

Internal Revenue Service

Department of the Treasury

Washington, DC 20224

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Date 11/6/98

Contact Person: [REDACTED]

Telephone Number: [REDACTED]

In Reference to:

OP:E:EO:T:2

Date:

AUG 27 1998

DO: [REDACTED]

EIN: [REDACTED]

Dear Applicant:

This is in regard to your application for recognition of exemption under section 501(c)(3) of the Internal Revenue Code.

We have reviewed the information you have submitted and have concluded that you do not qualify for recognition of exemption under section 501(c)(3) because more than an insubstantial portion of your activities are not qualifying section 501(c)(3) activities. In addition, you operate in a manner similar to a for-profit business and are operated for the benefit of private noncharitable interests.

You were incorporated to document the medical efficacy of medical marijuana, and to insure that seriously ill patients have access to a safe, and natural supply of [REDACTED] as prescribed by their physician. In your letter of [REDACTED], you describe yourself as a "collective of patients and caregivers seeking only to educate the general public and [your] membership regarding the medical usefulness of [REDACTED] and to insure that [your members and perhaps others] as seriously ill patients have access to a safe, natural supply of [REDACTED] to treat [their] individual medical conditions as recommended by [their own] physicians, and to document the medical efficacy of [REDACTED] through scientific observation." In this same letter you describe yourself as "an organization of patients and caregivers who collectively provide for [themselves] and each other as well as educate, supply, document and research."

The financial information you have submitted breaks your expenses down into several categories. These categories include general administration, distribution, cultivation, education and research.

The distribution program appears to involve providing direct aid to individuals. It appears, from what little information we have regarding this aspect of your program, that this program is designed to provide for the distribution of [REDACTED] for medicinal purposes to individuals. It appears that [REDACTED]

Re: [REDACTED]  
[REDACTED]

will be distributed to some individuals for free, however, contributions from the recipients or sponsorship by others is encouraged. Similarly, it appears that medicinal doses of [REDACTED] are only provided to members. The [REDACTED] specifically asks for information regarding membership and financial status. You have also submitted a copy of the [REDACTED] m. This document certifies that a medical doctor has determined that use of [REDACTED] could be medically beneficial. However, this document is not the equivalent of a prescription.

The cultivation program appears to allow you to enter into contractual arrangements with individuals who [REDACTED].  
[REDACTED] You have indicated that you do not charge for the [REDACTED] you distribute, however you do encourage contributions. As stated in your [REDACTED], "upon completion of the Agreement ([REDACTED]), I [REDACTED], agree to have my [REDACTED] weighed in order to provide for my own needs, and not to receive the weekly allotment given by [REDACTED], unless upon an approved product from [REDACTED], for a reasonable time, to be decided by [REDACTED] and myself, or unless otherwise discussed with me and agreed upon by [REDACTED]." The agreement also states that, [REDACTED] encourages tithing back any [REDACTED] should the net result of [REDACTED] provide me with more [REDACTED] than I might require. . . ." It is also clear from this agreement that you may loan equipment to individuals who are engaged in [REDACTED].

The financial information you have submitted indicates that between [REDACTED] you expended over \$[REDACTED] in your [REDACTED] program and approximately \$[REDACTED] in your [REDACTED] program. Your total income during this period was slightly over \$[REDACTED]. Your proposed budget for future years indicates that your [REDACTED] program will account for more than one-half of your annual expenditures.

It is unclear whether you are a membership organization or not or whether you only provide assistance to your members. However, you indicate in your application that you are not and your Articles and Bylaws are silent in the matter. However, your [REDACTED] participation states that the [REDACTED] is a member of your alliance and is acting in compliance with [REDACTED]. In addition the financial information you have submitted indicates that member donations are your major source of income. The other major source of income is identified as supporter donations.

