

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

Date: JUL 13 1999

Contact Person: [REDACTED]

ID Number: [REDACTED]

Telephone Number: [REDACTED]

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

Employer Identification Number: [REDACTED]

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The basis for our conclusion is set forth below.

You were incorporated on [REDACTED]. Your Articles state you were formed to collect royalties for distribution of your publications and to utilize said royalties to fund and provide continuing legal education programs throughout the [REDACTED], and to provide such other services and programs in furtherance of these purposes. Your membership shall be comprised of those who have written or will write materials for publication in your publication. Your initial Board of Directors may not be less than five.

You have stated your central activity is to collect royalties for distribution of your publications (10% of the net price of every book sold) and to utilize the royalties for a yearly scholarship and to fund and provide continuing legal education programs throughout the [REDACTED]. However, you indicated in your [REDACTED] response to the Service that most of the funds will be used as direct grants to the [REDACTED] ([REDACTED]), which may use such funds under their own scholarship programs. [REDACTED] is a business league tax-exempt under IRC 501(c)(6). You have no brochures and do not intend to prepare any brochures or publicity for your scholarship program. The procedure by which you may make grants to [REDACTED] will be through the "Application for Grant Funds" form. There is no written agreement between you and [REDACTED] regarding the funds.

In your response to the Service you submitted a copy of a publishing agreement between the [REDACTED] (which you stated was a dissolved 501(c)(6) corporation) and [REDACTED] dated [REDACTED]. The [REDACTED] then assigned the publishing agreement and the copyright (two separate agreements) to [REDACTED] on [REDACTED]. You also included another consent to assignment of copyright between the [REDACTED] and [REDACTED] dated [REDACTED].

You are the owner and holder of a publishing agreement and the copyright to [REDACTED] published by [REDACTED], a division of [REDACTED]. The book is

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marketed by ██████████ to whom the rights for publication have been licensed. You will write sections or update sections of this three-volume book set, and one of your board members will serve as editor for the ██████████ from which you receive royalties. From the royalties received, (anticipated royalty income is expected to be less than \$█████████ annually) you originally proposed to underwrite, financially, one or more scholarships, in amounts which were to be determined each year (generally in amounts not less than \$█████████ each) for students in legal secretarial or legal assistant science. Scholarships were to cover books and tuition, and be paid to the college or university attended by each scholarship recipient. The scholarship(s) were to be awarded on the basis of academic standing or grade point average and need. This was all changed per your letter to the Service dated ██████████. You stated you would underwrite financially, the cost of legal education seminars; workshops and/or training courses conducted by ██████████.

Your members shall consist of your Directors and those individuals who have in the past or in the future contribute literary efforts your publication(s)" (Article II, section 2.01). No officer/director will receive compensation. "Each director shall hold office until she resigns..." (Article III, section 3.02). ██████████ plans to only employ the directors and other members who are recruited to write for the ██████████. "There are no common officers or directors between you and ██████████. Both you and ██████████ are made up of persons interested in the legal field, primarily the legal secretarial field. Some of your members will likely be members of ██████████.

Your primary activity is to contract with and review work of independent contractors in production, writing and up-dating ██████████ (█████████% of the time). This includes collecting royalties, bookkeeping and meetings (█████████% of the time) and reviewing and approving or disapproving grant applications (█████████% of the time).

Section 1.501(a)-1(c) of the regulations defines private shareholder or individual. The words private shareholder or individual in section 501 refers to persons having a personal and private interest in the activities of the organization.

Section 501(c)(3) of the Code provides, in part, for the exemption from Federal income tax of corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(a)(1) of the regulations provides that an organization must be both organized and operated exclusively for one or more of the purposes specified in section 501(c)(3) of the Code in order to be exempt as an organization described in such section.

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 is engaged 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(c)(2) of the regulations provided that 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.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations states that an organization is not organized or operated for one or more exempt purposes unless it serves a public rather than a private interest. Accordingly, 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, shareholders, or persons controlled, directly or indirectly, by such private interests.

Section 1.501(c)(3)-1(d)(2) of the regulations provide that the term "charitable" as used in section 501(c)(3), include the relief of the poor and distressed or the underprivileged; advancement of religion; advancement of education or science; lessening the burdens of government, and the promotion of social welfare by organizations designed to lessen neighborhood tensions, eliminate prejudice and discrimination or combat community deterioration.

Section 1.501(c)(3)-1(d)(3) of the regulations defines the term educational as used in section 501(c)(3) to include:

- (a) The instruction or training of the individual for the purpose of improving or developing his capabilities; or
- (b) The instruction of the public of subject useful to the individual and beneficial to the community.

Section 1.501(c)(3)-1(a) of the regulations states that an organization may be exempt under section 501(c)(3) even though 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 purposes and if the organization is not organized or 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 facts and circumstances must be considered, including the size and extent of the trade or business and the size and extent of the activities which are in furtherance of one or more exempt purposes. An organization, which is organized and operated for the primary purpose of carrying on an unrelated business, is not exempt under section 501(c)(3).

Section 502(a) of the Code provides that an organization operated for the primary purpose of carrying on a trade or business for profit shall not be exempt from taxation under section 501 on the ground that all of its profits are payable to one or more organization exempt from taxation under section 501.

Rev. Rul. 66-104, 1966-1 C.B. 135, held that a nonprofit organization which makes funds available to authors and editors for preparing teaching materials and writing textbooks, and under the terms of the contract with the publisher, receives royalties from sales of the published materials and then shares them with those individuals, does not qualify for exemption because while the publication serves educational interests, the facts show only an enterprise conducted in an essentially commercial manner.

