



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Number: **200536025**

Release Date: 9/9/05

Date: 05/18/05

UIL: 501.06-00
501.27-00

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend:

X =

Dear _____ :

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code. You initially applied for recognition of exemption under section 501(c)(6). In a letter dated October 31, 2003, you requested that we consider you for exemption as an organization described in section 501(c)(27). In a letter dated November 19, 2004, you state that you are seeking exemption based on satisfying the requirements of section 501(c)(27)(B). Based on the information submitted, we have concluded that you do not qualify for exemption under section 501(c)(27), nor do you qualify for exemption under section 501(c)(6). The bases for our conclusions are set forth below.

Your organizing instrument is a Trust Agreement, executed and effective May 30, 1997, by and between The Participating Members and the Trustees to enable the Participating Members to fund the costs of Workers' Compensation Insurance Coverage through a self-insurance program. Four individuals as Trustees, and the same four individuals as Participating Members representing four separate organizations, signed the Trust Agreement. The Trust Agreement states that each Participating Member shall contribute a proportionate share of funds to be held in trust for the payment of workers' compensation insurance coverage, and that the Participating Members shall also place

on deposit with the Chairman of the Workers' Compensation Board such securities as that individual deems necessary of the kind prescribed by your State Banking Law.

Your Trust Agreement, as amended May 30, 1997, states that you shall be managed by four (4) Trustees, all of whom shall be officers, partners, members or employees of members. The Trustees shall be elected by ballot at the annual meeting of the members or at a special meeting of the members which may be called by the Trustees. The four (4) individuals receiving the greatest number of votes shall be elected Trustees. In the case of death, resignation, refusal or inability to act by any Trustee, a successor Trustee may be appointed by the remaining Trustees, such successor to serve until the next election of Trustees by the Members. In your letter dated November 19, 2004, you state that the Workers' Compensation Board's Adopted Rules & Regulations Groups Self Insurance, which are the rules and regulations promulgated by the Workers' Compensation Board and under which you operate, provide that members of the Trusts appoint the Trustees and the names of the Trustees are forwarded to the State Workers' Compensation Board. The State retains the right to make sure that elections are pursuant to the Rules and Regulations, and the State requires notice of election within ten days of election.

In your application, with regard to your membership, you state that (1) each member must be a State x facility, (2) the SIC Code (Standard Industrial Classification Code Division Structure as published in the United States Department of Commerce's Standard Industrial Classification Code Manual) for any new member must be in one of two particular groups, and (3) the governing NCCI codes must be from a select list. You explain that the SIC Codes referred to include ten (10) specific types of x facilities, and that the NCCI class codes referred to include fourteen (14) specific types of x facilities.

You state that your primary activity is providing a cost-effective market for your State x facilities to obtain workers' compensation coverage, and that you have developed methods to mitigate costs and enable members to achieve a stable, required contribution. Your secondary area of importance is your ongoing compliance with your State's Workers' Compensation Laws. As an example of this area, your application to accept a new member is a form that has been approved by the State. Your third area of importance is your ongoing development of new members. Your last activity of importance is your allocation of investments. Although your State articulates what investments can be made, your administrator must ensure the compliance with these rules. You state that your only sources of financial support are the contributions of premiums from your members and investment income.

In your letter dated November 19, 2004, in order to show that you were established by your State, you submitted a document from the State Workers' Compensation Board entitled Notice of Qualification as Group Self-Insurer under the Workers' Compensation

Law. The document states that you, in the x industry, having executed and filed the Agreement and Undertaking, deposited a Surety Bond, and complied with all other conditions provided for in the decision of the Chairman, Workers' Compensation Board, dated concurrent, the status of a group self-insurer under the Workers' Compensation Law became effective as of July 1, 1997 provided that at least six employers generating, in the aggregate, no less than five hundred thousand dollars in pure premium at current rates become participating employers on or before January 1, 1998. The document states it was given the 1st day of July, 1997, under the hand of the Chairman and seal of the Workers' Compensation Board.

