TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Date: MAR 12 2014

Contact Person:
Stephanie Robbins
ID Number:
2371105
Telephone Number:
(202) 317-8521

Lee A. Sheller
DLA Piper LLP
6225 Smith Avenue
Baltimore, MD 21209

Dear Mr. Sheller,

The enclosed copy of a letter is sent to you under the provisions of a Power of Attorney and Declaration of Representative, or other proper authorization currently on file with the Internal Revenue Service.

Sincerely,

Stephanie Robbins

Stephanie Robbins
Tax Law Specialist
Exempt Organizations
Technical Group 3

Enclosure:
Copy of letter

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

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Date: MAR 12 2014

OpenStack Foundation
1214 West 6th Street, Room/Suite 211
Austin, TX 78703

Contact Person:
Stephanie Robbins
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2371105
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46-0618689

LEGEND:

Computing	=	Cloud Computing
Project	=	OpenStack Project
Software	=	OpenStack Software
Companies 1	=	Hewlett Packard, IBM, Rackspace
Companies 2	=	Microsoft (Azure), Amazon (Web Services), Google (Cloud Services)
Companies 3	=	Eucalyptus (Eucalyptus), C12G Labs (OpenNebula)
Organization	=	Apache (CloudStack)

Dear Applicant:

We have considered your application for recognition of exemption from Federal income tax under Internal Revenue Code § 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under Code § 501(c)(6). The basis for our conclusion is set forth below.

FACTS

You are incorporated as a nonprofit under your State law. You filed Form 1024, *Application for Recognition of Exemption Under Section 501(a)*, seeking recognition under § 501(c)(6).

Your Certificate of Incorporation states that you are organized and operated exclusively for the purposes described in § 501(c)(6). Specifically, your Certificate states that your purpose is "to develop, support, protect, and promote the open source [Computing] project which is known as [the Project]." The purpose of the Project is to produce "a standard and massively scalable open source [Computing] operating system" known as Software, which is freely available for public use. The Software consists of several components, known as application programming interfaces (APIs), that allow entities to build Computing services to provide a method for managing computing, storage, networking, and other information technology (IT) resources. An entity may use all or part of the Software suite as dictated by business needs. You state that

the Software's modularity is designed to allow third-party software to integrate with the functionality provided by the Software.

You license the Software under the Apache 2 open source license, which allows reproduction and distribution, with or without modification, for free or for a fee, as long as any derivative work contains certain legal and attribution notices. The Apache 2 license does not permit the use of your trademarks. However, under your trademark policy, you allow the use of your trademarks with written permission. Otherwise, you allow use of the Software without attribution and without trademarks. In fact, you state that most entities that use Software do so without attribution and without trademarks. Accordingly, you cannot comprehensively track the Software's use. Nonetheless, you state that more than 200 entities, including colleges and universities, government agencies, and companies within and without the industry, have adopted the Software.

You do not intend for the Software to be an industry standard. In fact, your Bylaws specifically forbid the establishment of "any functional specifications or requirements for interoperability (a 'Standard') between third party technologies and the [Project]."

Activities

You conduct three activities. First, you spend approximately 60 percent of your time and resources conducting community building activities, which you describe as the following:

- Organizing events globally to grow the community of Software contributors and users and to educate the market about the benefits of Computing and open source;
- Creating and promoting content to educate the market about Computing and open source and publishing the content through various channels (websites, newsletters, press relations and outreach); and
- Coordinating the activities for the benefit of the Computing community.

Your community building activities include twice-yearly Project summits as well as participation in other Computing events. You state that the purpose of these events is to encourage further collaboration and to determine future software needs. Second, you spend 25 percent of your time and resources conducting community infrastructure activities, which include managing servers and systems that enable anyone to contribute to the Project; and organizing the work of the community of contributors to make the Software available to everyone. Finally, you spend 15 percent of your time and resources managing your operations, which involves hiring and managing staff; budget planning and reporting; and other governance activities.

You state that you do not provide Computing capabilities. Rather, you manage the community development of and provide access to the Software so that members and non-members can choose whether the employ a full or partial Software suite in conjunction with other types of software to provide themselves with Computing capabilities. As an example, you state that Companies 1 provide Computing services based on the Software.

You argue that your activities do not include providing particular services to individual persons or entities because the Software is open source and not subject to the payment of royalties.

