

# **Bond Case Briefs**

*Municipal Finance Law Since 1971*

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## **IRS LTR: IRS Denies Tax Exemption to Shareholder Organization.**

Citations: LTR 201329024

The IRS denied tax-exempt status to an organization formed to promote shareholders' interests in publicly traded companies, finding that its activities don't improve business conditions along one or more lines of business or of a certain area but rather are services for member convenience.

Person to Contact: \* \* \*

UIL: 501.06-00, 501.36-00

Release Date: 7/19/2013

Date: April 26, 2013

Taxpayer Identification Number: \* \* \*

Tax Period(s) Ended: \* \* \*

Dear \* \* \*:

We considered your appeal of the adverse action proposed by the Director, Exempt Organizations, Rulings and Agreements. This is our final determination that you do not qualify for exemption from Federal income tax under Internal Revenue Code (the "Code") section 501(a) as an organization described in section 501(c)(6) of the Code.

Our adverse determination was made for the following reason(s):

You are not described within the purview of section 501(c)(6) of the Code because your purpose, as stated in the Restated Articles of Incorporation, is to restore and then maintain appropriate and effective control of shareholders over the US corporations they own.

Your membership consists of individual investors of equity investment firms who wish to preserve and strengthen their shareholder rights.

You are required to file Federal income tax returns on Forms 1120 for the tax periods stated in the heading of this letter and for all tax years thereafter. File your return with the appropriate Internal Revenue Service Center per the instructions of the return. For further instructions, forms, and information please visit [www.irs.gov](http://www.irs.gov).

Please show your employer identification number on all returns you file and in all correspondence with Internal Revenue Service.

You also have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance

is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States Court. The Taxpayer Advocate can however, see that a tax matters that may not have been resolved through normal channels get prompt and proper handling. If you want Taxpayer Advocate assistance, please contact the Taxpayer Advocate for the IRS office that issued this letter. You may call toll-free, 1-877-777-4778, for the Taxpayer Advocate or visit [www.irs.gov/advocate](http://www.irs.gov/advocate) for more information.

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

Sincerely Yours,

Karen A. Skinder

Appeals Team Manager

\* \* \* \* \*

Contact Person: \* \* \*

Identification Number: \* \* \*

Contact Number: \* \* \*

FAX Number: \* \* \*

UIL 501.06-00, 501.36-00

Date: August 2, 2012

Employer Identification Number: \* \* \*

LEGEND:

C = individual

J = business

P = state

u = date

y = year

w = dollar amount

x = dollar amount

y = dollar amount

Dear \* \* \*:

We have considered your application for recognition of exemption from federal income tax under

Internal Revenue Code ("Code") section 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under Code section 501(c)(6). The basis for our conclusion is set forth below.

This letter supersedes our letter dated September 20, 2011

## ISSUE

Do you qualify for exemption under section 501(c)(6) of the Code? No, for the reasons stated below.

## FACTS

You are a corporation formed on u, and operate pursuant to the laws of the State of P. Your Articles of Incorporation state that your purpose is to restore and then maintain appropriate and effective control of shareholders over the US corporations they own. Your Articles of Incorporation also state that you shall not carry on any activities not permitted to be carried on by a corporation exempt from federal income tax under section 501(c)(6) of the Internal Revenue Code, or the corresponding section of any future federal tax code.

You initially applied for exemption under IRC 501(c)(3), then re-applied under IRC 501(c)(6). You state that you are a chamber of commerce with shareholders of various unrelated corporations as members that seek to improve business conditions for publicly traded US corporations by enhancing the effectiveness with which shareholders contribute to running those corporations. To accomplish this goal, you conduct the following activities:

You organize collective action by shareholders on matters pertinent to effectively running the corporation they own through virtual shareholder meetings, where the organized shareholders pressure public corporations to use remote communications technology in shareholder meetings such as online forums. This work is conducted by your membership — perhaps with leadership by your board or officers — primarily out of their homes. It will consume about \* \* \*% of your time.

You advocate for effective legislation and regulation. Examples of this work include the letters you sent to the SEC in v to comment on proposed regulations on behalf of shareholders. These letters were primarily written by your executive director working out of his office, but many shareholders contributed to and co-signed the letters. This will consume about \* \* \*% of your time.

You organize conferences, media events, rallies or other events that draw attention to critical issues affecting shareholders' ability to effectively run the corporations they own. This work is conducted by your membership — perhaps with leadership by your board or officers — primarily out of their homes. It will consume about \* \* \*% of your time.

