Internal Revenue Service
Director, Exempt Organizations
Rulings and Agreements

Department of the Treasury
P.O. Box 2508 - RM 7008
Cincinnati, OH 45201

Date:

Employer Identification Number:

Person to Contact - I.D. Number:

Contact Telephone Numbers:
Phone
FAX

Legend:

A =
M =
N =
x =

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under the provisions of section 501(c)(6) of the Internal Revenue Code of 1986 and its applicable Income Tax Regulations. Based on the available information, we have determined that you do not qualify for the reasons set forth on Enclosure I.

Consideration was given to whether you qualify for exemption under other subsections of section 501(c) of the Code. However, we have concluded that you do not qualify under another subsection.

As your organization has not established exemption from Federal income tax, it will be necessary for you to file an annual income tax return on Form 1041 if you are a Trust, or Form 1120 if you are a corporation or an unincorporated association.

If you are in agreement with our proposed denial, please sign and return one copy of the enclosed Form 6018, Consent to Proposed Adverse Action.

You have the right to protest this proposed determination if you believe it is incorrect. To protest, you should submit a written appeal giving the facts, law and other information to support your position as explained in the enclosed Publication 892, "Exempt Organizations Appeal Procedures for Unagreed Issues." The appeal must be submitted within 30 days from the date of this letter and must be signed by one of your principal officers. You may request a hearing with a member of the office of the Regional Director of Appeals when you file your appeal. If a hearing is requested, you will be contacted to arrange a date for it. The hearing may be held at the Regional Office or, if you request, at any mutually convenient District Office. If you are to be represented by someone who is not one of your principal officers, he or she must file a proper power of attorney and otherwise qualify under our Conference and Practice Requirements as set forth in Section 601.502 of the Statement of Procedural Rules. See Treasury Department Circular No. 230.

If we do not hear from you within the time specified, this will become our final determination.

Sincerely,

Lois G. Lerner
Director, Exempt Organizations
Rulings and Agreements

Enclosures: 4
Attachment I
Notice 437
Form 6018
Publication 892

Attachment 1

Issue 1

Does M, who is formed to operate as a health plan purchasing cooperative that is authorized by the Insurance Commissioner of the state in which they reside, qualify for exemption under section 501(c)(6) of the Internal Revenue Code (Code)?

Facts of the Case

You were incorporated within the state of N effective April 8, 2003 under the nonprofit corporate laws of the state. Your Incorporator and President, A, signed on April 30, 2003 an amendment to the Articles of Incorporation. While the Amended Articles of Incorporation appear to be a complete re-statement of the originally filed Articles of Incorporation, a copy of the originally filed Articles was not provided.

Your purpose is to operate as a health plan purchasing cooperative that is authorized by the Insurance Commissioner of the state of N. Your principal purpose is to assist your members in negotiating and obtaining the best possible major medical health care benefits (for members' employees) at the lowest possible costs. You will develop major medical plan designs and negotiate the implementation of such plans with major medical health insurance carriers on behalf of your business members to secure the best and most cost effective health insurance benefits. You will also provide administrative billing services, customer service, grievance tracking and settlement between employees and carriers, and State regulation compliance reporting.

You will receive your revenue in the form of membership dues and fees and in administrative fees from the insurance servicing agents. The insurance servicing agents pay you for your work in establishing and maintaining the membership, development and collection of census data for your members, carrier negotiation, providing marketing and instructional material to be used by the servicing agents, and for providing grievance resolution services for the members' employees. Your expenses will be the payment of the premiums for the covered health insurance in addition to marketing and various administrative expenses, including salaries.

Your membership is open to small businesses with at least two full-time employees and gross receipts of $50,000 or more per year. The member firm must have completed revenue-producing activities for at least 12 consecutive months and such activities must be operated on a regular and active basis throughout the calendar year. Large businesses can also participate, subject to your approval. You will not accept individual or sole proprietor type businesses. There is no

restriction on the type of business conducted nor is there a limit to businesses in any one particular industry. Your membership covers businesses in a 30 county area within the state of N.