Rather, you argue that you improve the business conditions of one or more lines of business by "encourage[ing] the development of a full range of [Computing] software which is available to members and nonmembers alike without charge"; by providing "the opportunity to use an efficient and cost effective [Computing] environment to process their electronic data"; and by "providing an alternative to proprietary technologies and preventing users from being locked into a particular [Computing] vendor," such as Companies 2; and by "driving down cost."

Moreover, you argue that you are not engaged in a business of a kind ordinarily carried on for profit because Computing businesses typically develop software to meet their customers' specific needs and provide their customers with maintenance and other services. For example, you stated that Companies 2 provide their Computing software and related services for a fee. You explain that the fee calculations are complex and change frequently. By contrast, you state that you do not provide services and that your software is developed by your members who are not your employees. Furthermore, you state that the decision to develop a particular Software capability is based on how useful that capability will be to developers and users and not on how such software will contribute to any revenue or profit. You state that none of your revenue is from the sale of the Software or services related to the Software.

You state that you are not in competition with any other Computing entities. However, Companies 2 provides proprietary software solutions similar to the Software. Companies 2 are not among your members. Additionally, Companies 3 are commercial companies that produce open source Computing software. You explain that the reason commercial companies produce open source software is "a marketing technique to spark interest in their broader suite of products and services for which they charge a fee." Furthermore, a non-profit exempt organization (Organization) provides another free, open source solution similar to the Software.

Membership

Your members include natural persons, business entities, academic institutions, government agencies, and any other legal person who have an interest in Computing; use the Software or other similar Computing software in their business; or engage in the business of information technology, software development, and high-tech marketing. You state that it is impossible to estimate the percentage of the industry represented by your membership.

Income

Your primary source of income is from membership fees. You also receive significant income from corporate sponsorship of your events and from the sale of event tickets.

LAW

I.R.C. § 501(c)(6) provides for the exemption from Federal income tax of business leagues, chambers of commerce, real-estate boards, boards of trade, or professional football leagues (whether or not administering a pension fund for football players), not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Treas. Reg. § 1.501(c)(6)-1 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.

Rev. Rul. 68-264, 1968-1 C.B. 264, held that a nonprofit organization is not exempt under § 501(c)(6) if it operates a traffic bureau for members and nonmembers as its primary activity. The ruling found that a traffic bureau of the type described was a business of a kind ordinarily carried on for profit. Furthermore, the operation of a traffic bureau for members and nonmembers was a clear convenience and economy to the members (and nonmembers) and their businesses, resulting in savings and simplified operations.

Rev. Rul. 74-147, 1974-1 C.B. 136, held that an organization organized to improve the efficiency of its members' use of computers and whose members represented diversified businesses that owned, rented, or leased computers produced by various manufacturers qualified for exemption under I.R.C. § 501(c)(6). The common business interest of the members of the organization was their common business problem concerning the use of digital computers. The organization provided a forum for the exchange of information which led to the more efficient utilization of computers by its members and other interested users that improved the overall efficiency of the business operations of its members.

Rev. Rul. 81-174, 1981-1 C.B. 335, held that a nonprofit association of insurance companies that provided medical malpractice insurance to health care providers did not qualify under § 501(c)(6) because the provision of medical malpractice insurance is a business of a kind ordinarily carried on for profit. The ruling noted that it is the nature of the activity that determines whether it is a business ordinarily carried on for profit.

Rev. Rul. 83-164, 1983-2 C.B. 95, held that an organization whose purpose is to conduct conferences for the dissemination of information concerning computers manufactured by one specific company, M, did not qualify for recognition under § 501(c)(6) because the organization improved the business conditions in a segment of a line of business rather than in an industry as a whole. Although the organization's membership was comprised of various businesses that owned, rented, or leased computers made by M, membership was open to businesses that used other brands of computers as well. At the conferences, presentations were given primarily by representatives of M, as well as by other experts in the computer field. Problems related to members' use of M's computers were also discussed and current information concerning M's products was also provided. The revenue ruling concluded that by providing a focus on the products of one particular manufacturer, the organization provided M with a competitive advantage at the expense of manufacturers of other computer brands.

In National Muffler Dealers Association, Inc. v. United Statues, 440 U.S. 472 (1979), the Supreme Court held that an organization that promoted a single brand of muffler was not exempt under I.R.C. § 501(c)(6) because it did not promote a line of business as required in the regulations. The Court defined "line of business" as meaning either "an entire industry" or "all components of an industry within a geographic area." The Court noted that organizations with

narrower purposes generally fail the "line of business" test because "these groups are not designed to better conditions in an entire industrial 'line,' but, instead, are devoted to the promotion of a particular product at the expense of others in the industry." Organizations failing the "line of business" test included "groups composed of businesses that market a single brand of automobile, or [that] have licenses to a single patentable product, or bottle one type of soft drink." In short, "a tax exemption is not available to aid one group in competition with another within an industry."

