

INTERNAL REVENUE SERVICE
District Director
2 Cupania Circle
Monterey Park, CA 91754

DEPARTMENT OF THE TREASURY
Western Key District

CERTIFIED MAIL

Date: JUL-07 1998

Employer Identification Number:

Case Number:

Person to Contact:

Telephone Number:

Refer Reply to:

Dear Applicant:

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

FACTS:

The information submitted with your application shows that you were incorporated under the non profit laws of [redacted] on [redacted] under the name [redacted]. You filed articles of amendment, approved by the Secretary of State on [redacted], changing your name to [redacted]. Your articles of incorporation do not contain a clause stating the specific purpose of your organization.

The purpose of your organization as stated in your application, Form 1023, is to "develop and maintain common areas and open space for use by members of the corporation and their guests. Walkways, benches, landscaping, lighting, trash receptacles, water features, irrigation systems, and similar amenities will be installed and maintained together with other common area improvements. All such improvements will be for the mutual benefit of all members of the corporation."

Support to the organization will come from assessments to its members. Members are owners of units of [redacted]. There is no effort to attract members, membership is mandatory for purchasers of units.

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CODE	INITIATOR	REVISOR	REVISOR	REVISOR	REVISOR	REVISOR	REVISOR
SUB.	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
NAME	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
DATE	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

DEPARTMENT OF THE TREASURY—INTERNAL REVENUE SERVICE CORRESPONDENCE APPROVAL AND CLEARANCE FORM 1937-A (9-74)
U.S. GOVERNMENT PRINTING OFFICE: 1979 - 270 - 902

0420 0000

The officers of your organization are the developers of condominium units known as [REDACTED]. Upon completion there will be three buildings with [REDACTED] units in this retirement community. There will also be a clubhouse, swimming pool and private parking garage for tenants and their guests. The tenants will be assessed an association fee in the range of \$[REDACTED]-\$[REDACTED] a month. These fees will be used to help pay for maintenance to the common areas of the buildings such as sweeping leaves, upkeep of elevators and air filtration system, and maintenance of the parking garage.

Your proposed budgets for [REDACTED] and [REDACTED] list expenditures for landscaping, installation of walkways, benches, trash receptacles, and an irrigation system. You will maintain a reserve account for future budgeted expenses related to the upkeep of the three condominium units.

ISSUE:

Does the organization qualify for exemption from Federal income tax as an organization described in section 501(c)(3) of the Code:

LAW:

Section 501(c)(3) of the Code describes certain organizations exempt from income tax under Code section 501(a) and reads in part as follows:

"(3) 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 provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on legislation, (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distribution of statements), any political campaign on behalf of any candidate for public office."

Section 1.501(c)(3)-1(a) of the Income Tax Regulations (Regs) provides that in order to be exempt as an organization described in section 501(c)(3) of the Code, the organization must be one that is both organized and operated exclusively for one or more of the purposes specified in that section. An organization that fails to meet either the organizational or the operational test is not exempt.

Section 1.501(c)(3)-1(a)(2)(b) of the Regs provides that an organization is organized exclusively for one or more exempt purposes only if its articles limit an organization to such exempt purposes.

Section 1.501(c)(3)-1(d)(1)(ii) of the Regs states that an organization is not organized or operated exclusively for one of more of the purposes of section 501(c)(3) unless it serves a public rather than a private interest. The Regs provide that, "to meet the requirements of this subdivision, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests."

Section 1.501(c)(3)-1(c)(2) of the Regs state that an organization is not operated exclusively for statutory purposes if its net earnings inure to the benefit of individuals.

In Benedict Ginsberg v Commissioner, 46 T.C. 47 (1966) the court held that in order to qualify for exemption under Code section 501(c)(3) an organization must serve a public rather than a private benefit. Although an incidental private benefit will not destroy the qualification of an otherwise religious and educational organization, where an organization is serving both public and private interests, the private benefit must be clearly incidental to the overriding public interest.

In Better Business Bureau of Washington, D.C. v. United States, 326 U.S. 279 (1945), the Supreme Court interpreted the requirement in section 501(c)(3) that an organization be "operated exclusively" by indicating that in order to fall within the claimed exemption, an organization must be devoted exclusively to exempt purposes. The Court held that the presence of a single non exempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes.

In Human Engineering Institute, TC Memo 1978-145, affd (1980, CA6) 629 F2d 1160, 90-2 USTC section 9600, 46AFTR 2d 80-5479; Kenner Williams v. Comm., (1963 CA7) 318 F2d 632 63-2 USTC section 9519, 11 AFTR 2d 1596; and Gondia Corp., TC Memo 1982-422 all affirm that an organization not organized and operated exclusively for one or more exempt purposes if its net earnings inures in whole or in part to the benefit of private shareholders or individuals.