Applicable Law

Section 501(c)(6) of the Internal Revenue Code provides for the exemption from Federal income tax of business leagues not organized for profit, 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 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 engage in a regular business of a kind ordinarily carried on for profit. Its activities should be directed towards 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 a 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.

Revenue Ruling 81-175, 1981-1 C.B. 337, held that an organization was engaged in an activity that is a business ordinarily carried on by commercial companies for profit (even though this organization did not operate to make a profit) and that the activities it conducted constituted the performance of services for its member companies. As such exemption would not be allowed under section 501(c)(6) of the Code. 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 who could not otherwise obtain coverage. Member companies, who are required by law to furnish insurance to any customer, regardless of the degree of risk involved, were able to reinsure up to 50 percent of their insurance business through the organization. Thus the organization accepting such reinsurance from its members provided the state required guarantee of the availability of insurance. The ruling found not only that the reinsurance activity was a commercial activity, but that it was also providing a particular service to its members. The organization was providing an economy or convenience to members in the operation of their own insurance business by accepting the risk of insuring their high-risk customers. Both the provision of services to individuals and operating a commercial activity were preclusions to exemption under section 501(c)(6) of the Code for the organization.

Revenue Ruling 81-174, 1981-1 C.B. 335, holds that an organization created as a non-profit association by an act of the state legislature for the purpose of providing malpractice insurance to doctors, nurses,

hospitals, and other medical providers in the state is not exempt under IRC 501(c)(6). Membership in the association is mandatory for all insurance companies providing certain types of liability insurance in the state. A member's assessment is based on its company's share of all liability insurance written in the state during the prior year. Any losses incurred by the association in its payment of malpractice insurance to policyholders are shared proportionally by the members. Any profits that may arise are refunded to policyholders as the policy rates are set to meet only losses and expenses. The ruling concludes that providing malpractice insurance is a business activity of a kind ordinarily carried on for profit. In addition, since the association's method of operation involves it in its member companies' insurance business, and since the association's insurance activities serve as an economy or convenience in providing necessary protection to its policyholders engaged in providing health care, the association is performing particular services for its member companies and policyholders.

In Revenue Ruling 74-81, an organization, whose principal activity was providing its members group workman's compensation insurance that was underwritten by a private insurance company, was denied exemption under section 501(c)(6) of the Code since it rendered particular services for individual persons (its members). The ruling concluded 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 and a service to them. Exemption under section 501(c)(6) of the Code makes a distinction between activities that are directed to the improvement of business conditions in one or more lines of business from those activities that are the performance of particular services to individuals.

Prior to the determination found in Revenue Ruling 74-81, exemption under section 501(c)(6) was allowed an association of insurance companies in Revenue Ruling 71-155, 1971-1 C.B. 152. The facts are fairly different in this ruling, however. The association in this ruling makes insurance *available* to persons in high-risk categories who cannot otherwise obtain coverage. The association was formed pursuant to state and federal programs to ensure availability of insurance to persons in high-risk categories and eliminate the criticism towards the industry for high-risk policy cancellations. The state's Insurance Commission requires membership in the association. The association will accept persons in high-risk categories and *refer* their insurance handling to a member company. In this way the organization is equitably spreading the risk to every (member) insurer. The ruling concluded the association's activities promoted the common business interests of the members as it minimized the public criticism of the industry by creating an avenue for persons who would normally be unable to obtain insurance. Since the association did not actually provide the insurance (assume the risk) but referred the work to member businesses, the association was not

conducting (insurance) business normally carried on for profit. And while member businesses would benefit from the referred business, such benefit was equally spread among the entire member insurer population and would be considered incidental to the overall purpose of complying with the state regulations of providing insurance coverage to all individuals, regardless of risk.