In Bluetooth SIG, Inc. v. United States, 611 F.3d 617 (9th Cir. 2010), the Ninth Circuit Court of Appeals held that an association that owned and marketed a wireless networking protocol and trademark was not exempt under I.R.C. § 501(c)(6) because it engaged in a business ordinarily conducted for profit, it did not improve the conditions of one or more lines of business, and it provided particular services for members. The court cited the District Court's discussion of the differences between Bluetooth and American Plywood Association v. United States, 267 F. Supp. 830 (W.D. Wash. 1967), finding that:

> [T]he product in American Plywood was something the members were already selling to begin with; the product here is something the members banded together to create. Thus, the collective enterprise of the Association derives from the fact that it has created a thing of value, which its members can then use to enhance the value of the products they sell.

In MIB, Inc. v. Commissioner, 734 F.2d 71 (1st Cir. 1984), the First Circuit Court of Appeals held that an organization that provided a data bank and exchange for certain information concerning the health and insurability of people who apply for life insurance was not exempt under I.R.C. § 501(c)(6) because it provided its members with a particular service. When determining whether an organization offers "particular services for individual persons," "[t]he ultimate inquiry is whether the association's activities advance the members' interests generally, by virtue of their membership in the industry, or whether they assist members in the pursuit of their individual businesses." Where an association's "service is operated primarily for individual members as a convenience and economy in the conduct of their respective businesses, rather than for the improvement of business conditions within the [industry] generally . . . the operation is not an activity warranting an exemption under the statute." Furthermore, "a major factor in determining whether services are 'particular' is whether they are supported by fees and assessments in 'approximate proportion to the benefits received."

In Pepsi-Cola Bottlers' Association, Inc. v. United States, 369 F.2d 250 (7th Cir. 1966), the Seventh Circuit Court of Appeals held that the line of business test was "wholly unsupported by the legislative history" and therefore invalid. The Service non-acquiesced in Rev. Rul. 68-182, 1968-1 C.B. 263, and the Supreme Court disapproved the Seventh Circuit Court's holding in National Muffler Dealers Association.

In American Plywood Association v. United States, 267 F. Supp. 830 (W.D. Wash. 1967), the District Court for the Western District of Washington determined that a business league devoted to promoting the common business interest of the plywood industry qualified for recognition under § 501(c)(3). The business league engaged in activities, such as promotion and quality control, that the IRS argued were not exempt activities within the meaning of § 501(c)(6). The court agreed but found that these activities were merely incidental to the organization's primary

purpose. The court stated that an organization "will not forfeit tax exempt status by engaging in incidental activities which, standing alone, would be subject to taxation." Determining whether an activity is primary or incidental requires examination of all the facts and circumstances.

In MIB, Inc. v. Commissioner, 80 T.C. 438 (1983), rev'd on other grounds, 734 F.2d 71 (1st Cir. 1984), the Tax Court ruled that exchanging insurance underwriting information among an organization's members with virtually all insurers in the nation as members was not a regular business of a kind ordinarily conducted for profit and therefore did not preclude exemption of organization as a business league under § 501(c)(6). In making this determination, "the case law has generally focused on the existence of competing profit-oriented businesses." Factors indicating the existence of competing profit-oriented businesses include whether there was reasonably foreseeable competition, whether a for-profit business would or could perform a similar function if the organization ceased operations, and the existence of actual competition.

RATIONALE

Based on the information provided, your primary activity is the development, support, protection, and promotion of the Software, which is a particular Computing operating system. Even though your membership is open to all individuals and entities interested in Computing, the key consideration is whether your activities give a competitive edge to your members, as opposed to the industry as a whole. See Rev. Rul. 83-164. Therefore, you do not qualify for recognition under § 501(c)(6).