In response to the Service's request for you to provide documents that show you provide workmen's compensation insurance to any employer in the State, you provided a copy of the Adopted Rules & Regulations Groups Self Insurance. You stated that you provide workers' compensation insurance to "any" employee in the x industry which meets the classification codes established by the Workers' Compensation Board as noted in the Rules and Regulations. The Rules and Regulations provide, among other matters, that all group members in a group self-insurer must be classified within the same or a related SIC Code operating as self-insurers, and that all group members must be members in good standing in an industry-specific trade association.

The Rules and Regulations also provide that a group self insurer that fails to satisfy the requirements set forth in the Rules and Regulations to maintain authorization to operate as a group may be subject to dissolution at the direction of the chair. You state that the State extends financial support to organizations under the Workers' Compensation Board, and that in the event of the dissolution of one of these organizations, should the organization not be able to pay employee claims, the State would not be relieved from the financial liability of making the payments. As the final guarantor of these claim payments, the State's financial support is established.

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

Section 501(c)(27)(A) of the Code provides for the exemption of any membership organization if-

- (i) such organization is established before June 1, 1996, by a State exclusively to reimburse its members for losses arising under workmen's compensation acts,
- (ii) such State requires that the membership of such organization consist of-

- in
- (I) all persons who issue insurance covering workmen's compensation losses such State, and
 - (II) all persons and governmental entities who self-insure against such losses,
- and
- (iii) such organization operates as a non-profit organization by-
 - (I) returning surplus income to its members or workmen's compensation policyholders on a periodic basis, and
 - (II) reducing initial premiums in anticipation of investment income.

Section 501(c)(27)(B) of the Code provides for the exemption of any organization (including a mutual insurance company) if-

- (i) such organization is created by State law and is organized and operated under State law exclusively to-
 - (I) provide workmen's compensation insurance which is required by State law or with respect to which State law provides significant disincentives if such insurance is not purchased by an employer, and
 - (II) provide related coverage which is incidental to workmen's compensation insurance,
- (ii) such organization must provide workmen's compensation insurance to any employer in the State (for employees in the State or temporarily assigned out-of-State) which seeks such insurance and meets other reasonable requirements relating thereto,
- (iii)(I) the State makes a financial commitment with respect to such organization either by extending the full faith and credit of the State to the initial debt of such organization or by providing the initial operating capital of such organization, and (II) in the case of periods

after the date of enactment of this subparagraph, the assets of such organization revert to the State upon dissolution or State law does not permit the dissolution of such organization, and

(iv) the majority of the board of directors or oversight body of such organization are appointed by the chief executive officer or other executive branch official of the State, by the State legislature, or by both.

Section 1.501(c)(6)-1 of the Income Tax Regulations provides that 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. 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. An association engaged in furnishing information to prospective investors, to enable them to make sound investments, is not a business league, since its activities do not further any common business interest, even though all of its income is devoted to the purpose stated.

Rev. Proc. 74-81, 1974-1 C.B. 135, holds that a nonprofit organization formed to promote the business welfare and interest 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 not entitled to exemption under section 501(c)(6) of the Code. The revenue ruling cites Rev. Ruls. 68-264, 1968-1 C.B. 264 and 68-265, 1968-1 C.B. 265, which hold that an activity that serves as a convenience or economy to members in the operation of their businesses is a particular service of the type proscribed under section 501(c)(6). The revenue ruling concludes that by providing group workmen's compensation insurance for its members, the organization relieves the members of obtaining this insurance on an individual basis, resulting in a convenience in the conduct of their businesses. Therefore, the organization is rendering particular services for individual persons as distinguished from the improvement of business conditions in the contracting and related industries generally.

Although you were formed in accordance with certain State laws pertaining to Workers' Compensation Law and were accepted by the State Workers' Compensation Board effective July 1, 1998, as a group self-insurer, and you are subject to its Rules and

Regulations, you have not provided any documentation showing that you were specifically created or established by the State. You were created as the result of a Trust Agreement, executed and effective May 30, 1997, by and between The Participating Members and the Trustees. For this reason, you do not meet the requirements provided in section 501(c)(27)(B)(1) of the Code.

