



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

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U.I.L. Numbers:

501.06-00

511.00-00

512.07-00

513.00-00

Employer Identification Number:

LEGEND:

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Dear :

This is in response to X's request for a ruling under section 513(d) of the Internal Revenue Code, submitted by X's legal representative.

X was recognized as being exempt from Federal income tax under section 101(7) of the Revenue Act of 1937 [which corresponds to section 501(c)(6) of the Internal Revenue Code of 1986]. It was organized to improve business conditions and promote the a manufacturing industry. X promotes the common interests of its members through educational programs, trade shows, and annual conferences. X also promotes voluntary safety requirements in the industry.

X fulfills its purposes by a number of activities including the regular operation of trade shows. Both members and nonmembers exhibit at X's trade shows, which are designed for the display and demonstration of a products. The products must be displayed as an integral part of the equipment for which the product was designed, either by displaying the product itself or through visual presentations where it is not practical to display the actual product.

X establishes all policies, standards, and rules regarding the show, and as a result is generally perceived by the exhibitors as having ultimate responsibility for the show, show services, and for the exhibitor's successful show experience. In the past, X designated an "official" trade show contractor or contractors to perform services for the benefit of exhibitors at the exhibitors' expense, including services such as drayage, machinery moving and erecting, rigging, rental of furniture, booth and floral decorating, drinking water, telephone service,

electrical, plumbing, carpentry, and sign making. Because of its size, equipment is normally shipped to the trade show for unloading and set up, or occasionally sent by rail to the vicinity of the trade show site, and then trucked to the trade show site.

Under the arrangement with the trade show contractors, X did not itself execute contracts with the show contractors but merely directed exhibitors to work with particular contractors for trade show services. Exhibitors entered into contracts with the trade show contractors to perform work necessary to exhibit at the show according to the rules and standards set by X, but did not enter into contracts with X for anything other than exhibit space. Since X did not contract directly with the show contractors or subcontractors, X had virtually no control over the quality or efficiency of the work provided by the show contractors. If exhibitors became dissatisfied with contractor services, X was (and is) perceived as the responsible party since X manages, operates, and promotes the trade show. Because there is no privity of contract between X and the trade show contractors, X has advised the exhibitors that it is not responsible for the conduct of the show contractors or their employers or subcontractors and that it assumes no responsibility for the show contractor's failure. Despite the disavowal, exhibitors present their grievances or disputes to X with the expectation that X will resolve them. In order to protect the integrity of the show and to make the experience enjoyable for exhibitors, X generally obliges in any way it can to address the grievances or resolve disputes. Since the contracts are between the exhibitors and one or more trade contractors, X generally has no recourse. While X can designate new "official" show contractors for future shows, choosing new vendors after the show is over is inadequate relief to the exhibitor who had spent money to exhibit at the trade show.

X states that the quality (or lack thereof) of a show, along with the exhibitors' experience at the trade show, and, perhaps more importantly, the perception of quality or thereof on the part of trade show attendees can potentially have a negative effect on X, and consequently on the trade show as a whole. The trade show is intended to promote the industry as a whole. If the show does not run smoothly, or if the show does not run smoothly for a number of exhibitors, the exhibitors will suffer from the attendees' poor perception caused by the show contractors' failure to perform as intended. Not only will an inferior show reflect poorly on exhibitors, in the long run an inadequately run show may reflect poorly on the industry as a whole.

X seeks to assume control over the quality of its tradeshow and to successfully promote the industry by providing the services at its trade shows presently made available through trade show contractors. X will provide the services through Y, a single member LLC, whom exhibitors would contract directly with for activities and services that were previously the legal duties and obligations of an unrelated third party contractor. Y will not elect to be treated as separate from X, with X being recognized as Y's sole member on Form 8832. As a result, Y will be treated as a disregarded entity under section 301.7701 of the Procedure and Administration Regulations and pursuant to Announcement 99-102. As Y's sole owner, X will have actual control and ultimate responsibility for the show through the LLC. Y's structure will offer X protection for its assets from legal liabilities that may arise from performing activities associated with the show.

Y is organized and required to operate consistent with section 501(c)(6) of the Code, and its articles provide that no part of the net earnings will inure to the benefit of any manager, officer, or a member of the company, or to any private individual. X states that even though Y is not itself a tax-exempt organization under section 501(c)(6), its organization and operation are

expressly limited to be consistent with the Code section, and its activity will consist of engaging in what is otherwise qualified trade show activity in service to X only.