Section 501(c)(6) authorizes federal income tax exemption for business leagues defined in § 1.501(c)(6)-1. An organization must satisfy the following factors to be recognized as exempt:

(1) It must be an association of persons having some common business interest, and its purpose must be to promote this common business interest.
(2) It must not be organized for profit.
(3) It must be a membership organization and have a meaningful extent of membership support.
(4) No part of its net earnings may inure to the benefit of any private shareholder or individual.
(5) Its purpose must not be to engage in a regular business of a kind ordinarily carried on for profit, even if the business is operated on a cooperative basis or produces only sufficient income to be self-sustaining.
(6) Its activities must be directed at the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons.
(7) Its primary activity cannot be performing particular services for members.
(8) It must be primarily engaged in activities or functions constituting the basis for its exemption.

Treas. Reg. § 1.501(c)(6)-1; see Bluetooth SIG, Inc. v. United States, 611 F.3d 617 (9th Cir. 2010). You fail to meet the requirements of factors (5)-(8) because your primary activity is the development, support, protection, and promotion of the Software.

1. Business Purpose

Your primary activity is the development, support, protection, and promotion of the Software. This activity is a regular business of the kind ordinarily carried on for profit. However, a business league is expressly forbidden from engaging in a business of the 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. Treas. Reg. § 1.501(c)(6)-1. The business' nature determines whether it is ordinarily carried on for profit. Rev. Rul. 81-174. The inquiry focuses on "the existence of competing profit-oriented businesses." MIB, Inc. v. Commissioner, 80 T.C. 438 (1983), rev'd on other grounds, 734 F.2d 71 (1st Cir. 1984). Factors indicating the existence of competing profit-oriented businesses include whether there was reasonably foreseeable competition, whether a for-profit business would or could perform a similar function if the organization ceased operations, and the existence of actual competition.

In your case, the Software is not the only Computing software available. For instance, Companies 2 and Companies 3, not to mention Organization, produce competing software. The fact that you focus on more general Computing development rather than niche Computing markets is irrelevant. Furthermore, the existence of these competitors indicates that for-profit business would and could perform a similar function if you ceased operations. Finally, Computing is a relatively new and rapidly growing medium, meaning that competition was reasonably foreseeable. Therefore, you engage in a business of the kind ordinarily carried on for profit.

Moreover, your distribution of the Software to the public for free does not change this conclusion. In Bluetooth SIG, Inc. v. United States, the court recognized that licensing intellectual property for a low-price is a business tactic to prevent competitors from forming rival technology standards. 611 F.3d 617. You entered a line of business with existing competitors and developed and marketed the Software. Instead of charging a low price to prevent the formation of rival products, you charge zero to persuade the market to abandon pre-existing products. Furthermore, you admit that one of the purposes of the Software is to provide an alternative to proprietary technologies. Accordingly, the fact that the Software is royalty free does not change the fundamental commercial nature of the transaction. Therefore, you engage in a business ordinarily conducted for profit.

2. Improvement of Business Conditions of One or More Lines of Business

Your activities do not improve the business conditions of one or more lines of business. A business league's activities must be directed at the improvement of business conditions of one or more lines of business. Treas. Reg. § 1.501(c)(6)-1. "Line of business" means an "entire industry or all components of an industry within a geographic area." National Muffler Dealers Association, Inc. v. United States, 440 U.S. 472 (1979) (citations omitted). Benefitting non-members and members alike is the key to this requirement. Bluetooth SIG, 611 F.3d 617.

For example, Rev. Rul. 74-147 describes an organization whose members represented diversified businesses that own, rent, or lease digital computers produced by various manufacturers. The organization held semi-annual conferences at which members discussed operational and technical problems relating to computer use. Here, the common business interest of the organization's members was the common business problems concerning the use

of digital computers. The organization improved the business conditions of its members by providing a forum for the exchange of information that would lead to the more efficient utilization of computers by its members and other interested users. Accordingly, the Service determined that the organization qualified for recognition under § 501(c)(6). By contrast, Rev. Rul. 83-164 describes an organization whose members represented diversified businesses that own, rent, or lease computers produced by a single computer manufacturer. The Service determined that the organization's activities were not directed toward the improvement of business conditions in one or more lines of business because, by directing its activities only to the users of a particular brand of computers, the organization directed its activities toward the improvement of business conditions in only segments of various lines of business to which its members belonged. Additionally, the organization provided a competitive advantage to the computer manufacturer and its customers at the expense of its competitors and their customers. Therefore, the organization did not qualify for recognition under § 501(c)(6).

Similar to the organization in Rev. Rul. 74-147, you represent individuals and entities that create and use Computing software. However, rather than addressing Computing problems generally, you produce the Software to address specific Computing problems and promote the Software to the exclusion of other Computing software. Accordingly, like the organization in Rev. Rul. 83-164, you direct your activities to improving the business conditions in only the segments of various lines of business that have adopted the Software. Additionally, your activities provide a competitive advantage to Software adopters because they are saved the expense of developing software similar to the Software.

