

Rules of Conduct of 501(c) 5- Activities that Jeopardize Exemption

A labor organization is an association of workers who have combined to protect or promote their interests by bargaining collectively with their employers to secure better working conditions, wages, and similar benefits. Similar benefits include benefits traditionally provided by labor organizations such as strike, lockout, death, sickness, accident, and other benefits. Labor organizations need not be recognized labor unions. An organization does not qualify for exemption if its net earnings inure to the benefit of any member.

A labor organization will jeopardize its exemption under Code section 501(c)(5) if it ceases to have as its purposes bettering the conditions of persons engaged in the pursuit of labor; improving the grade of their products; and developing a higher degree of efficiency in their occupations. In addition, an organization's net earnings may not inure to the benefit of its members. These organizations may conduct political campaign and lobbying activities furthering their exempt purposes, but may have to pay a proxy tax if they use member dues for this purpose.

Below are three major categories of activities that can jeopardize a trade association exemption status. They include:

- I. Inurement
- II. Political and Lobbying Activities
- III. Engaging in Business Activities

I. Inurement

An organization does not qualify for exemption if any of its net earnings inures to the benefit of any member. What is inurement of earnings to a member of an agricultural or horticultural organization may not be inurement of earnings to a member of a labor organization. For example, a labor organization may pay death, sick, accident, and similar benefits to members because paying such benefits serves the members' mutual interest in improving their shared working conditions.

In contrast, the exempt purposes of an agricultural organization are to better the conditions of those engaged in agricultural pursuits generally, rather than to benefit individual members specifically. Therefore, providing welfare aid and financial assistance to members is proscribed inurement for an exempt agricultural organization, but not for a labor organization.

Similarly, the concept of inurement under Code section 501(c)(5) differs somewhat from that applied under section 501(c)(3) and 501(c)(4).

Note, too, that members may receive incidental benefits from an organization's exempt activities. For example, members may benefit incidentally when an organization provides data on milk production to an agricultural extension organization. That incidental benefit is not inurement, although providing the same information only to members might be

- 1861 Wiehle Avenue, Suite 125, Reston, VA 20190
Tel: 703.437.8877 • Fax: 703.437.8937
- 10502 Crestwood Drive, Manassas, VA 20109
Tel: 703-365-8877 • Fax: 703-365-8937
- Email: info@millermusmar.com • www.millermusmar.com



II. Political and Lobbying Activities

An organization that otherwise qualifies for exemption under Internal Revenue Code section 501(c)(5) will not be disqualified merely because it engages in some political activity. In addition, these organizations may engage in lobbying that is germane to accomplishing their exempt purposes without placing their exemption in jeopardy. An organization that engages in these activities may need to give members notice of dues used for such activities, or be subject to a proxy tax on the amount of the expenditures.

III. Engaging in Business Activities

The following examples illustrate activities not furthering the exempt purposes of a labor organization under Code section 501(c)(5). If non-qualifying activities are an organization's principal activity, the organization may lose its exempt status.

1. Providing employment to members through a business activity.
2. An organization, created by an association of manufacturers and a labor union, that collected and paid to government agencies employment taxes.
3. A savings plan established pursuant to a collective bargaining agreement.
4. A strike fund controlled by private individuals who controlled the organization that paid benefits to workers.
5. An organization whose principal activity is managing funds associated with savings or investment plans or programs, including pension or other retirement plans. (see below).

A labor organization is not exempt under Code section 501(c)(5) if its principal activity is to manage savings or investment plans, including pension or other retirement savings plans or programs. This prohibition does not apply, however, to an organization that--

Is established and maintained by another section 501(c)(5) labor organization; Is not directly or indirectly established or maintained by one or more -

- a. Employers,
- b. Governments (or agencies or instrumentalities thereof), or
- c. Government controlled entities;

Is funded by dues from members of the labor organization that established or maintained it; and
Has not permitted or accepted employer contributions at any time after the enactment of the Employee Retirement Income Security Act (September 2, 1974).

If you would like additional information about this new filing requirement or information about other new developments, subscribe to Exempt Organization's contact MillerMusmar CPAs main office in Reston Virginia at 703-437-8877 or Manassas at 703-365-8877.

Please be advised that, based on current IRS rules and standards, the advice contained herein is not intended or written by the practitioner to be used and cannot be used by the taxpayer for the purpose of avoiding penalties.

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