Y would conduct all aspects of the show, including activities that were, in the past, carried out by the show contractor such as drayage, machinery moving and erecting, rigging, rental of furniture, booth and floral decorating, drinking water, telephone service, electrical, plumbing, carpentry, and sign making. Y will enter into an arm's length contract with a third party primary contractor with particular trade show expertise to provide services that are needed to conduct the trade show in a high quality manner. The contract between Y and the trade show contractor is a fee for services contract with the compensation to the show contractor for trade show services based on the profitability of the trade show. A fee arrangement based on the trade show income minus expenses serves to protect the interest of Y. The arrangement is intended to provide a protective mechanism for Y and, importantly, because it is the sole member of Y, a protective mechanism for X as well.

X has requested the following rulings:

1. Income resulting from activity conducted by the single member LLC (Y) should not be considered unrelated business income because Y is a "disregarded entity" and because of the exception contained in section 513(d) of the Code.

As an alternative to Ruling Request (1), X requests a ruling as follows:

2. If the exception under section 513(d) of the Code does not apply to the activity conducted by Y, then the activity of Y should be considered related to the tax-exempt purposes of X and therefore does not constitute unrelated business income as defined in section 513(a).

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 511 of the Code imposes a tax on the unrelated business taxable income (defined in section 513) of organizations exempt from tax under section 501(c).

Section 512(a)(1) of the Code defines the term "unrelated business taxable income" to mean the gross income, with certain modifications, derived by any organization from any unrelated trade or business (defined in section 513) regularly carried on by it.

Section 513(a) of the Code provides that the term "unrelated trade or business" means, in the case of any organization subject to the tax imposed by section 511, any trade or business the conduct of which is not substantially related to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption.

Section 513(d)(1) of the Code provides, in part, that the term "unrelated trade or business" does not include qualified convention and trade show activities of an organization described in section 513(d)(3)(C).

Section 513(d)(3)(A) of the Code defines the term "convention and trade show activity" as any activity of a kind traditionally conducted at conventions, annual meetings, or trade shows. A convention and trade show activity includes, but is not limited to, any activity one of the purposes of which is to attract persons in an industry generally (without regard to membership in the sponsoring organization) as well as members of the public to the show for the purpose of displaying industry products or to stimulate interest in, and demand for, industry products or services, or to educate persons, engaged in the industry in the development of new products and services or new rules and regulations affecting the industry.

Section 513(d)(3)(B) of the Code defines the term "qualified convention and trade show activity" as a convention and trade show activity carried out by a qualifying organization described in section 513(d)(3)(C) in conjunction with an international, national, State, regional, or local convention, annual meeting, or show conducted by an organization described in section 513(d)(3)(C) if one of the purposes of such organization in sponsoring the activity is the promotion and stimulation of interest in, and demand for, the products and services of that industry in general or to educate persons in attendance regarding new developments or products and services related to the exempt activities of the organization, and the show is designed to achieve such purpose through the character of the exhibits and the extent of the industry products displayed.

Section 513(d)(3)(C) of the Code defines the term "qualifying organization" as an organization described in section 501(c)(3), (4), (5), or (6) which regularly conducts as one of its substantial exempt purposes a show which stimulates interest in, and demand for, the products of a particular industry or segment of such industry or which educates persons in attendance regarding new developments or products and services related to the exempt activities of the organization.

Section 1.513-3(a)(1) of the regulations provides, in part, that convention and trade show activities carried on by a qualifying organization in connection with a qualified convention or trade show will not be treated as unrelated trade or business. Consequently, income from qualified convention and trade show activities, derived by a qualifying organization that sponsors the qualified convention or trade show, will not be subject to the tax imposed by section 511 of the Code.

Section 1.513-3(b) of the regulations provides, in part, that a convention or trade show activity, as defined in section 513(d)(3)(A) of the Code and section 1.513-3(c)(4), will not be considered unrelated trade or business if it is conducted by a qualifying organization.

Section 1.513-3(c)(2) of the regulations provides, in part, that the term qualified convention or trade show means a show that is conducted by a qualifying organization. At least one purpose of the sponsoring organization in conducting the show is the education of its members.

Section 301.7701-1(a)(1) of the Procedure and Administration Regulations provides that whether an organization is an entity separate from its owners for federal tax purposes is a matter of federal tax law and does not depend on whether the organization is recognized as an entity under local law.

Section 301.7701-1(a)(4) provides that under sections 301.7701-2 and 301.7701-3, certain organizations that have a single owner can choose to be recognized or disregarded as entities separate from their owners.

Section 301.7701-2(a) provides that a business entity is any entity recognized for federal tax purposes (including an entity with a single owner that may be disregarded as an entity separate from its owner under section 301.7701-3) that is not properly classified as a trust under section 301.7701-4 or otherwise subject to special treatment under the Code. A business entity with two or more owners is classified for federal tax purposes as either a corporation or a partnership. A business entity with only one owner is classified as a corporation or is disregarded; if the entity is disregarded, its activities are treated in the same manner as a sole proprietorship, branch, or division of the owner.