You improve shareholders ability to effectively run the corporations they own by helping shareholders engage qualified proxies, agents or board members to represent their interests. While you have facilitated a number of grants of proxies in the past, these efforts will be advanced through implementing social networking software. You have a team of volunteer information technology professionals who will implement that technology. The general membership will also be engaged, with direction from your officers. Work is conducted primarily from members' homes. It will consume about \* \* \*% of your time.

You improve shareholders ability to effectively run the corporations they own by mitigating the risk of frivolous corporate lawsuits against shareholders who exercise their rights or responsibilities as owners of corporations. This work entails securing legal advice for shareholders who are sued by corporations. You have, for example, been assisting shareholder C who was sued by J over a

shareholder resolution he submitted for inclusion in that corporation's 2010 proxy materials. You will also form a legal defense trust for shareholders who are victimized by such lawsuits. This work is conducted by your membership — perhaps with leadership by your board or officers — primarily out of their homes. It will consume about \*\*\*% of your time.

Your members are owners of various unrelated publicly traded US corporations who share a common business interest of improving the effectiveness with which the corporations they own are managed. Currently, your members consist solely of your board members. Your membership requirements, duties, and privileges are as follows:

You distinguish members who have not yet reached the age of majority.

You grant full voting rights only to members who have demonstrated commitment to your cause.

You separate classes of membership for shareholders who are natural persons and shareholders that are institutions.

You grant honorary — non-voting — memberships to certain parties, such as academics or service providers who are not shareholders but have knowledge or expertise that could be useful to your organization.

You grant non-honorary membership only to shareholders. Individuals are considered shareholders if they satisfy either the first or both the second and third of the following criteria:

Currently owns at least \$\*\*\* in publicly traded US equities, either directly or indirectly, through a mutual fund or other pooled investment vehicle.

Has owned at least \$\*\*\* in publicly traded US equities in the past, either directly or indirectly, through a mutual fund or other pooled investment vehicle.

Will very likely own at least \$\*\*\* in publicly traded US equities within the next three years, either directly or indirectly, through a mutual fund or other pooled investment vehicle.

An institution is considered a shareholder if it is an institutional investor that routinely invests \*\*\*% or more of its portfolio in publicly traded US equities, either directly or indirectly, through mutual funds or other pooled investment vehicles.

You have nine classes of members that include:

Nominal individual — an individual of any age who is not a shareholder. This honorary membership provides member benefits but no voting rights.

Junior individual — an individual who is a shareholder but has not yet reached his 18th birthday. This membership provides member benefits but no voting rights.

Associate individual — an adult shareholder who has not been promoted to general member. This membership provides member benefits but limited voting rights on policy issues, as permitted by the board.

General institutional — an associate institutional member can be promoted to general institutional member in recognition of service and commitment to the organization. Provides for full voting rights.

Nominal charitable — Essentially nominal institutional membership but for a 501(c)(3). Membership dues are lower.

Associate charitable — Essentially associate institutional membership but for a 501(c)(3). Membership dues are lower.

General charitable — Essentially general institutional membership but for a 501(c)(3). Membership dues are lower.

Membership dues are:

w dollars a month for all individual memberships

x dollars annually for institutional memberships

y dollars annually for charitable memberships

You have estimated membership to be the following:

Year 1: approximately 20 individual, 2 institutional, 2 charitable

Year 2: approximately 30 individual, 4 institutional, 4 charitable

Year 3: approximately 40 individual, 6 institutional, 6 charitable

## LAW

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

Section 1.501(c)(6)-1 of the Income Tax Regulations states, “A business league is an association of persons having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of the kind ordinarily carried on for profit. It is an organization of the same general class as a chamber of commerce or board of trade. Thus, its activities should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons. An organization whose purpose is to engage in a regular business of a kind ordinarily carried on for profit, even though the business is conducted on a cooperative basis or produces only sufficient income to be self-sustaining, is not a business league.”

In Revenue Ruling. 59-391, 1959-2 C.B. 151, exemption under 501(c)(6) was denied to an organization composed of individuals, firms, associations, and corporations, each representing a different trade, business, occupation, or profession. The organization was created for exchanging information on business prospects and has no common business interest other than a desire to increase sales of members. The revenue ruling found that the members of the instant organization had no common business interest other than a mutual desire to increase their individual sales. It stated that the organization’s activities were not directed to the improvement of business conditions of one or more lines of business, but rather to the promotion of the private interests of its members.

