



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

Date:

AUG 23 2001

Contact Person:

Identification Number:

Contact Number:

NO POSTS RECEIVED
Related copies to District

Date

Surname

Employer Identification Number

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)(4). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The reasons for our conclusion are set forth below.

You were incorporated on [redacted] under the laws of the state of [redacted]. Your stated purpose, as represented in your Articles of Incorporation, is to "decrease juvenile crime and gang activities, discourage drug use and encourage young teens to stay in school, for the betterment of the community by providing wholesome activities."

Your primary activity, in furtherance of your purpose, is the sale of products door-to-door by your youth member participants, in various neighborhoods in the state of [redacted]. Products to be sold include cookies, various candy products, scented candles, gourmet tea, novelty products geared toward children, and other products that would become available through vendors of fundraising products. You indicate that the participants do not purchase the products from you and sell them directly. A participant will receive a specific number of items to sell during that day's sales session. At the end of each day's sale session, the participant will turn over any unsold items, plus cash from the sale of items sold.

You state that your youth members participate in the program 2 to 3 days per week after school and on Saturdays. You indicate that training is done by lectures, skits and role playing, daily meetings, various sales seminars and motivational tapes. Participants are taught how to conduct themselves during presentations. They are taught how to describe the products, how to describe the program in which they are involved, and how to overcome objections. The training will be geared toward the age of the participants. You state that virtually all participants are from economically disadvantaged households.

You indicate that each participant will receive a commission of 25% of the price of each sale. Your organization will receive the remaining 75% from which you will pay for the product and the other expenses of the organization. No other person or organization receives a commission on the sales activity. Team or group leaders may receive compensation tied to

[REDACTED]

performance, but it is not anticipated that it will be a commission as such. Information provided by you indicates that the director would be paid \$ [REDACTED], the secretary/bookkeeper \$ [REDACTED], the team or group leader \$ [REDACTED], the warehouse person \$ [REDACTED], and the contract labor \$ [REDACTED]. You further state that the commission rates are market rates, considering the extras given to the participants, and would be under market rates if the participants were not given the extras. You estimate that the number of participants will be 25-40 in each locale.

In addition to door-to-door sales activity, you represent that the youth participants get monthly trips to local attractions, i.e. amusement parks, camping trips, sporting events, dances, bowling, skating, fishing trips, movies, plays, etc. Other activities include participation in food drives, and drug awareness programs.

Your revised financial data indicates that for the year [REDACTED] you expect total revenue of \$ [REDACTED]. Of this total, you expect to pay \$ [REDACTED] in participant commissions. Other salaries and wages will amount to \$ [REDACTED]. For expenses attributable to activities related to the organization's exempt purposes, you show \$ [REDACTED] in expenditures. Of this amount you do not indicate that any expenditures will be made for other than operation of your door-to-door sales business.

Section 501(c)(4) of the Code provides for the exemption from federal income tax of 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.

Section 1.501(c)(4)-1(a)(2)(ii) of the Income Tax Regulations provides that an organization is not operated primarily for the promotion of social welfare if its primary activity is carrying on a business with the general public in a manner similar to organizations that are operated for profit.

Rev. Rul. 68-45, 1968-1 C.B. 259, describes a war veterans' post whose principal source of income is from bingo games open to the general public but whose principal activity is not bingo. In concluding that the organization is primarily engaged in social welfare activities even if it receives a substantial portion of its funds from bingo, the Service emphasized the importance of determining the primary activity as opposed to the primary source of income. A determination of the primary activity requires an analysis of all the facts and circumstances.

Rev. Rul. 68-46, 1968-1 C.B. 260, describes a similar war veterans' post. After an analysis of all the facts and circumstances, the Service determined that the organization's primary activity was the conduct of a business rather than a social program. The organization rented a commercial building and operated a public banquet and meeting hall with a bar and dining facilities. Although the organization carried on veterans' programs and other social welfare activities, based on an analysis of the whole operation, the Service concluded that the business activities relating to the operation of the facility exceeded all other activities.

Rev. Rul. 61-158, 1961-2 C.B. 115, describes an organization that was created exclusively for the promotion of social welfare but whose principal activity was conducting a lottery on a weekly basis with the general public. Its principal source of income was the gross receipts from

[REDACTED]

the weekly lottery. It used the profits of the lottery for the payment of general expenses and social welfare purposes. The ruling holds that the organization is not operated exclusively for the promotion of social welfare because its primary activity is the conduct of a business for profit. Accordingly, it is not exempt under section 501(c)(4) of the Code.

Section 501(c)(4) of the Code imposes an operational test on organizations seeking exemption. Social welfare organizations are not precluded from engaging in business activities per se, either as a means of providing direct community benefit or as a means of financing their social welfare programs. Thus, in Rev. Rul. 68-45, the fact that the organization engaged in some activities characterized as business with the general public for the purpose of raising funds, rather than to provide direct community benefit, did not preclude a finding that they were nevertheless described in section 501(c)(4). An analysis of the organization's operations as a whole showed that the business of conducting veterans' activities (activities that directly benefit the community as a whole) were the organizations' "primary" activities.

On the other hand, a business activity conducted to raise funds used for the promotion of social welfare may, if it is the organization's primary activity, preclude exemption under section 501(c)(4). Thus, in Rev. Ruls. 68-46 and 61-158, exemption was precluded by a finding that the business activity of operating banquet facilities or conducting a public lottery was the organizations' primary activity. Such activities, standing alone, provide no special benefit to the community independent from the monies raised. They differ little from the operation of commercial businesses other than the fact that the profits are earmarked for social welfare purposes.

An analysis of the information you have submitted shows that the sale of various products door-to-door in the manner of an ordinary commercial business is your primary activity. That you are operating an ordinary commercial business is reflected in the fact that you will pay youth participants commissions at the market rate, that you will pay salaries at the market rate, and that your products will be sold at the market rate to the general public in the manner of other commercial door-to-door businesses. Your youth participants are prepared to conduct themselves in a manner commonly associated with salespersons working for an ordinary commercial business.

Moreover, your financial data shows that for the year [REDACTED], all of your expenses attributable to activities related to your exempt purposes will go to operation of your door-to-door sales business. You have not shown any expenses related to social welfare activities involving youth participants or the general community. Therefore, you are operated in a manner similar to the organizations described in Rev. Ruls 68-46 and 61-158 because you are primarily engaged in carrying on a business with the general public in a manner similar to organizations which are operated for profit rather than primarily promoting or conducting social welfare activities that benefit the general community.

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(4) of the Code and you must file federal income tax returns.

[REDACTED]

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 we do not hear from you within 30 days, this ruling will become final and a copy will be forwarded to the Ohio Tax Exempt and Government Entities (TE/GE) 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, TE/GE Customer Service, P.O. Box 2508, Cincinnati, OH 45201.

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

Internal Revenue Service
[REDACTED] T:EO:RA:T:4
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.

Sincerely,

(signed) Gerald V. Sack

Gerald V. Sack
Manager, Exempt Organizations
Technical Group 4