provide a benefit to the industry as a whole, but the activities being performed are still particular services for individual persons, and not necessarily just to persons conducting the businesses, but rather also to family members, employees, or others (directly or indirectly). Furthermore, the provision of these benefits is personal in nature, rather than related to the operation of the members' businesses, as in MIB and Rev. Rul. 71-155, Rev. Rul. 73-452, and Rev. Rul. 76-410.

The Business League's provision of administrative services for its health and pension program is the provision of particular services to individual persons rather than the improvement of a line of business. Therefore, the 2012 PLR Business League's provision of pension and welfare benefits to its members and possibly to their families, employees, and others does not further its exempt business league purposes.

Issue 2: Whether Providing Pension and Health Benefits for Members in the Manner Described will Create Unrelated Trade or Business

The question is whether the Business League's activities related to the provision of pension and health benefits would generate unrelated business taxable income.

In determining whether an activity constitutes an "unrelated trade or business," it is necessary to decide:

- (1) Whether it is a trade or business; IRC 511.
- (2) Whether it is regularly carried on; IRC 512(a)(1) and

- (3) Whether it is substantially related to the purpose or function forming the basis of Taxpayer's exemption under IRC 501(c)(6). IRC 513(a); Regs. 1.513-1(d)(1) and (2).

The term trade or business has the same meaning it has in IRC 162 and generally includes any activity carried on for the production of income from the sale of goods or the performance of services. Reg. 1.513-1(b). The provision of pension and health benefits is a trade or business because it is the performance of services. See Rev. Rul. 66-151, which holds that the management of health and welfare plans, including the performance of services therewith, constitutes a business that is not substantially related to the basis for which exemption is granted under IRC 501(c)(6). The activity is also regularly carried on. The remaining issue is whether the activity is substantially related within the meaning of IRC 513 to the Business League's exempt business league purpose of promoting a line of business.

The Business League interviews insurance providers and administrators and selects the plan features to be provided as well as the provider. The Business League pays the premiums as they become due based on a billing from the provider. One of the Business League's employees tracks the eligibility standards for each member. When an individual achieves the required eligibility standards, his name is added to the monthly roster sent to the provider. The Business League is reimbursed from the State Development Fund for a portion of the controller's compensation. In this case, providing pension and health benefits to individual members, family members, and employees constitutes a regular business of a kind ordinarily carried on for profit and does not further IRC 501(c)(6) purposes, even if fees are used to pay the expenses.

With respect to compliance with state law, Rev. Rul. 81-174, and Rev. Rul. 81-175, illustrate that the creation of an organization by state statute does not independently qualify the organization for exemption under IRC 501(c)(6). Although the organizations described in these rulings were established pursuant to state statutes, the organizations were still deemed to be performing services for individuals rather than promoting a business purpose. Similarly, in this case, an activity that is provided for by state statute is not necessarily substantially related to an IRC 501(c)(6) business league's exempt purpose. See Rev. Rul. 81-174, and Rev. Rul. 81-175. (Although these rulings deal with exemption, Rev. Rul. 81-174 concludes that that an organization that provided medical malpractice insurance is operating in a manner similar to a business ordinarily carried on for profit; Rev. Rul. 81-175 states that reinsurance is a business ordinarily carried on by commercial insurance companies for profit.) Additionally, in this case, the state and the state statute do not appear to require organizations such as the Business

League to receive funds from Development Fund. Rather, if any amounts are received from Development Fund, those amounts must be used solely for providing benefits and paying the reasonable administrative expenses of paying such benefits.

The Business League's facts are more similar to the facts in Steamship Trade Association of Baltimore, Inc., which involved an organization that administered certain benefit plans for its members. By administering these benefit plans for its members, the organization was performing an activity that was unrelated to its exempt business league purposes; therefore, the organization was subject to tax under IRC 511(a). The Business League performed a variety of administrative services with respect to the pension and health benefits. These activities included interviewing insurance providers and administrators and selecting the plan features to be provided as well as the provider, paying the premiums as they become due based on a billing from the provider, tracking the eligibility standards for each member, and adding eligible names to the monthly roster sent to the provider. Absent the Business League, members would have been required to pay for their own pension and health benefits. The Business League enabled its members to share certain administrative services among themselves that they otherwise would have had to purchase separately.

The Business League is also like the organization held taxable in Rev. Rul. 66-151. In Rev. Rul. 66-151, the IRC 501(c)(6) organization regularly manages health and welfare plans for its members and receives a fixed fee for each employee covered by the plan; significant amounts of the organization's income and expenses are attributable to the management of these plans. The revenue ruling concludes that the management of the plans by the organization was not substantially related to the functions forming the basis for the exemption of the organization and therefore, constituted the conduct of an unrelated trade or business.

Additionally, in ABA Retirement Funds, the court stated that the organization was engaged in the business of providing retirement plans, a business ordinarily conducted for profit. The court stated, "Returning to the question at hand – whether ABA Retirement was engaged in business ordinarily done for profit...- the answer is an unequivocal yes."

Similar to the organizations described in Steamship and ABA, the services provided by the Business League are readily available in the marketplace through commercial entities such as insurance companies, banks, investment firms or data processing firms. The performance of services connected with the management of pension and health

benefits constitutes an activity that is not substantially related to promoting a particular industry, for which exemption under IRC 501(c)(6) is granted.

With respect to the discussion of issue one, the guidelines provided by the regulations with respect to the purpose or function of an exempt business league are that the 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. Reg. 1.501(c)(6)-1. However, if the activities constitute the performance of commercial services to individual members, they would ordinarily be unrelated to the purpose or function constituting the basis for exemption and would constitute unrelated trade or business with the meaning of IRC 513. Rev. Rul. 66-151.

The Business League's provision of administrative services in connection with its pension and health benefits constitutes the conduct of an unrelated trade or business under IRC 513.

CONCLUSION

In general, providing pension and health benefits to members does not further IRC 501(c)(6) purposes and is not substantially related to the promotion of the common interest of the membership of an IRC 501(c)(6) business league. These activities relieve members of the business expense and burden of separately providing for and managing their health and pension benefits. Therefore, these activities are generally subject to tax under IRC 511 because they constitute unrelated trade or business under IRC 512 and are not substantially related within the meaning of IRC 513.

Based on this analysis, the conclusion in the 2012 PLR is not in accord with the current views of this office. We are issuing this memorandum specifically to state our view that, under the facts and circumstances described in the PLR, the organization's proposed activities do not further an IRC 501(c)(6) purpose and are not substantially related to the function forming the basis of the organization's exemption under IRC 513.

We make no comment regarding the organization's continuing exemption that was the basis of the rulings requested.

Please call Sadie Copeland at 202-317-6012 or Virginia Richardson at 202-317-4086 if you have any further questions.

PRESP-113092-17

Cc:

Deputy Division Counsel
CC:TEGEDC