In Revenue Ruling 67-176, 1967-1, CB 140, the organization was formed to advance a given profession, contribute to the welfare and education of students preparing for that profession, to

furnish financial aid to that profession in the form of grants and loans and to do other things for the benefit, welfare and security of its members. The ruling found that the emergency loan plan, among other activities served primarily as a convenience and for the economy of the members in providing financial aid, which is found to be the performance of particular services to members as opposed to improving a line of business. Thus, exemption under section 501(c)(6) was not afforded to the organization.

In Revenue Ruling 76-38, 1976-1 C.B. 157, the organization in question was formed to maintain the goodwill and reputation of the credit unions in a particular state. To achieve this goal, they maintained a fund for assistance to credit unions having financial difficulty to keep them solvent so that their members would not lose deposits upon liquidation. They allowed member credit unions to take interest free loans from the fund. The loans were to be repaid only if the borrowers were financially able to do so. The ruling found that the loan activities were not solely calculated to accomplish the objective of improving the industry's image by protecting depositors. Further, the favorable terms of the loans to members was done in a manner that would provide little or no additional security to depositors and is clearly for the convenience (and economy) of the members in their business and does not constitute an exempt activity under section 501(c)(6).

In MIB, Inc. v. Commissioner, 734 F.2d 71 (1986), an organization whose membership consisted of insurance companies was denied exemption as a business league under section 501(c)(6) of the Internal Revenue Code. The principal activity carried on by MIB was the maintenance and operation of a computerized system for compiling, storing and distributing information about applicants for life insurance. MIB argued that its activities created a deterrent to fraud, which created benefits to the industry through reduced investigation expenses and reduced losses due to misclassification of applicants. The Court held MIB's activities by their nature consisted of rendering particular services for individual member companies and served to benefit the individual members' businesses. The Court also stated that even though the services produced various indirect and intangible benefits for the industry as a whole, the fact remained that the rendered services were in form and substance particular services for individual member companies. According to the Court in this case, the ultimate inquiry is whether the association's activities advance the members' interests generally, by virtue of their membership in the industry, or whether they assist members in the pursuit of their individual businesses.

## APPLICATION OF THE LAW

You are not described within section 501(c)(6) of the Code as you are not a business league, chamber of commerce, real-estate board, board of trade, or professional football league. You are instead an entity that promotes shareholders' interests in publicly traded corporations.

You are not operated as described in section 1.501(c)(6)-1 of the regulations because your activities are not directed to the improvement of business conditions of one or more lines of business. Rather, your activities provide particular services for individual persons. Additionally, because of the nature of your activities, you do not have a line of business to improve. Your members are individuals and institutions who are in various occupations and business. The only common interest is protecting and improving stockholders' rights. All of your activities consist of promoting the exercise of the rights of shareholders of publicly traded corporations and offering members legal advice. Such programs constitute a particular service to individuals because you vote on behalf of the individuals who delegate their rights to you and provide legal advice to the shareholder who are in litigation with publicly traded corporations.

You state that you are improving the common interest of your member organizations that consist of economic and community development; thus, you qualify for exemption under section 501(c)(6) of

the Code. However, there is no common interest since your members own shares of various publicly traded corporations that conduct all kinds of business. There is also no defined geographic area for the improvement of business conditions for a certain area because your members and the stock corporations are all over the world. Like Revenue Ruling 59-391, you are an organization composed of individuals, firms, associations, and corporations, each representing a different trade or business, having no common business interest other than to advocate for shareholder rights. For these reasons you do not meet the qualifications for a 501(c)(6) entity.

The organizations in Revenue Rulings 67-176 and 76-38, above, ran a fund for their members. The rulings conclude that it is the performance of particular services to members as opposed to improving a line of business since it is for the convenience and economy of the members. You are providing a specific service to your members through your programs. You provide direct services to your members for their convenience and economy because your purpose is to maximize members' voice as a shareholder for the company in which the member owns stocks.

In *MIB, Inc. v. Commissioner* the Court found that even though services produced various indirect and intangible benefits for the industry as a whole, the fact remained that the rendered services were in form and substance particular services for individual member companies. Even if your programs bring some general benefits to the industry under which the companies perform, or benefits to various companies themselves operating under a common line of business, it still holds that programs and services are performed first to benefit your members. In advocating for shareholder rights you are benefitting members specifically, not generally, in pursuing their own interests. Because of this any indirect benefit to the industry does not overcome your main purpose of providing individualized service to members.

#### PROTEST FROM APPLICANT

You protested our initial adverse ruling in that first, certain facts were not accurate and second, you disagreed with the application of relevant law.