Rev. Rul. 77-4, 1977-1 C.B. 141, found that a nonprofit organization, whose only activities are preparing and publishing a newspaper of local, national, and international new articles with an ethnic emphasis, soliciting advertising and selling subscriptions to that newspaper in a manner indistinguishable from ordinary commercial publishing practices, is not operated exclusively for charitable and educational purposes and does not qualify for exemption.

*Better Business Bureau v. United States*, 316 U.S. 279 (1945), holds that the existence of a single non-exempt purpose, if substantial in nature, will destroy the exemption under section

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501(c)(3). 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 purposes.

*Harding Hospital, Inc. v. United States*, 505 F.2d 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. See, also, *Christian Stewardship Assistance, Inc. v. Commissioner*, 69 T.C. 1037, 1042 (1978).

*United Libertarian Fellowship, Inc. v. Comm'r* 65 T.C.M. 2175, 2181 (1993), holds that where the creator (of an organization) control the affairs of the organization, there is an obvious opportunity for abuse, which necessitates an open and candid disclosure of all facts bearing upon the organization, operation, and finances so that the Court can be assured that by granting the claimed exemption it is not sanctioning and abuse of revenue laws. The court added that, where this disclosure is not made, the logical inference is that the facts, if disclosed, would show that the taxpayer [organization] fails to meet the requirements for tax exempt status. See also, *Bubbling Well Church of Universal Love, Inc., v. Comm'r*, 74 T.C. 531, 535 (1980), *AFF'D*, 670 F.2d 104 (9th Cir. 1981).

*est of Hawai'i v. Commissioner* 71 T.C. 1067 (1967), holds that petitioner's activities, although educational in nature, served the commercial purposes of the for-profit corporations and petitioner was therefore not operated exclusively for exempt purposes within the meaning of section 501(c)(3), I.R.C. 1954.

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable purposes. The requirement that an organization operate exclusively for a charitable purpose is further amplified in section 1.501(c)(3)-1(c)(1) of the regulations. This section 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. In the fundamental case of *Better Business Bureau of Washington D.C., Inc.*, *supra*, the court concluded that the presence of a single nonexempt purpose, if substantial in nature, will preclude exemption regardless of the number or importance of statutorily exempt purposes.

Your Articles of Incorporation (Article II), state that you are "...organized exclusively for charitable and educational purposes...". Section 501(c)(3)-1(a)(1) of the Income Tax Regulations, *supra*, provides that an organization must be both organized and operated exclusively for one or more of the purposes...". Section 501(c)(3)-1(b), *supra*, states generally that an organization cannot empower itself to engage in activities which in themselves are not in furtherance of one or more exempt purposes.

Your activities consist of producing a commercially salable three volume set of books, for sale to the general public, which can be utilized by legal secretaries throughout [REDACTED] and others who may engage in their own legal representation. The books are marketed in a commercial manner for a full retail value. You have stated that members will write sections or update sections of this three-volume book set, and one of our Board members serves as editor for the book. You receive royalties from the sale of this [REDACTED]. Your activities are not distinguishable

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from the activities of an ordinary commercial publishing operation. Your activities have a commercial or business hue - writing, updating, and editing a legal secretary's manual for sale to the public for which you will receive royalties. Your market is not limited enough to indicate a less than commercial purpose. Taken together, these factors present a picture of a commercial publishing enterprise more than having a charitable, educational purpose.

To be tax-exempt, it is necessary for an organization to establish that it is not organized and operated for the benefit of private interests such as designated individuals, the creator(s) of the organization, family or shareholders of the organization, persons controlled (directly or indirectly) by these private interests, or any other person(s) having a personal and private interest in the activities of the organization. Here, members are furnishing a service to you. This service is in the form of writing the ██████████ and supplying the required updates. This money is to be used for the training activity of ██████████. ██████████ has many of the same members as you. From the facts it is evident that you will be collecting royalties from the publication and sale of your ██████████ that your members have written, edited, and updated, for the specific purpose of making grants to ██████████. You have indicated that ██████████ has as its primary objective to maintain the professional standards of legal secretaries through legal seminars and instruction and thereby furthering the common business interest of your members who are also members in common with ██████████.

You have indicated that both you and ██████████ have the same members, and as such serve one purpose, that is, to benefit ██████████, which has a common membership with you. Although educational interests are served by the publication of reference manuals, the facts in this case show only an enterprise conducted in an essentially commercial manner. Your income-producing activities are not incidental to your educational activities but are the very justification for your existence. See, *est of Hawai'i, supra*. See also, *American Institute for Economic Research v. United States*, 157 Ct. Cl. 548, 302 F.2d 934 (1962); *Fides Publishers Assn. v. United States*, 263 F.Supp. 924 (N.D. Ind. 1967).

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns or Form 1120.

Contributions to you are not deductible under section 170 of the Code.

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

If you do not protest this ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the 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 United States Court of Federal 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 we do not hear from you within 30 days, this ruling will become final and a copy will be

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forwarded to the Ohio EP/EO key district office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling 877-829-5500 (a toll free number) or sending correspondence to: Internal Revenue Service, EP/EO Customer Service, P.O. Box 2508, Cincinnati, OH 45201. The appropriate State Officials will be notified of this action in accordance with Code section 6104(c).

When sending additional letters to us with respect to this case, you will expedite their receipt by using the following address:

Internal Revenue Service  
████████████████████ OP:E:EO:T:4, Room 6238  
1111 Constitution Ave, N.W.  
Washington, D.C. 20224

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

We have sent a copy of this letter to your representative as indicated in your power of attorney.

Sincerely,

(signed) ~~Gerald Sack~~  
Gerald Sack  
Chief, Exempt Organizations  
Technical Branch 4

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