Revenue Ruling 68-264, 1968-1 C.B. 264, held that an organization that operates as its primary activity a traffic bureau that assisted members and nonmembers in the shipment of their goods and products is conducting an activity that constitutes a regular business of a kind ordinarily carried on for profit and constitutes the performance of particular services for individual persons. As such, the organization is not exempt from tax under IRC 501(c)(6). The services the organization provides includes quotations of freight rates, rules and practices; investigations of loss, damage, and overcharge claims; handling of rate cases for individual members before regulatory bodies; investigation of complaints on transportation services; and furnishing of information on transportation laws. The ruling concluded that the operation of a traffic bureau is a clear convenience and economy to the members in their businesses, resulting in savings and simplified operations. Exemption under IRC 501(c)(6) was not allowed.

Revenue Ruling 66-338, 1966-2 C.B. 226, held that an organization formed to promote the interest of a particular retail trade which advises its members in the operation of their individual businesses and sells supplies and equipment to them is not exempt from tax under IRC 501(c)(6). Field representatives make visits to member businesses offering them advise on business problems that the member may be experiencing at the time. They also inform the members about supplies, equipment and additional services that the organization can make available to them at low prices. Such activities were found to be providing the members with an economy and convenience in the conduct of their individual businesses by enabling them to secure supplies, equipment and services more cheaply than if they had to secure them on an individual basis. These activities are considered a performance of particular services for individual persons as distinguished from activities aimed at the improvement of business conditions in their trade as a whole and thus exemption under section 501(c)(6) of the Code was not allowed.

A determination of whether members in an organization had a common business interest and whether their activities were directed toward the improvement of one or more lines of business was made in Revenue Ruling 59-391, 1959-2 C.B. 151. The organization was composed of individuals, firms, associations, and corporations each representing a different trade, business, occupation or profession. The organization met at various time to exchange information on business prospects. The ruling concluded that there was no common business interest other than a mutual desire to increase their individual sales and that the

activities were not directed to the improvement of one more lines of business, but rather to the promotion of the private interests of its members. Thus, exemption was not allowed under section 501(c)(6) of the Code.

In Revenue Ruling 69-106, 1969-1 C.B. 153, exemption was not allowed to a manufacturers' organization that conducted research and development in projects of common interest to their industry. While no research was conducted for any member in particular, the results of the research were made available only to members. The ruling concluded that since the organization distributed the results of its research only to its members, its activities were not aimed at the improvement of business conditions for the entire industry. For exemption to be allowed, the research would have to be made available to all members of an industry.

Revenue Ruling 56-65, 1956-1 C.B. 199, held that while the activities of the entity carried many of the attributes normally found in business leagues entitled to exemption under section 501(c)(6) of the Code with many benefits to the industry, the general public and the state and federal governments, it was found that the entity was created and primarily operated as a service to its individual members. Its principal activity consisted of furnishing particular information and specialized individual service to its members who were engaged in a particular industry through publications and other means that effect economies in the operation of their individual businesses. As such exemption under section 501(c)(6) of the Code was not allowed since the organization was primarily engaged in the performance of particular services for individual persons.

Revenue Ruling 65-164, 1965-1 C.B. 238, clarified Revenue Ruling 56-65 on the labor relations activities that can be allowed organizations exempt under section 501(c)(6) of the Code. The organization in Revenue Ruling 65-164 negotiated terms of a uniform labor contract for the entire industry. As an incidental activity the organization also provided interpretations of such contracts and adjustments of labor disputes on an industry-wide basis. The ruling concluded that negotiating labor contracts for the general membership, mediating or settling jurisdictional and other disputes, and furnishing general information furthered the membership's common business interests, that being their labor problems. The negotiations were for industry-wide labor problem resolution and harmony between members, labor groups and employees. Such negotiations did not represent services to individual members that they could purchase elsewhere. Thus, exemption under section 501(c)(6) of the Code was allowed for its industry-wide negotiations.

In *American Automobile Association v. Commissioner, 19 TC 11146 (1953)*, The American Automobile Association (also known as "Triple A" or AAA) was held not to be exempt as a business league under section 501(c)(6) of the Code. This national association of individual

automobile owners and affiliated auto clubs has broad purposes to improve highway traffic safety and to educate the public in traffic safety. However, the court concluded that its principal activities were to secure benefits and perform particular services for its members.

