

Internal Revenue Service
District Director
2 Cupania Circle
Monterey Park, CA 91755

Department of the Treasury

Date:

JUL 30 1999

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

Employer Identification
Number

[REDACTED]

Case Number:

[REDACTED]

Refer Reply To:

[REDACTED]

Person to Contact:

[REDACTED]

Contact Telephone Number:

[REDACTED]

CERTIFIED MAIL

Dear Applicant:

We have considered your application for exemption from Federal income tax as an organization described under section 501(c)(3) of the Internal Revenue Code of 1986.

ISSUES:

1. Whether the organization [REDACTED] hereinafter called the "farmers' market", as described below qualifies for exemption under section 510(c)(3) of the Code.

2. If it is not described under section 501(c)(3), whether the organization qualifies for exemption under any of the sub-paragraph of section 501(c) of the Code.

FACTS:

The information submitted on your Form 1023 application discloses that you were organized and incorporated as a non-profit corporation in [REDACTED]. Briefly, your purpose as stated in your Articles of Incorporation is "...to establish a nonprofit [REDACTED] in [REDACTED] solely for the common good and general welfare of people in the community and the surrounding area, pursuant to authority granted by [REDACTED]...the purpose of which was to authorize the establishment and operation of a [REDACTED] in [REDACTED]..."

[REDACTED]

Your object as further clarified in your By-Laws, is "...to promote the sale of locally grown produce to the [REDACTED]; to provide an educational forum for consumers to learn the uses and benefits of quality locally grown produce and for growers to test and diversify their produce and improve their marketing skills; and to enhance the quality of life in the [REDACTED] by providing a community activity which fosters social gathering and interaction.."

The narrative description of your program activities discloses:

- a) the operation of the farmers' market every [REDACTED] for approximately [REDACTED]s from [REDACTED] through [REDACTED], with an additional market day for approximately [REDACTED] months during the peak growing season which is in [REDACTED] through [REDACTED];
- b) that the organization is dedicated to providing a place where local farmers and backyard gardeners could sell their produce to city dwellers;
- c) that its all-volunteer governing board is made up of half buyers (general public) and half sellers, with an ex-officio, non-voting member appointed by the [REDACTED] to serve as [REDACTED];
- d) that in its over [REDACTED] years of operation the market has grown steadily and currently, has attracted [REDACTED] vendors and an estimated [REDACTED] shoppers in the latest season;
- e) that the organization, in the past has had a series of bi-annual workshops for [REDACTED] that teaches them American merchandising practices; that the organization has provided classes and workshops to growers offered on a no-charge basis and will continue to do so;
- f) that for [REDACTED], an annual public meeting is conducted by the Board at the end of each season to receive public suggestions (presumably on matters affecting the [REDACTED] operations); and that the [REDACTED] has come to be a vital forum for social gathering and interaction - an important contributor to the pride people have in their community.
- g) that the organization has developed an educational program in conjunction with [REDACTED] whereby people leaving welfare are encouraged to help grow and sell produce utilizing the best growing practices and merchandising skills as provided by established growers.

[REDACTED]

h) that the organization has other educational/informational activities such as (1) plans to have informational meetings with local experts speaking on topics related to gardening and/or marketing, (2) have available on market days board members and vendors that are capable of answering questions from buyers and sellers, and the general public, and (3) an extension class in [REDACTED], where graduates of the course are encouraged to participate as market vendors;

Your primary source of support is from sellers' fees for market space(s). In-kind contributions and support is provided by [REDACTED]

LAW:

Internal Revenue Code section 501(c)(3) briefly stated, provides Federal income tax exemption to corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provisions of athletic facilities or equipment), or for the prevention of cruelty to children or animals.

Income Tax Regulations 1.501(c)(3)-1(d)(1)(ii) provides in part that an organization is not organized or operated exclusively for one or more of the purposes specified in subdivision (i) of the subparagraph unless it serves a public rather than a private interest.

Internal Revenue Code section 501(c)(4) briefly stated, provides Federal income tax exemption to civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes.

Income Tax Regulations 1.501(c)(4)-1(2) provides in part, that an organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community. An organization embraced within this section is one which is operated primarily for the purpose of bringing about civic betterments and social improvements.

Internal Revenue Code section 501(c)(5) briefly stated, provides Federal income tax exemption to labor, agricultural, or horticultural organization.

Income Tax Regulations 1.501(c)(5)-1 provides briefly, that organizations contemplated by section 501(c)(5) as entitled to exemption are those which have no net earnings inuring to the benefit of any member, and those that have as their objects the betterment of the condition of those engaged in such pursuits, the development of the grade of their products, and the development of a higher degree of efficiency in their respective occupation.