Section 301.7701-2(c)(2)(i) provides, in general, that a business entity that has a single owner and is not a corporation under section 301.7701-2(b) is disregarded as an entity separate from its owner.

Section 301.7701-3(a) provides that a business entity that is not classified as a corporation under section 301.7701-2(b)(1), (3), (4), (5), (6), (7), or (8) (an eligible entity) can elect its classification for federal tax purposes. An eligible entity with at least two owners can elect to be classified as either an association (and thus a corporation under section 301.7701-2(b)(2)) or a partnership, and an eligible entity with a single owner can elect to be classified as an association or to be disregarded as an entity separate from its owner.

Section 301.7701-3(b)(1) provides generally that in the absence of an election otherwise, a domestic eligible entity is (a) a partnership if it has at least two members, or (b) disregarded as an entity separate from its owner if it has a single owner.

Section 301.7701-3(c) provides generally that an eligible entity may elect to be classified other than as provided under paragraph (b) of this section, or to change its classification, by filing Form 8832, Entity Classification Election.

Announcement 99-102 states that when an entity that is wholly owned by a single owner is disregarded as separate from its owner, its operations are treated as a branch or division of the owner. Therefore, an owner that is exempt from taxation under section 501(a) of the Code must include, as its own, information pertaining to the finances and operations of the disregarded entity in its annual information return.

The unrelated business taxable income of an organization exempt from tax under section 501(c)(6) of the Code is subject to tax under section 511. "Unrelated business taxable income" is defined in section 512(a)(1) as the gross income, with certain modifications, derived by the organization from any unrelated trade or business that it regularly carries on. An "unrelated trade or business" is defined as any trade or business the conduct of which is not substantially related to the exercise or performance of the charitable, educational, or other purpose or function constituting the basis for the organization's exemption. Under Section 513(d)(1), the qualified convention and trade show activities of the organization, as described in section 513(d)(3)(C), are excluded from the term "unrelated business or trade".

X conducts trade shows on a regular basis as part of its activities. At the trade shows, a products are exhibited in order to educate the public about the industry and to promote the industry. X is a "qualifying organization" within the meaning of section 513(d)(3)(C) of the Code. X's "qualified trade show activities" are those carried out by it in conjunction with the trade shows for the purpose of promoting and stimulating interest in and demand for industry products or of educating the public about the industry. X seeks to assume control over the exhibits to ensure that the shows, as demonstrated in the character of the exhibits and the extent of the industry products displayed, continue to help it achieve its exempt purposes.

As sponsor of the trade shows, exhibitors look to X to resolve problems with the trade show contractors, who have been designated as such by X. However, lacking any privity of contract, X's means of resolving the problems with the contractors is limited. X has determined that it can better conduct its trade shows by being in a position where it can legally enforce the contracts with the contractors. Rather than providing the services directly, X will use Y, insulating itself from legal liability. Y's activities will be limited to qualified trade show activities in service to X only. If X performed, as described, the services previously provided by third party contractors, the activities would be excluded from the definition of an unrelated business or trade under section 513(d)(1) of the Code as qualified trade show activity. Providing the services in the manner described would assist X in retaining exhibitors, attracting future exhibitors and enhancing the visitors' enjoyment of the exhibits and creating a positive image of the industry. It would also provide X with the means to enforce contracts so as to minimize the disruptions caused by a contractor's failure to provide the services needed to properly display products and to conduct demonstrations.

While Y is not exempt from tax under section 501(c)(6) of the Code and is not itself a qualifying organization, as a single member limited liability company wholly owned by X that is being treated as a disregarded entity, the activities of Y will be treated as those of X. Therefore, Y's performance of services that would be considered qualified trade show activities for X would be considered the same for Y. The fee arrangement with the contractors is intended to encourage them to provide quality service at the trade shows. If X received income directly from a qualified trade show activity, it would not be considered unrelated business income. Section 1.513-3(a)(1) of the regulations. In the hands of Y, a disregarded entity, income derived from the same activities would not be considered unrelated business income.

Accordingly, based on the facts presented, we rule as follows:

1. Income resulting from activity conducted by the single member LLC (Y) will not be considered unrelated business income because Y is a "disregarded entity" and because of the exception contained in section 513(d) of the Code.
2. Since we have ruled that the income received by Y would not be considered unrelated business income, we have not ruled on the alternative.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Because this letter could help resolve any future questions about tax consequences of X's activities, X should keep a copy of this ruling in its permanent records.

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

Sincerely,

Joseph Chasin
Manager, Exempt Organizations
Technical Group 2