In the case *Associated Master Barbers & Beauticians of American, Inc. v. Commissioner, 69 T.C. 53 (1977 U.S. Tax Ct.)*, the purposes and activities of an organization were analyzed to determine whether the organization would qualify for exemption under section 501(c)(6) of the Code. Among the rulings from the court, one found and concluded that the bulk of the activities performed by the organization during the years at issue did not contribute to the improvement of business conditions in one or more lines of business but were the performance of particular services for individuals. The organization offered various insurance programs for its members and other benefits such as eyeglass and prescription lens replacement services, sales of supplies including styling charts, appointment books, and hair products. It also sold to the members shop emblems and association jewelry, textbooks and hairstyling books. The court ruled that because the above activities serve as a convenience or economy to the organization's members in the operation of their businesses, such activities constitute "particular services." If the organization did not provide these goods and services, its individual members would have to obtain them from nonexempt businesses at a substantially increased cost.

In the case *Southern Hardwood Traffic Association v. United States of America, 283 F. Supp. 1013 (1968 U.S. Dist.)*, the court determined whether some of the organization's activities that were considered the performance of particular services to its members was more than incidental to its other activities taken as a whole. In addition to its many other services that were found to be general in nature and which promoted the common interests of the industry as a whole, the organization offered (and charged a fee for) some services to its members who requested them, including rate quotes, bills of lading, tracing and reconciling shipments, and collecting claims and refunds on behalf of the requesting members. The court stated that any particular activity or service performed, which does not inure to the benefit of all of its members generally and which would otherwise have to be done by or for the member in order for him to properly perform his business, must be classified as an individual service. The court determined a more appropriate method of determining whether the individual services performed by this organization are incidental to its alleged "main" purposes. The court found the more appropriate method was to calculate the amount of time devoted by the employees of the organization to perform the individual services compared to the amount of time the employees devoted to those services that are of common interest and equal benefit to all of the members. In this case the court found that the amount of time spent by the employees of the organization providing the above-described individual services

requested by its members was a substantial part rather than an incidental part of its total activities. Thus, with a substantial part of the organization's activities constituting the performance of particular services to individuals, exemption under section 501(c)(6) of the Code was not allowed.

In the case *United States of America v. Oklahoma City Retailers Association, 331 F.2d 328 (1964 U.S. App.)*, the court reversed earlier decisions and also rejected a jury's decision regarding exemption for the above organization. Incorporated in 1916, the association had maintained a credit rating bureau for the exclusive use of its members. Membership was available to approved persons, firms and corporations located and engaged in business in the city. The organization charged a fee to each member requesting a credit rating inquiry. Almost all of the organization's (employees') time was spent and income received from conducting the credit rating activity. The court ruled that the association chiefly performed 'particular services for individual persons,' namely, the supplying of credit information to some but not all of its members. It also furnished the same services to non-members and charged the same fixed fee as required of members. Such activity, being a substantial activity of the organization, does not warrant exemption for the organization under section 501(c)(6) of the Code.

In the case *Evanston-North Shore Board of Realtors v. The United States, 162 Ct. Cl. 682; 320 F.2d 375 (1963 U.S. Ct. Cl.)*, the court ruled that the addition of a multiple listing service activity, which the court determined became a primary activity of the organization, caused the organization to lose its tax exempt status under section 501(c)(6) of the Code. This multiple listing activity was not regarded by the court to be directed to the improvement of business conditions in the real estate market, but rather constituted the performance of a particular service for brokers participating in the service. The multiple listing service was found to be operated primarily for the individual members as a convenience and economy in the conduct of their respective real estate businesses.

In the case *Produce Exchange Stock Clearing Association, Inc. v. Helvering, 71 F.2d 142 (1934 U.S. App.)*, the court ruled whether an activity that was provided to its members advanced the interests of the community and thus would be considered within the allowances for exemption from tax or whether the activity directly benefited the members. The law in this ruling was the predecessor to section 501(c)(6) of the Code but still had the same stipulations that the activities advance the interests of the community, or improve the standards or conditions of a particular trade. The clearing service was provided to aid member traders in their security dealings. Such service was determined to merely be a convenience or economy in their businesses. Thus, exemption from tax was not allowed to the organization that primarily provided this service.