Re: [REDACTED]  
[REDACTED]

In [REDACTED] passed by initiative, [REDACTED] court in [REDACTED]. However, as recognized by the [REDACTED], the Federal Government's policies regarding the illegality of [REDACTED] are governed by the prohibitions in the [REDACTED]

Section 501(c)(3) of the Code provides for the exemption from federal income tax for organizations organized exclusively for religious, charitable, educational, scientific and other specified exempt purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(a)-1(c) of the Income Tax Regulations defines "private shareholder or individual" as referring to persons having a personal and private interest in the activities of the organization.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations states that an organization is not organized or operated exclusively for one or more of the purposes specified in section 501(c)(3) unless it serves a public rather than a private interest. Thus, to meet these requirements, 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(d)(3)(i) of the regulations states that the term "educational," as used in section 501(c)(3) of the Code relates to (1) the instruction or training of the individual for the purpose of improving or developing his capabilities; or (2) the instruction of the public on subjects useful to the individual and beneficial to the community.

Section 1.501(c)(3)-1(e)(1) of the regulations states that an organization may meet the requirements of section 501(c)(3) of the Code although it operates a trade or business as a substantial part of its activities, if the operation of such trade or business is in furtherance of the organization's exempt purpose or purposes and if the organization is not organized or

Re: [REDACTED]

operated for the primary purpose of carrying on an unrelated trade or business as defined in section 513. In determining the existence or nonexistence of such primary purpose, all the circumstances must be considered, including the size and extent of the activities which are in furtherance of one or more exempt purposes.

Section 513(a) of the Code defines the term "unrelated trade or business" as 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 forming the basis for its exemption under section 501.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279 (1945), Ct.D. 1650, C.B. 1945, 375, the Supreme Court of the United States held that the presence of a nonexempt purpose, if more than insubstantial, would destroy tax exempt status as a charitable organization.

Harding Hospital, Inc. v. United States, 505 F2d 1068 (1974), holds that an organization seeking a ruling as to recognition of its tax exempt status has the burden of proving that it satisfies the requirements of the particular exemption statute. Whether an organization has satisfied the operational test is a question of fact. In this situation the hospital was held not entitled to exemption under section 501(c)(3) of the Code because it limited its admissions and emergency room care substantially to a private group of patients.

In Old Dominion Box Co. v. United States, 477 F 2d. 344 (4th Cir. 1973) cert. denied 413 U.S. 910 (1973), the court held that operating for the benefit of private parties constitutes a substantial non-exempt purpose.

In B.S.W. Group, Incorporated v Commissioner, 70 T.C. 352, the court held that an organization which operated at a profit whose only role is that of a conduit linking individual researchers with interested client organizations, both exempt and nonexempt, did not qualify for exemptions under section 501(c)(3) of the Code. It was conducting a consulting business of the sort which is ordinarily carried on by commercial ventures organized for profit.

Rev. Rul. 61-170, 1961-2 C.B. 112, holds that a nurses' association which maintained an employment register primarily for the employment of its members was not entitled to exemption under section 501(c)(3). On the basis of the information presented,

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the instant organization is primarily engaged in the performance of personal services by operating an employment service principally for the benefits of its members. Public participation in the management and support of the organization is negligible. This is shown by the fact that it draws its support primarily from members and is controlled by a board of trustees composed of professional nurses, without public participation of any kind. Therefore, the organization is not free from substantial private considerations in the operation of its nurses' register.

Rev. Rul. 69-175, 1969-1 C.B. 149 holds that a nonprofit organization formed by parents of pupils attending a private school that provides school bus transportation for its members' children serves a private rather than public interest. The organization's income approximately equals the expenses involved in its operations.

Rev. Rul. 73-349, 1973-2 C.B. 179 holds that an organization formed to purchase groceries for its membership at the lowest possible prices on a cooperative basis is not exempt as a social welfare organization described in section 501(c)(4) of the Code. The organization was a private cooperative enterprise for the economic benefit or convenience of its members. Any benefit to the community was incidental to the benefit received by the members.

Rev. Rul. 75-384, 1975-2 C.B. 204 holds that a non-profit organization formed to promote world peace and disarmament and nonviolent direct action and whose primary activity is the sponsoring of antiwar protest demonstrations in which demonstrators are urged to commit violations of local ordinances and breaches of public order does not qualify for exemption under section 501(c)(3) or (c)(4) of the Code. As a matter of trust law, one of the main sources of the general law of charity, no trust can be created for a purpose which is illegal. The purpose is illegal if the trust property is to be used for an object which is in violation of the criminal law, or if the trust tends to induce the commission of crime, or if the accomplishment of the purpose is otherwise against public policy. IV Scott on Trusts Sec. 377 (3d. ed. 1967). Thus, all charitable trusts, (and by implication all charitable organizations, regardless of their form) are subject to the requirement that their purposes may not be illegal or contrary to public policy. See Restatement (Second), Trusts (1959) Sec. 377, Comment (c).