Regarding bullet point five, above, Facts section, you have indicated that you have not and will not provide legal services. Rather, you have petitioned for and prepared amicus curiae briefings, in this instance, regarding the case against C. You were not representing C, but were instead submitting protest to a position you felt could harm you or any U.S. shareholders. Any benefit received on the part of C was incidental and not intentional. You have filed no other briefs, but will do so in the future if the need arises. You have also canceled any attempt at forming any form of legal defense fund.

Regarding our positions stated in the Application of Law section, you disagree with the statement that you do not improve any line of business. The line of business you improve is that of equity finance of corporations and for investment by equity shareholders. You have cited the case of *Associated Industries of Cleveland v. Commissioner*, 7 TC 1449 (1946) in arguing your members share a common business interest. Petitioner in this case was an association of persons, firms and corporations with offices in Cleveland, OH, meeting to consider labor problems and difficulties confronting industry in that city following the first World War. Petitioner was a business league; members cooperated to employ labor under circumstances deemed advantageous.

You disagree with the position that your activities are not improving business conditions but are instead providing particular services to members. Your efforts are devoted towards communication among shareholders, and facilitating this communication is not a service to members but improves business conditions.

You disagree with the position that you have no defined geographic area in improving business. You focus exclusively on improving business conditions for equity investment in U.S. corporations.

You cited three other entities, all of which are exempt under 501(c)(6), and indicated similar goals and agendas, missions and operations.

#### SERVICE RESPONSE TO PROTEST FROM APPLICANT

Removing the activity of securing legal advice for shareholders does not change the primary reason for which you are formed, as this made up only \* \* % of your total activities. The submission of briefs, which may serve to benefit your position or that of other shareholders, still serves no common business interest nor improves any particular line of business. The changing of this initial fact does not alter the position on our ruling.

You are different from the organization in Associated Industries in that you are advocating for all shareholders across the U.S, rather than employers in a particular city, and your members are individuals who hold stock in any company whereas the members of the organization in Associated Industries were workers and owners of businesses in one geographic area.

While you are improving communication among shareholders, this in and of itself improves no particular business conditions. It serves as a service to your members allowing them to share responsibility in serving proxies, when needed, and acting in place when they are unable to be personally present to protect or represent their interests.

The particular geographic area is not determinate in this particular case. Instead, it is the fact you are composed of individuals, firms, association and corporations, each representing a different trade or business, having no common interest other than to advocate for shareholder rights.

Regarding the entities you referenced currently exempt under 501(c)(6). The qualification of another entity is not a basis for a similar ruling as each application for exemption is determined on its own merits.

#### CONCLUSION

Based on the information submitted, your primary purpose is to promote shareholders' interests in publicly traded corporations and provide legal advice to your members. Such activities do not improve business conditions along one or more lines of business or of a certain area but instead are services for the convenience of your members. Therefore, you do not qualify for exemption under IRC 501(c)(6).

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter.

We will consider your statement and decide if that information affects our determination. If your statement does not provide a basis to reconsider our determination, we will forward your case to our Appeals Office. You can find more information about the role of the Appeals Office in Publication 892, Exempt Organization Appeal Procedures for Unagreed Issues.

Types of information that should be included in your appeal can be found on page 2 of Publication 892, under the heading "Regional Office Appeal". The statement of facts (item 4) must be declared true under penalties of perjury. This may be done by adding to the appeal the following signed declaration:



"Under penalties of perjury, I declare that I have examined the statement of facts presented in this appeal and in any accompanying schedules and statements and, to the best of my knowledge and belief, they are true, correct, and complete."

Your appeal will be considered incomplete without this statement.

If an organization's representative submits the appeal, a substitute declaration must be included stating that the representative prepared the appeal and accompanying documents; and whether the representative knows personally that the statements of facts contained in the appeal and accompanying documents are true and correct.

An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you during the appeal process. To be represented during the appeal process, you must file a proper power of attorney, Form 2848, Power of Attorney and Declaration of Representative, if you have not already done so. For more information about representation, see Publication 947, Practice Before the IRS and Power of Attorney. All forms and publications mentioned in this letter can be found at [www.irs.gov](http://www.irs.gov), Forms and Publications.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter to you. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to the applicable address:

Mail to:

Internal Revenue Service

EO Determinations Quality Assurance

Room 7-008

P.O. Box 2508

Cincinnati, OH 45201

Deliver to:

Internal Revenue Service

EO Determinations Quality Assurance

550 Main Street, Room 7-008

Cincinnati, OH 45202

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

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

Sincerely,

Holly O. Paz

Director, Exempt Organizations

Rulings and Agreements

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