Internal Revenue Code section 501(c)(6) provides exemption from Federal income tax to business leagues, chambers of commerce, real estate boards, boards of trade, or professional football leagues, not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individuals.

Income Tax Regulations 1.501(c)(6)-1 recognizes chambers of commerce, real estate boards, and boards of trade, as being in the general class as business leagues. A business league, as defined therein, 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. 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. (emphasis added)

Internal Revenue Code section 513(a) provides that the term "unrelated trade or business" means, in the case of an organization subject to the tax imposed by section 511, any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under section 501 (or in the case of an organization described in section 511(a)(2)(B), to the exercise of or performance of any purpose or function described in section 501(c)(3),

Income Tax Regulations 1.513-1(a) provides in part that unless one of the specific exceptions of 512 or 513 is applicable, gross income of an exempt organization subject to the tax imposed by section 511 is includible in the computation of unrelated business taxable income if (1) it is income from trade or business, (2) such trade or business is regularly carried on by the organization, and (3) the conduct of such trade or business is not substantially related (other than through the production of funds) to the organization's performance of its exempt functions.

APPLICANT'S POSITION:

In support of your claim for exemption under section 501(c)(3) of the Code, you stated that your purpose is to provide an educational forum for consumers and that such purpose "...is inextricably interwoven with.." and is not (merely) incidental to your goal of establishing a farmer's market for "...the common good and general welfare of the people of the community and surrounding areas..." You stated that your organization is not primarily a social welfare organization within the meaning of section 501(c)(4), nor an organization described in section 501(c)(5). You stated that the purpose of the [REDACTED] is "...to promote appreciation and support of and interest in local produce and to assist customers and growers to learn about and appreciate local produce and to provide them an opportunity to buy and sell strictly regional seasonal produce..."

You also represented that the majority of your sellers are not farmers, but are instead, for the most part, backyard gardeners and growers.

You further represented that a large percentage of your efforts is to educate the community as to the benefits of local produce, to educate the consumer about the value and quality of fresh local produce not available in super-markets, and to educate your backyard gardeners and growers by providing information to keep them up-to-date, as well as to get them started.

IRS POSITION:

After all relevant facts and circumstances were considered, we find that the operation of the farmers' market is your primary activity. The farmers' market for the most part since its inception in [REDACTED] has served as the vehicle where the local community's produce merchants and patrons, buyers and sellers, and growers and end-consumers alike, meet and get together in order to facilitate and consummate their market business transactions. The farmers' market has become a convenient and inexpensive place where farmers, growers, and backyard gardeners in the community can market their produce and food wares. The farmers' market operations constitute a substantial part of your overall operational activity. There is no question that this dominant activity is the cornerstone of your organization's very existence and there is no reason to believe otherwise. Notwithstanding the number of incidental activities which you claim are "educational" and "inextricably interwoven" into your primary activity, said incidental activities will not alter the purely business character of the farmer's market selling operations, which as herein determined, is the dominant activity of your organization.

ANALYSIS:

In Better Business Bureau of Washington, D.C., Inc., vs. United States, 326 U.S. 279, 66 S.Ct. 112, the court, ruling on petitioner's claim as being "...organized and operated exclusively for ...scientific...or educational purposes...no part of the net earnings of which inures to the benefit any private shareholder or individual..", and therefore is entitled to exemption from payment of social security taxes, stated that "...in order to fall within the claimed exemption, the organization must be devoted to educational purpose exclusively. This plainly means that the presence of a single non-educational purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly educational purposes. It thus becomes unnecessary to determine the correctness of the educational characterization of petitioner's operations, it being apparent beyond dispute that an important if not the primary pursuit of petitioner's organization is to promote not only an ethical but also a profitable business community. The exemption is therefore unavailable to petitioner."

(Please note that the petitioner's claim in this particular court case is for exemption from social security taxes. However, it should also be noted that the petitioner's claim is intrinsically tied-in to its claim that it is "...organized and operated exclusively for ..scientific..or..educational purposes..." within the meaning of section 811(b)(8) of the Social Security Act, a provision that was drawn almost verbatim from section 101(6) of the Internal Revenue Code of 1939, which now corresponds to section IRC 501(c)(3) of the Internal Revenue Code of 1954.)

In the same cited court case, the Court in rejecting the petitioner's basic contention that all of its purposes and activities are directed toward the education of business men and the general public, further opined that "...Even the most liberal of constructions does not mean that statutory words and phrases are to be given unusual or tortured meanings unjustified by legislative intent or that express limitations on such an exemption are to be ignored..."

