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[redacted]

MAY 17 1988

Key District: [redacted]
Employer Identification Number: [redacted]

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(c)(9) of the Internal Revenue Code.

You are a trust formed on [redacted] for the purpose of providing benefits to the employees of [redacted]. Your organization provides death, disability, and severance pay benefits to full-time employees. Out of [redacted] employees, there are only [redacted] participants in your plan. Of those [redacted] members, [redacted] are salaried and only [redacted] are hourly personnel. [redacted] of the participants are owners of the sponsoring company. The death benefit provided is equal to 7.5 times annual compensation, the disability benefit is 60% of earned income, and the severance benefit is determined on a combination of compensation and years of service. The cost to the employer of these benefits was $[redacted] in [redacted], $[redacted] in [redacted], and $[redacted] in [redacted].

Section 501(c)(9) of the Code provides for exemption from federal income tax of voluntary employees' beneficiary associations (VEBA's) providing for the payment of life, sick, accident, or other benefits to the members of such association or their dependents or designated beneficiaries, if no part of the net earnings of such association inures (other than through such payments) to the benefit of any private shareholder or individual.

Section 1.501(c)(9)-4(a) of the regulations provides, in part, that no part of the net earnings of an employees' association may inure to the benefit of any private shareholder or individual other than through the payment of permissible benefits. Whether prohibited inurement has occurred is to be determined by considering all of the facts and circumstances.

Based on the information submitted, we conclude that you are not a voluntary employees' beneficiary association as that term is used in section 501(c)(9) of the Code.

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[redacted]

A section 501(c)(9) VEBA functions primarily as a cooperative device for pooling funds and distributing risks over and benefits to a defined group of employees sharing an employment-related common bond. Prohibited inurement arises when a VEBA benefits one or more individuals other than through the performance of functions characteristic of an organization described in section 501(c)(9). Thus, the inurement proscription would bar tax-exempt treatment of an organization predominantly organized and operated to promote the interest of an individual standing in relationship to the organization as an investor for private gain.

In your case, the owners of the employer corporation are entitled to a dominant share of the aggregate amount of each benefit available under the plan, because their annual compensation (averaging $[redacted] in [redacted]) is so much higher than that of participating non-owners (averaging $[redacted] in [redacted]), and benefits are based on compensation levels. It also appears that owner-members account for a dominant share of the cost of each benefit under the plan.

Under the circumstances, we believe that the owner-members maintain a posture that is incompatible with the inurement proscription of section 1.501(c)(9)-4(a) of the regulations. A limited membership in combination with allocation of a dominant share of the aggregate benefits to the owner-members indicates that the VEBA is organized and operated for the benefit of its owner-members and not for any employee group. An organization functioning in this manner is inconsistent with the exempt purpose of a VEBA of providing benefits to promote the common welfare of an association of employees, as opposed to the welfare of the owners of the sponsoring employer.

We note that even if there were no inurement present in your situation, your severance pay benefits are based on both years of service and compensation. Because your owner-members have the most years of service, thereby qualifying for the highest level of severance pay benefits, you would not satisfy the safe harbor guidelines we apply in testing for discrimination. Thus, continued suspense of your application would be warranted. It should also be noted that the plan requires that members be at least 25 years of age. Sections 79 and 505(b)(2) of the Code permit only the exclusion of employees less than 21 years of age in testing for discrimination.

[redacted]

Accordingly, based on all the facts and circumstances, we conclude that you do not qualify for recognition of exemption from federal income tax under section 501(c)(9) of the Code. Therefore, you are required to file federal income tax returns.

You have a right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views, with a full explanation of your reasoning. This statement, signed by one of your principal 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 statment 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 principal officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Procedures.

If we do not hear from you within 30 days, this ruling will become final and a copy of it will be forwarded to your key District Director. Thereafter, any questions about your federal income tax status or the filing of tax returns should be addressed to that office.

When submitting additional letters with respect to this case to the Internal Revenue Service, you will expedite their receipt by placing the following symbols on the envelope: [redacted]. These symbols do not refer to your case but rather to its location.

Sincerely yours,

[redacted]

[redacted]
Chief, Exempt Organizations
Rulings Branch

cc: DD, Cincinnati
Attn: EO Group

cc: ARC (Examination) Central Region

cc: [redacted]