It is incumbent upon an organization seeking recognition of its tax exempt status to carry the burden of proving that it satisfies the requirements of the particular exemption statute.

Whether an organization has satisfied the operational test is a question of fact. See Harding Hospital, Inc. v. United States, supra. Furthermore, it must be established that an organization is operated exclusively for exempt purposes. The presence of a single nonexempt activity, if more than insubstantial will preclude exemption. See Better Business Bureau of Washington, D.C., Inc. v. United States, supra.

Although, section 1.501-1(e) of the regulations provides that an organization may meet the requirements of section 501(c)(3) although it operates a trade or business as a substantial part of its activities, if the operation of such trade or business is in furtherance of the organization's exempt purpose or purposes, where the business activities do not directly further the exempt section 501(c)(3) purposes, exemption will be denied. See B.S.W. Group, Incorporated v Commissioner, supra. In addition, activities which directly benefit private interests, if more than insubstantial, will preclude exemption. See Old Dominion Box Co. v. United States, supra.

Your activities go beyond merely educating the public about [REDACTED]. The information you have submitted establishes that providing material assistance and [REDACTED] to individuals who wish to [REDACTED] to individuals who have received advice from a licensed medical doctor that the use of [REDACTED] could be medically beneficial to that individual is, if not, your primary activity, at least more than an insubstantial part of your activities. Furthermore, the submitted information indicates that you are only or primarily providing [REDACTED] as a drug or for [REDACTED] to your members. It should also be recognized that you are seeking recognition of exemption from Federal income tax and the current Federal policy, as a general rule, prohibits the use the [REDACTED]

Accordingly, we have concluded that you do not qualify for recognition of exemption under section 501(c)(3) of the Code. More than an insubstantial part of your activities are in violation of Federal [REDACTED]. As stated in Rev. Rul. 75-384, supra, as a matter of trust law a trust, and by implication any charitable section 501(c)(3) organization, can not be created for a purpose which is illegal or contrary to public policy.

Furthermore, assisting others to [REDACTED] and distributing a [REDACTED] is similar to acting as a broker or an agent. You provide the [REDACTED] and some equipment, a product [REDACTED] and a portion of this product will be distributed by you. You encourage [REDACTED]

contributions in return for the assistance you have provided. However, a payment in guise of a contribution is at least in part a payment. The mere fact that profits if any are negligible, or that some [redacted] are given away is not governing. Nor is the fact that no legal commercial market is present. In addition, the provisions of section 1.501(c)-1(e) of the regulations are not applicable because assisting as a broker or agent in [redacted] [redacted] is not in furtherance of the accomplishment of any the exempt purposes you are carrying on.

In addition, you indicate that you are a cooperative organization, and it appears that the primarily beneficiaries of your program are your members. The Service has consistently taken the position that operating primarily for the benefit of an organization's members establishes that such an organization is primarily serving the interests of a select group of individuals rather than the general community. A business or any other activity which only assists the community incidentally and provides direct benefits to a limited number of members of the community is not necessarily charitable. For example, in Rev. Rul. 61-170, *supra*, the Service determined that maintaining a nurses registry provides some benefit to the community, however the primary beneficiaries of the organization's activities were the nurses themselves. Similarly, in Rev. Rul. 69-175, *supra*, although the school and the community received a benefit by reason of the school bus transportation program, the primary beneficiary of this program was the private interests of the parent/members. See also Rev. Rul. 73-349, *supra*, where a cooperative grocery store was denied exemption.

Accordingly, as previously state we have determined that you do not qualify for recognition of exemption under section 501(c)(3) of the Code. Contributions to you are not deductible under section 170 of the Code. You are required to file federal income tax returns.

You have the 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 the right to a conference in this office after your statement 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 Practice Procedures.

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