Therefore, for us to allow 501(c)(3) exemption to any organization claiming to be engaged in "educational" activities without giving due consideration and/or ignoring the underlying motive that dictates the conduct of such educational activities, would be tantamount to rendering obsolete the adjectival description for each of the other exempt provisions of section 501(c) as Congress has intended. Such adjectival descriptions are meant to distinguish organizations described in section 501(c)(3) from other organizations that are appropriately described under the various exempt provisions of section 501(c) of the Code. In other words, all exempt organizations may conduct and/or engage in educational activities, however, such does not guarantee automatic exemption under section 501(c)(3) as an exclusively "educational organizations" within the meaning of section

[REDACTED]

The adjectival description that best describes your organization's primary activity is reflected in your corporate charter wherein it is stated that your purpose, is to establish a nonprofit [REDACTED] in [REDACTED] solely for the common good and general welfare of the people of the community and the surrounding area.

Thus, initial consideration was given as to whether exemption can be allowed under section 501(c)(5) of the Code. The proposed rationale being that the farmer's market is an agricultural organization. The membership has for its object the betterment of the conditions of those engaged in agriculture-related pursuits, the improvement of the grade of their products, and the development of a higher degree of efficiency in their respective occupation. However, the prospect of the organization engaging in substantial "unrelated trade or business" as defined in section 513 arising from the operation of the farmers' market increases the likelihood of a finding that the organization's primary activity is "unrelated", and could warrant a denial of exemption. Further, a related finding that the operation of the farmers' market only benefits and serves the private interests of vendors and sellers that will further support the denial of exempt status under this Code section.

Consideration was also given to allow Federal income tax exemption under the exempt provisions of section 501(c)(6) of the Code. The rationale being, that the farmers' market is a trade organization, or business league of merchants, farmers and/or growers of agricultural produce. However, the proscription on "performance of particular services for individual persons" by way of your organization providing the necessary amenities that comes in the form of an economical marketing facility that is provided for use by vendors and sellers, along with a similar likelihood of a finding that the organization is primarily engaged in a "regular business of a kind ordinarily carried on for profit", could also result in a denial of exemption.

Finally, exemption was proposed under the exempt provisions of section 501(c)(4) on the rationale that the collective community benefits derived by both the general public and the agricultural farmers and growers, through their common access to and use of the farmers' market, appears to outweigh whatever private benefits that may seem to accrue to each individual farmer/vendor. Moreover, the low-cost agricultural produce that is made available to the general public (produce buyers and end-consumers) appears to contribute to an enhanced economic advantage for the people of the community. However, your organization declined to accept this proposed Code section reclassification.

CONCLUSION:

Your primary purpose and activity is not exclusively educational within the meaning of section 501(c)(3). Your primary purpose and activity is the conduct of a regular business of a kind ordinarily carried on for profit. Vendors and buyers participating in the farmers' market operations do so, not so much in pursuit of the "educational" benefits which your organization claims to offer, but rather, for the more realistic expectation of making a profit from their selling activities. Thus, your primary activity is designed to lend support to, and facilitate the conduct of a regular business undertaking by local farmers and produce growers in the community.

Therefore, it is the conclusion of the Internal Revenue Service that your organization does not qualify for exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code. It is our determination that you do not meet the qualifying requirements for exemption under section 501(c)(3) of the Code. Further, no determination is made as to whether you qualify for exemption under other exempt provisions of the Internal Revenue Code.

Accordingly, you are required to resume filing income tax returns on Form 1120, U.S. Corporate Income Tax Return, annually with your respective Service Center, as you have been doing since 1972, beginning with tax year ended December 31, 1997.

If you are in agreement with this proposed determination, we request that you sign and return the enclosed agreement Form 6018. Please note the instructions for signing the agreement on the reverse side of the form.

If you are not in agreement with this proposed determination, we recommend that you request a hearing with our office of Regional Director of Appeals. Your request for hearing should include a written appeal giving the facts, law, and any other information in support of your position as explained in the enclosed Publication 892. You will be contacted to arrange a date for a hearing. The hearing may be held at the Office of Regional Director of Appeals, or if you request, at a mutually convenient District Office. A self-addressed envelope is enclosed.

If you do not appeal this determination within 30 days from the date of this letter, as explained in Pub. 892, this letter will become our final determination on this matter. Further, if you do not appeal this determination within the time provided, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Internal Revenue Code provides, in part, that, "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the district court of the United States for the District of Columbia determines that the

organization involved has exhausted administrative remedies available to it within the Internal Revenue Service."

If you have any questions, please contact the person whose name appears on the heading of this letter.

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Sincerely,

A handwritten signature in dark ink, appearing to read "Steven R. Jensen".

Steven R. Jensen
District Director

Enclosures: Form 6018
Publication 892

cc: Power-of-Attorney

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