Application of the Law

Your activities would be considered providing services to or on behalf of your members. The Regulations for section 501(c)(6) of the Code clearly states that exemption is not allowed for organizations providing particular services to individuals. In addition, your membership represents no common business interests, other than the common desire to lower health benefit costs experienced by both employers and employees. Your cooperative sharing and pooling of covered employees to better spread the risks and costs of health care is not an activity that promotes any particular industry as a whole as required by the Code and Regulations, but results in economies to individual member businesses that ultimately improve their businesses' profits. Thus, your sole purpose and the activities conducted to accomplish this purpose, would not meet the exemption requirements and stipulations under section 501(c)(6) of the Code and Regulations.

A comparison can be made between you and those described in Revenue Rulings 81-174, 81-175, and 74-81 in the type of activities provided and the purpose of their activities. They are dissimilar, however, in that you do not actually provide the insurance products to your members (i.e. assume the risk involved in providing insurance). Nonetheless, the organizations in the rulings are clearly providing a benefit to their members that allows them to enjoy lowered risks and therefore costs (in their own insurance businesses). Their spreading of the risks and costs creates a convenience to their members and an economy to their businesses. The rulings conclude such economies are a service to them. You conduct an activity that similarly creates an economy for your members that lowers their business costs. It also provides them with a more attractive (health) benefit that they can offer their employees. Not only would this economy be considered a service according to the rulings, but the additional activities you conduct are also considered services - the administrative billing services, customer service, grievance tracking and settlement between employees and carriers, and State regulation compliance reporting. The member entities would have to be doing all of these on an individual basis if it weren't for you conducting them on their behalf. It is clear you are providing services to individuals, which is precluded in exemption under section 501(c)(6) of the Code.

You are distinct from the association in Revenue Ruling 71-155 where exemption was allowed. The first difference is in the membership requirements. The association in Revenue Ruling 71-155 required all insurers of a particular insurance to be members and thus share in the equitable distribution of the high-risk policies of that particular insurance coverage. Their membership therefore represented the entire population of insurers for that specified type of insurance and their activity equally benefited that particular segment of the industry as a whole. You define and restrict your membership to lucrative small businesses whose employee numbers will be a benefit to

the pooling of employee coverage. Small businesses that do not meet your criteria do not benefit from your activities. The second difference between you and the association described in Revenue Ruling 71-155 is that there is no particular industry that benefits from the activities, other than general commerce. And with the limits and restrictions to your membership, not all businesses benefit directly from your activities, only those meeting certain requirements and participating. Therefore, it cannot be said that your activities are meant to improve the conditions of any one particular line of business or even the entire business community, only participating members' businesses. And because not all businesses can benefit from your activities (only your selected and qualifying membership), the benefits cannot be said to be incidental, where in order to meet the state regulations everyone benefits equally.

A benefit to members in the organization versus benefits to members of an entire industry is also the key factor in the determination made in Revenue Ruling 69-106. The ruling concluded that since only members could receive the research results (where it is assumed they could use it advantageously over those who do not have access to such research results) the organization was providing services to its members. If the organization had provided its research to everyone in the industry, regardless of a membership in the organization, a different conclusion about its motives could be reached. Instead, a conclusion was drawn that the activities serve the more personal interests of its members. Your benefits are directed and limited only to members and therefore a similar conclusion is drawn: you are providing a beneficial service to your members.

Further similarities are found in Revenue Rulings 68-264, 66-338, and 56-65 in your activities and those of the organizations in the rulings. The activities of the organizations in the rulings assist their members in the conduct of their own individual businesses. The rulings concluded that such assistance would be considered providing services to individuals that creates conveniences and economies. As these activities constituted their primary activities and purposes, exemption was not allowed under section 501(c)(6) of the Code. Your pooling of employees' health benefit coverage creates cost savings and economies in the individual members' businesses. Following the rulings, this assistance in lowering their costs would be considered providing services to the members.