In Puritan Church of America v. Comm., (1953, Dist Col) 209 F2d 3-6, 53-2 USTC section 9601, 45 AFTR 119 cert den (1954) 347 US 975, 9898 L ED 1115, the court found that an organization is disqualified if it serves a private rather than a public interest. It must therefore establish that it is not organized or operated for the benefit of private interest such as designated individuals, the creator of the organization or his family, shareholders, or persons controlled (directly or indirectly) by such private interest, and the accomplishment of the exempt purpose must not be accompanied by personal, private or selfish consideration.

In American Campaign Academy, (1989) 92 TC 1053 the court found that non incidental benefits conferred on disinterested persons may

also serve private and non public interest and unrelated third parties (i.e. those not within the scope of private shareholders or individuals but merely members of the general public) are not excluded from the class of private persons whose receipt of benefit would cause the organization to be operated for non exempt purposes.

See Church of Boston v. Commissioner, (1978) 71 T.C. 102' Colorado State Chiropractic Society, (1989) 93 T.C. 487; Best Lock Corporation, (1959) 31 T.C. 1217; St. Louis Science Fiction Limited v. Commissioner, T.C. Memo 1985-162 and Minnesota Kingsmen Chess Association Inc. v. Commissioner, T.C. Memo 1983-495. All of these court cases held that the presence of a single non exempt purpose and substantial non 501(c)(3) activities results in loss of exemption despite the presence of other exempt purposes.

Revenue Ruling 69-175, 1969-1 C.B. 149, held that an organization formed by parents of pupils attending a private school that provided school bus transportation for its members' children served a private rather than a public interest. Revenue Ruling 69-175 states, in pertinent part, as follows:

"When a group of individuals associate to provide a cooperative service for themselves, they are serving a private interest."

Revenue Ruling 69-632, 1969-2 C.B. 120, held that an organization composed of members of a particular industry whose purpose is to develop new improve uses for existing products of the industry is not exempt under section 501(c)(3) of the Code. The organization contracts with various research organizations, institutes, and universities for specific projects selected by the organization's membership. Patents and trademarks that may result from research projects sponsored by the association are licensed royalty free to all applicants meeting the qualifying standards set by the association. The ruling states that the results of the organization's research projects benefit the public but the benefit is secondary to the benefit derived by the organization's members.

Revenue Ruling 71-395, 1971-2 C.B. 228, held that a cooperative art gallery formed and operated by a group of artists for the purpose of exhibiting and selling their works does not qualify for exemption under section 501(c)(3) of the Code. The Revenue Ruling states in pertinent part, as follows:

"The cooperative gallery in this case is engaged in showing and selling only the works of its own members and is a vehicle for advancing their careers and promoting the sale of their work. It serves the private purposes of its members, even though the exhibition and sale of paintings may be an educational activity in other respects."

In Revenue Ruling 72-102, 1972-1 C.B. 149, an organization formed to provide housing to low-income families was held not to be exempt under 501(c)(3) of the Code because it gave preference to

low-income families employed on a farm owned by the individual who created and controlled the organization. The Revenue Ruling reasoned that, even though the organization was providing housing for low-income families, the fact that all families occupying the housing were farm employees of the creator of the organization demonstrated that the organization was operated for a private benefit.

In Revenue Ruling 72-206, 1976-1 C.B. 154, an organization formed to generate community interest in the retention of a classical music program by a local for profit radio station by seeking program sponsors, encouraging continuation of contracts by existing sponsors, urging the public to patronize the sponsor, soliciting subscription to the station's program guide, and distributing material promoting the classical music program, all which tried to increase the station's revenue, does not qualify for exemption under section 501(c)(3) of the Code.

We have also considered your organization for exemption as an organization described in section 501(c)(4) of the Code as a social welfare organization.

ISSUE:

Does the organization qualify for exemption as an organization described in section 501(c)(4) of the Code?

LAW:

Section 501(c)(4) of the Code exempts from Federal income tax organizations which foster the common good and general welfare of the community and reads in part as follows:

"(4)...Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local association of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes."

Regs section 1.501(c)(4)-1(a)(2)(i) states that an organization will be considered to be operating exclusively for social welfare purposes if it is primarily engaged in promoting the common good and general welfare of the people of the community.

Regs section 1.501(c)(4)-1(a)(2)(ii) states that an organization will be considered to be operated exclusively for social welfare purposes if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community, i.e., primarily for the purpose of bringing about civic betterment and social improvement.

Regs section 1.501(c)(3)-1(c)(i) states, "An organization is not operated exclusively for one or more exempt purposes if its net

earnings inure in whole or in part to the benefit of private shareholders or individuals."

Regs section 1.501(a)-1(c) states, "The words 'private shareholders or individuals' in section 501 refers to persons having a personal and private interest in the activities of the organization."

In Comm v. Lake Forest, Inc., (1962, CA4) 305 F2d 814, exemption was denied a non profit corporation that erected low rent public housing where the tenant members obtained an equity in the units through monthly payments and all assets were distributed to the members upon dissolution. The benefits rebounded chiefly to the private purchasers of the housing units.