Furthermore, you do not benefit all or nearly all members of an industry. In Bluetooth SIG, the court determined that Bluetooth did not benefit a line of business because Bluetooth did not benefit "all or nearly all" of the members of both the wireless communications and consumer electronics industries. 611 F.3d 617. Furthermore, the court determined that "Bluetooth-enabled products" was not an industry. Here, you characterize Computing as an industry. However, your membership consists of individuals and organizations from many industries. Therefore, like Bluetooth, you cannot conceivably benefit "all or nearly all" members of these various industries. Furthermore, "organizations that use or are interested in the Software" cannot be considered an industry.

You argue that you are like the organization in Rev. Rul. 69-632, 1969-2 C.B. 120, which describes an organization composed of members of a particular industry to develop new and improved uses for existing products of the industry. The ruling determined that the organization qualified for recognition under § 501(c)(6) because the organization did not perform services for any individual members and because the organization's patents and trademarks were not licensed to any member on an exclusive basis. Similarly, you do not develop software for individual members and your patents and trademarks are not licensed to any member on an exclusive basis. Nonetheless, your activities are distinguishable from the organization in Rev. Rul. 69-632 because you produce a specific product, the Software, rather than developing new and improved uses for existing Computing products. Organizations that promote a single brand or product within a line of business do not qualify for exemption under § 501(c)(6). National Muffler, 440 U.S. 472; Rev. Rul. 68-182 (service non-acquiescence to Pepsi-Cola Bottlers' Association, Inc. v. United States, 369 F.2d 250 (7th Cir. 1966)); Rev. Rul. 83-164. Therefore, you do not qualify for recognition under § 501(c)(6) because you promote a single brand or product within a line of business.

3. Performance of Particular Services for Members

By developing and promoting the Software, you are performing particular services for members. Rev. Rul. 68-264 defines "particular services" as including an activity that serves as a convenience or economy to the members of the organization in the operation of their own businesses. See MIB, Inc. v. Commissioner, 734 F.2d 171 (1st Cir. 1984). In your case, your membership includes members who engage in software development. Many of your members would have to either develop or purchase software similar to the Software. Instead, you develop the Software for your members and non-members, which is a clear convenience and economy that results in savings and simplified operations for the adopters in their businesses. Your program benefits your members and non-members by relieving them of a burden they would otherwise incur, which is considered to be a particular service as described in Rev. Rul. 68-264. Furthermore, no benefit accrues to members and non-members unless they adopt the Software, as the Software is not currently the Computing standard. Accordingly, this activity constitutes the performance of a particular service for individual persons.

4. Primarily Engaged in Activities or Functions Constituting the Basis for its Exemption

You engage in activities or functions other than those constituting the basis for your exemption. If an organization qualifies for recognition under § 501(c)(6), it "will not forfeit tax exempt status by engaging in incidental activities which, standing alone, would be subject to taxation." American Plywood Association v. United States, 267 F. Supp. 830 (W.D. Wash. 1967). A determination of an activity's nature, primary or incidental, requires examination of all the facts and circumstances. As discussed above, you do not qualify for recognition because your primary activity—the development, support, protection, and promotion of the Software—is commercial in nature, fails to improve the business conditions of one or more lines of business, and is a particular service to your members. Therefore, you are not primarily engaged in activities or functions constituting the basis for your exemption.

CONCLUSION

For the reasons described above, we conclude that you do not qualify for recognition of exemption from federal income tax under § 501(c)(6). You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination.

Your protest statement should be accompanied by the following declaration:

> *Under penalties of perjury, I declare that I have examined this protest statement, including accompanying documents, and, to the best of my knowledge and belief, the statement contains all the relevant facts, and such facts are true, correct, and complete.*

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an

individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative,* if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney.* All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

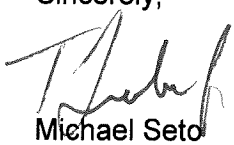
Please send your protest statement, Form 2848 and any supporting documents to this address:

Internal Revenue Service
TE/GE (SE:T:EO:RA:T:3)
Stephanie Robbins (534-25)
1111 Constitution Ave, N.W.
Washington, DC 20224

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

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

Sincerely,



Michael Seto
Manager
Exempt Organizations, Technical