Your purposes are very similar to those found in Revenue Ruling 59-391 where exemption under section 501(c)(6) of the Code was not allowed because the association had no common business interest, a required characteristic to section 501(c)(6) organizations. The membership of the association in the revenue ruling was made up of individuals from various businesses. The ruling found that the only common business interest and purpose to their activities was the mutual desire to increase their individual sales. Such an individual

benefit is not allowed in organizations exempt under section 501(c)(6) of the Code. Your purpose and activities are a similar mutual desire: to lower (health benefit) costs thereby making it more affordable for such coverage to be offered to member businesses' employees.

You are distinct from the findings in Revenue Ruling 65-164 because the negotiations you conduct are to procure the more advantageous health benefits for small employers. Small employers can obtain health benefit services (coverage) on their own. But as your member, they are able to experience lower premium costs through the pooling of their employee counts and risk factors with numerous other small business employer members. The negotiations result in a direct benefit of lower health benefit costs to members and their employees. The ruling emphasized when individual members derive a direct and non-incidental benefit from the services rendered (by the organization), exemption would not be allowed. Any services provided by the organization must further the common interests of the membership as an industry-wide group. In the ruling, any individual benefits the members in the organization received from the labor negotiations the organization conducted were incidental to the overall purpose of the negotiations, that being the successful fulfillment of labor agreements in the industry. The ultimate individual member benefits were simply better labor relations between employers and employees.

In all of the court cases described above, the courts concluded that activities which individually assist, benefit, and/or provide a convenience to members or individuals in the conduct of their own businesses were considered performing particular services to individuals rather than improving business conditions within a common industry. Exemption under section 501(c)(6) of the Code was not allowed these organizations because the particular services provided were found to be the primary activities and not incidental to the purposes of the organizations. Your activities are similar to those described in the court cases. The pooling of covered employees for each member and negotiating for health benefit coverage based upon this pooling, results in a cost savings for members. As such, it would be considered a service provided to the members. The administrative and other services provided to maintain the health benefit coverage is also clearly considered services provided to or on behalf of the members. If you were not doing these activities for the members, they would have to do them and incur costs on their own. And, similar to the court cases, the above activities are your primary activities; therefore, following the decisions in the court cases, exemption under section 501(c)(6) would not be allowed.

Applicant's Position

You have addressed your position to the portions of section 501(c)(6) of the Code that restrict the net earnings of an organization from inuring to the benefit of private shareholders or

individuals and that restrict an organization from being organized for profit or organized to engage in activities ordinarily carried on for profit. You stipulate that by the state regulations you are required to be organized as a nonprofit entity and that no distributions or payments of a dividend or any part of the income or profit is allowed to your members, directors, or officers (except as reasonable compensation for services rendered). In addition, the state regulations restrict the presence of a financial interest in your financing, marketing, or delivery of services. Thus, with these state-mandated restrictions, you are prevented from allowing your earnings to inure to the benefit of private shareholders or individuals.

You have also explained that an entity with your purposes and activities has not been in existence until only recently when defined by the Insurance Commissioner of the state of N. Therefore, your activities have not "ordinarily been carried on" until the recent enactment of the state law. And to clarify further, you stated your activities are not the provision of insurance, which would be an activity ordinarily carried on for profit, and you are not considered an insurance agent. In fact, the state law prohibits you from providing insurance or bearing any risk associated with any health benefit plan or other insurance.

You explain the intension of the state regulations to form cooperatives like yours is for "the improvement of business conditions of multiple lines of business." The state law is attempting to make health care coverage available to more private citizens to avoid the state from having to bear the financial costs of heath care provided to those not covered by health benefits. Since more and more small businesses are not financially able to pay for health care benefits for their employees, more and more of the working people are without health care coverage. If or when health crises occur for these non-covered workers, the state are responsible for the costs. The cooperatives are allowed to pool together multiple businesses' employees to obtain the volume of covered lives similar to public employees health coverage plans and experience the lower costs realized from risk spreading in large volumes. This idea allows the private citizens of the state to have the same chance of affordability of health care, and other employee benefits, as the public sector has with its state, federal, and labor union collectively bargained benefits. Finally, because the cooperatives cross all business lines, include both for-profit and non-profit entities, and cover large geographic zones that span across multiple counties within the state, their services are provided to a "community" much broader than what a 'chamber of commerce' in a county or municipality could cover.