Each of your members, for which you provide workers' compensation insurance as your primary activity, must be a State x facility, and be described as an organization listed as one of ten (10) specific types under a particular Standard Industrial Classification Code or described as one of fourteen (14) specific types under a particular NCCI class code. You provide workers' compensation insurance to "any" employee in the x industry which meets these classification codes which you state are established by the Workers' Compensation Board as noted in the Rules and Regulations which you are required to follow. These rules, however, do not coincide with the requirements under section 501(c)(27)(B)(ii) of the Code, which provides that organizations must provide workmen's compensation insurance to any employer in the State which seeks such insurance and meets other reasonable requirements. For this reason, you do not meet the requirements provided in section 501(c)(27)(B)(ii).

Your Trust Agreement, as amended, states that you shall be managed by four (4) Trustees, all of whom shall be officers, partners, members or employees of members. The Trustees shall be elected by ballot at the annual meeting of the members or at a special meeting of the members which may be called by the Trustees, and a successor Trustee may be appointed by the remaining Trustees. The Workers' Compensation Board's Adopted Rules & Regulations Groups Self Insurance, under which you operate, provide that members of the Trusts appoint the Trustees and the names of the Trustees are forwarded to the State Workers' Compensation Board. The State retains the right to make sure that elections are pursuant to the Rules and Regulations. Section 501(c)(27)(B)(iv) of the Code requires that the majority of the board of directors or oversight body of the organization be appointed by the chief executive officer or other executive branch official of the State, by the State legislature, or by both. The legislative history of this Code section indicates that Congress intended the oversight body to be "comparable" to a board of directors (see H.R. Rep. No. 148, 105th Cong., 1st Sess., 411 – 412). A board of directors traditionally has the authority to select, direct, monitor, compensate, and fire the officers of the organization and make decisions on extraordinary matters. In your operation, your trustees carry out these activities. Your State's Workmen's Compensation Bureau possesses only monitoring power, and performs none of the traditional activities of a board of directors. For this reason, you do not meet the requirements provided in section 501(c)(27)(B)(iv).

Your primary activity, the provision of a cost-effective market for your State x facilities to obtain workers' compensation coverage, and your development of methods to mitigate

costs and enable members to achieve a stable, required contribution, is described in Rev. Rul. 74-81, supra, as rendering particular services for individual persons as distinguished from the improvement of business conditions in an industry generally. Since this activity of rendering particular services for individual persons is your primary activity, you are not described in section 501(c)(6) of the Code pursuant to section 1.501(c)(6)-1 of the regulations.

Accordingly, for these reasons, you do not qualify for exemption as an organization described in section 501(c)(27) or as an organization described in section 501(c)(6) of the Code and you must file federal income tax returns.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views to this office, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If we do not hear from you within 30 days, this ruling will become final and a copy will be forwarded to the Ohio Tax Exempt and Government Entities (TE/GE) office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling 877-829-5500 (a toll free number) or sending correspondence to: Internal Revenue Service, TE/GE Customer Service, P.O. Box 2508, Cincinnati, OH 45201.

In the event this ruling becomes final, it will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

If you decide to protest this ruling, your protest statement should be sent to the address shown below. If it is convenient, you may fax your reply using the fax number shown in the heading of this letter. If you fax your reply, please contact the person identified in the heading of this letter by telephone to confirm that your fax was received.

Internal Revenue Service
TE/GE

1111 Constitution Ave, N.W., PE-3N3
Washington, D.C. 20224

If you do not intend to protest this ruling, and if you agree with our proposed deletions as shown in the letter attached to Notice 437, you do not need to take any further action.

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

Sincerely yours,

Lois G. Lerner
Director, Exempt Organizations
Rulings & Agreements

Enclosure
Notice 437