In United States v. Pickwick Electric Membership Corp., 158 F2d 272 (6 Cir. 1046), the Court stated that a civic organization is described as embodying "the ideas of citizens of a community cooperating to promote the common good and general welfare of the community."

The Court in Erie Endowment v. United States, 316 F2d 151 (1063), while acknowledging the difficult task in arriving at a specific definition of "civic organization," states that "the organization must be a community movement designed to accomplish community ends."

Revenue Ruling 54-394, 1954-2 C.B. 131, denied exemption to an organization that provided television reception for its members exclusively.

Revenue Ruling 62-167, 1962-2 C.B. 142, held that an organization was exempt where it transmitted television signals by a reflector type apparatus so that the signals were available to any television receiver in the community. All members of the community were benefited whether or not they were members of the organization.

Revenue Ruling 69-280, 1969-1 C.B. 152, held that a non profit organization formed to provide maintenance of exterior walls and roofs of members' homes in a development is not exempt from Federal income tax under section 501(c)(4) of the Code.

Revenue Ruling 73-306, 1973-2 C.B. 185, denied exemption to a tenant organization formed to protect the rights of tenants in one particular rental complex.

Revenue Ruling 74-17, 1974-1 C.B. 130, held that while condominium associations and homeowners' associations provide similar services, a substantial distinction existed between them. Specifically, the essential nature and structure of condominium ownership, both statutory and contractual, is inextricably and compulsorily tied to the owner's acquisition and enjoyment of the property. Basic condominium ownership necessarily involves common

ownership of all condominium property in the development, the care and maintenance of which would constitute the provision of private benefit to the owners to a degree that would disqualify it from exemption under Code section 501(c)(4).

Revenue Ruling 74-99, 1974-1 C.B. 131, which modifies Revenue Ruling 71-102 provides that in order to qualify for exemption under Code section 501(c)(4), a homeowners' association must serve a "community" which bears a reasonable relationship to an area ordinarily identified as governmental, it must not conduct activities directed to the exterior maintenance of private residences, and the common area it owns and maintenance must be for the use and enjoyment of the general public.

Revenue Ruling 80-205, 1980-2 C.B. 185, held that an organization formed to promote the legal rights of tenants in a community by publishing a newsletter, conducting public meetings dealing with matters of concern to tenants, and operating an information center, were promoting the common good and general welfare of the people of the community.

ANALYSIS AND CONCLUSION:

As stated in the above Code sections, regulations, court case, and revenue rulings, to meet the operational test, an organization must be engaged in activities furthering "public purposes" rather than private interests. It must not be operated for the benefit of designated individuals or the persons who created it.

The activities of your organization are similar to the organizations described in Benedict Ginsberg v. Commissioner, court case and Revenue Ruling 74-17 in that your income is generated from member assessments based on their condominium ownership and the income is used for expenditures associated with the maintenance of the condominium units and the common areas of the units. These maintenance expenses serve the private interests of your members and not the general public. Your activities can be compared with the organization described in the above Revenue Ruling in that you are also operated to serve the private interests of your members. You are operating to fulfill your individual responsibility of the upkeep of your condominium units.

The concept of social welfare includes the provision of benefits to the community at large. The providing of benefits to a narrow group of recipients, in most instances, is not considered as promoting social welfare. Therefore, a social welfare organization may not, if it is to qualify for tax exemption under Code section 501(c)(4), be operated for the private benefit of the organization's membership or other select groups of individuals or organizations.

By failing to meet the operational test for exemption, we conclude you are not exempt under any section 501(c)(3) of the Code. Also, you are not primarily operated for the good of the community under section 501(c)(4) of the Code.

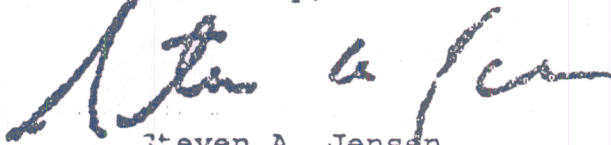
Accordingly, we hold that you are not entitled to exemption under section 501(c)(3) of the Code because you are not organized and operated exclusively for charitable purposes. You are not entitled to exemption under Section 501(c)(4) of the Code because you are not operated exclusively for social welfare purposes.

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 a hearing should include a written appeal giving the facts, law, and any other information to support your position as explained in the enclosed Publication 892. You will then be contacted to arrange 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.

If we do not hear from you within 30 days from the date of this letter, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies and will then become our final determination. Section 7428(b)(2) of the Internal Revenue Code provides in part that, "A declaratory judgement or decree under this section shall not be issued in any proceeding unless the Tax Court, the Court of Claims, 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.

Sincerely,



Steven A. Jensen
District Director

Enclosure(s):
Publication 892
Form 6018