You explain further how employee benefit structures for the working employee is a major significance for the citizenry of our country and is an important need in our communities. The ability of our community to attract good workers and provide for the betterment

of our community is dependent on employee benefit structures. However, the costs of health plan benefits are almost beyond affordability in the private sector. Thus, your purpose is to mirror the state and federal entities' benefit programs in order to reduce costs and allow more of the community's citizenry into covered health plans. The more these benefits are affordable to private citizens the lesser the number of citizens that will enter the "uninsured" lines of the state and become the responsibility of the state and federal governments.

Service Response to Applicant's Position

We have not disputed that you were established as a nonprofit corporation with the required stipulations that earnings and distributions would not be made to officers, directors, or shareholders. We would also agree that you are not providing insurance, you are not considered an insurance agent, nor are you assuming any risk associated with administering insurance and are therefore not operating an insurance activity in a manner ordinarily carried on for-profit. However, while the idea of a 'health plan purchasing cooperative' as created by the state of N appears to be a new idea and because of its newness any current operation cannot be considered "ordinarily" carried on, we would disagree. You have taken that phrase out of its context as it is used in defining what an organization exempt under section 501(c)(6) of the Code can or cannot do. Basically, it cannot operate in a similar manner as, or conduct similar activities as, entities designed to operate with the intension to make a profit. "Ordinarily carried on" is only a reference as to what is usually expected, not that it (a profit) always occurs or is even meant to occur. The Regulations even add situations where the business is conducted on a cooperative basis or that produces only sufficient income to be self-sustaining as prohibitive. The "newness" of an idea should have no affect on determining whether the activities conducted compare to other activities "ordinarily carried on."

While the intent and outcome of your pooling of employee coverage would ultimately mean that more employees (and public citizens) in the private sector are covered by health benefits (a current public concern), the fact that your membership is limited prevents a purpose allowed exemption under section 501(c)(6) of the Code. In your case your membership restrictions are an indication that you operate to serve only your members. In addition, the "non" limitation of your membership to any particular line of business or particular industry prevents you from having activities that would be considered improving conditions within a particular industry or line of business as required by the Code and Regulations under section 501(c)(6). We agree that your activities ultimately benefit a "community" much larger than single cities or towns within the state and that your benefits are certainly meant to go beyond serving only certain industries or lines of business. However, this broad coverage is

beyond what the statute allows for organizations exempt under section 501(c)(6) of the Code. Finally, the activities you conduct provide your members with economies and conveniences in conducting their own businesses; the provision of such would be considered providing particular services to your members, which is another preclusion to exemption under section 501(c)(6) of the Code.

Conclusion

Your activities are considered activities normally carried on for a profit (the administrative services to maintain health benefits for your members). In addition, the provision of the administrative services and the negotiations for the health benefit plans (as well as other employee benefits) would be considered the performance of particular services for your members. These services provide your members with a convenience and an economy in the conduct of their own individual businesses that results in savings and simplified operations. Your members are able to secure health insurance more cheaply than if they were to secure such on their own. Several of our rulings conclude that such economies and conveniences constitute the performance of particular services for the individual members as distinguished from activities aimed at the improvement of business conditions in a particular trade or industry. Furthermore, since your membership is not limited to any particular industry, the activities cannot be considered an improvement of the business conditions in a particular industry as required under section 501(c)(6) of the Code. The health plan (and other employee benefit) negotiations and administrative services are your primary activities and purposes; therefore, exemption would not be allowed under section 501(c)(6) of the Code.

Issue 2

If M is determined to not qualify for exemption under section 501(c)(6) of the Code, does it qualify for exemption under section 501(c)(4) of the Code?

Facts

[The facts are the same as described in Issue 1.]

