



## Rules of Conduct of 501(c) 6- Activities that Jeopardize Exemption

A business league is an association of persons having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried on for profit.

To be exempt as a business league, an organization's activities must be devoted to improving business conditions of one or more lines of business (as distinguished from performing particular services for individual persons). It must be shown that the conditions of a particular trade or the interests of the community will be advanced. Merely indicating the name of the organization or the object of the local statute under which it is created is not enough to demonstrate the required general purpose.

No part of a business league's net earnings may inure to the benefit of any private shareholder or individual and it may not be organized for profit to engage in an activity ordinarily carried on for profit (even if the business is operated on a cooperative basis or produces only enough income to be self-sustaining).

To be exempt, a section 501(c)(6) organization must receive meaningful membership support.

Trade associations that meet the requirements of Internal Revenue Code section 501(c)(6) are exempt from federal income tax as business leagues. The same provision extends exemption to chambers of commerce, real estate boards, boards of trade, and professional football leagues.

During its existence, a tax-exempt business league has numerous interactions with the IRS – from filing an application for recognition of tax-exempt status, to filing the required annual information returns, to making changes in its mission and purpose. A trade association will jeopardize its exemption under section 501(c) 6 if it ceases to operate primarily to be a business league. Below are four major categories of activities that can jeopardize a trade association exemption status. They include:

- I. Engaging in Business Activities
- II. Performance in non-exempt services
- III. Inurement
- IV. Political and Lobbying Activities

### **I. Engaging in Business activities**

An organization whose primary purpose is to engage in a regular business of a kind ordinarily carried on for a profit is not a business league, and does not qualify for exemption under Internal Revenue Code section 501(c)(6). For example, the following have been found to be non-exempt business activities:

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1. Testing the safety of electrical products for commercial enterprises
2. Selling credit information and collection services
3. Employment agency
4. Providing commercial towing services for members of an automobile association
5. Laboratory services that are an organization's principal activity and only source of income
6. Providing insurance
7. Selling television advertising rights
8. Qualified Convention and trade Show Activities.

Qualified convention and trade show activities conducted by organizations exempt under section 501(c)(5) or 501(c)(6) are not unrelated trade or business if:

The activities are designed to attract persons to a show for the purpose of displaying or stimulating interest in and demand for the industry's products, or to educate persons engaged in the industry about new products or matters affecting the industry; and

The event is sponsored by a section 501(c)(5) or 501(c)(6) organization that regularly conducts such shows as one of its substantial exempt purposes.

If an activity is not unrelated or trade or business, it is also an exempt activity of the organization that conducts it.

Shows that are designed merely to bring buyers and sellers together, not in conjunction with an annual meeting or to stimulate demand for products of the industry as a whole, are not within this exception.

## **II. Performance of particular non-exempt services**

An organization's performance of particular services for its members or others is not an exempt activity under Code section 501(c)(6). Although such activities do not alone preclude exemption, an organization engaged primarily in performing particular services is not exempt under section 501(c)(6).

Examples:

1. Advertising that carries the names of members may be performing particular services; but promoting the business of an industry by encouraging the use of its products is not.
2. Furnishing particular information and specialized individual services to members through publishing and other means to effect economies in business operations may be performing particular services; but educating members on how to improve their business results is not.



3. Operating a multiple listing service for members of a real estate involves performing particular services.
4. Operating parking lots for members' customers may be performing particular services, but providing parking, as part of a plan to promote patronage of businesses in an area may not be.
5. Providing insurance coverage often involves performing particular services. Similarly, negotiating discounted healthcare or similar services for members and/or nonmembers and providing related services may be performing particular services

### **III. Inurement**

An organization does not qualify for exemption if any of its net earnings inures to the benefit of any member. Members may nevertheless receive some kinds of benefits from the organization, such as newsletters and similar material. In addition, return of dues or contributions members paid to support the organization, in proportion to amounts paid, is not inurement. Moreover, the profitability of the members' individual enterprises may be enhanced by the successful promotion of the common business interest.

The statutory inurement proscription, however, precludes furnishing benefits for some members at special rates, at the expense of other members. Other examples of inurement include:

1. Providing financial assistance and welfare benefits for members
2. Paying members for expenses incurred in defending, and judgments rendered in, malpractice suits
3. Owning a copyright on a product sold, and distributing the royalties to, members
4. Distribution of non-member income to members in the form of rebates or reduced dues
5. Rebates to members of amounts paid by both members and nonmembers for space rental at a trade show.

### **IV. Political and Lobbying Activities - Agricultural/Horticultural Organizations and Business Leagues**

An organization that otherwise qualifies for exemption under Internal Revenue Code section 501(c)(5) or 501(c)(6) 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.

If you would like additional information about this topic, including notification when the filing system is ready, or information about other new developments, subscribe to Exempt Organization's Newsletter,

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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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