Applicable Law

Section 501(c)(4) of the Code provides in part for the exemption from Federal income tax of civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare.

Section 1.501(c)(4)-1(a)(2)(i) of the Regulations states that an organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community and bringing about civic betterment and social improvements.

Section 1.501(c)(4)-1(a)(2)(ii) of the Regulations provides that an organization is not operated primarily for the promotion of social welfare if its primary activity is carrying on a business with the general public in a manner similar to organizations that are operated for profit.

In Revenue Ruling 70-535, 1970-2 C.B. 117, exemption under section 501(c)(4) of the Code was not allowed an organization that provided managerial, developmental, and consultative services to other entities involved in low-income housing projects. The ruling concluded that the organization's primary activity was a business activity - that of managing low-income housing projects in a manner similar to organizations operated for profit. It was not operated primarily for the promotion of social welfare and therefore did not qualify for exemption under section 501(c)(4) of the Code.

Revenue Ruling 73-349, 1973-2 C.B. 179, denied exemption under section 501(c)(4) of the Code to a grocery cooperative. The organization was formed to purchase groceries for its membership at the lowest possible prices on a cooperative basis. It received orders from its members, consolidated them and purchased the food in quantity. Membership was open to all individuals in a particular community. Despite the open membership, the ruling concluded that the organization was operated primarily for the private benefit of its members and any benefits to the community were not sufficient to meet the requirements of the regulations that the organization be operated

primarily for the common good and general welfare of the people of the community.

In Revenue Ruling 54-394, 1954-2 C.B. 131, an organization that provided television reception antenna service only to its members on a cooperative basis was found not exempt as a civic league under the section of the Code that preceded section 501(c)(4). Such an organization was held to be operating for the benefit of its members.

The above facts in Revenue Ruling 54-394 were compared to an organization described in Revenue Ruling 62-167, 1962-2 C.B. 142, and found to differ distinctly enough to allow exemption under section 501(c)(4) of the Code. The organization in Revenue Ruling 62-167 provided television reception service in a manner that was available to the entire community, not just those that paid a membership fee and regular monthly maintenance charges. Therefore the manner in which the services were made available to users created the distinction between serving the community and meeting exemption under section 501(c)(4) of the Code and serving only members or certain individuals where exemption was precluded under section 501(c)(4) of the Code.

Application of the Law

As noted in Revenue Rulings 73-349 and 54-394, cooperative activities serve to benefit only those participating members. Organizations meeting exemption under section 501(c)(4) of the Code must have activities that benefit the community as a whole, not a set or defined group. Your cooperative purchasing and negotiating to acquire health benefits for your member's employees serves your individual members. Since membership restrictions limit the businesses in the community that can participate in the cooperative nature of your activities, it cannot be said that the community as a whole benefits.

Also, our position discussed for Issue 1 regarding your activities being considered providing services to your members remains the same. In addition to the health plan negotiations you conduct on behalf of your members, you conduct administrative billing services, customer service, grievance tracking and resolution services, and State regulation compliance reporting for your member businesses. If it were not for your providing these services, your members would have to either conduct them themselves or contract out for such services. Providing services is a business activity as concluded in Revenue Ruling 70-535 and if conducted in a manner similar to for-profit entities (regardless if a profit is actually realized) exemption under section 501(c)(4) of the Code is precluded. You do receive fees for the administrative services and other services you provide not unlike any other service provider and similar to the organization in Revenue Ruling 70-535. Therefore, exemption under section 501(c)(4) of the Code would not be allowed.

Applicant's Position

You did not request exemption under any other section of the Code; however, this section of the Code was considered if exemption would not be allowed under section 501(c)(6) of the Code.

Conclusion

Your activities and purposes serve the individual needs of your membership rather than benefit the community as a whole. Since your membership is restrictive and limited to certain businesses, not all business within a community can benefit from your activities. Therefore, your activities and purposes do not promote the common good of the community as a whole. In addition, you conduct administrative services in a manner similar to entities that operate for a profit. As the administrative services and services to your members are your primary activities, exemption under section 501(c)(4) of the Code would not be allowed.