

INTERNAL REVENUE SERVICE  
DISTRICT DIRECTOR  
P O BOX 2350 ROOM 5127 ATTN: E.O.  
LOS ANGELES, CA 900532350

DEPARTMENT OF THE TREASURY

Date: APR. 5, 1991

[REDACTED]

Employer Identification Number:

[REDACTED]

Case Number:

[REDACTED]

Contact Person:

[REDACTED]

Contact Telephone Number:

[REDACTED]

Dear Applicant:

This is in reference to your application for exemption from Federal income tax as an organization described in section 501(c)(3) of the Internal Revenue Code.

In a previous contact made with your organization, you were informed that it was our opinion that you did not qualify for exemption from Federal income tax as an organization described in section 501(c)(3) of the Code. We have previously informed you of your rights of appeal in this matter and, if you were in agreement with our conclusions, we requested that you execute an agreement Form 6018.

You have indicated your agreement to our conclusion that you do not qualify for exemption from Federal income tax as an organization described in section 501(c)(3) of the Code by executing and returning the Consent to Proposed Adverse Action Form 6018.

Accordingly, we conclude that you do not qualify for exemption from Federal income tax as an organization described in section 501(c)(3) of the Code and furthermore, contributions made to you are not deductible by the donors for Federal income tax purposes.

The appropriate state officials will be notified of this action as required by section 6104(c) of the Code.

Sincerely yours,

[REDACTED]  
District Director

Letter 1633(CG)

Internal Revenue Service

Department of the Treasury

District Director

P.O. Box 2350 Los Angeles, CA 90053

Employer Identification Number:  
[REDACTED]

Case Number:  
[REDACTED]

Contact Person:  
[REDACTED]

Contact Telephone Number:  
[REDACTED]

Date:

Dear Applicant:

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

The information submitted discloses that you were formed under articles of association on [REDACTED].

Article II of your articles of association states that you were formed to bring "a fine art ~~of~~ activity for the enjoyment and edification of the citizens in the area" and that the "profits from the western art show are [to be] distributed into a scholarship fund for [REDACTED] Students or for other charitable purposes" as determined by the Board.

Your organization's sole activity is the [REDACTED] ("Show") held over a three day weekend each October. The application Form 1023 and correspondence dated [REDACTED] provides details regarding the Show. 100% of your organization's activities are devoted to the show. These activities include: attracting artists, selecting the artists to fill the [REDACTED] available spaces, advertising, scheduling the opening night wine and cheese tasting donated by the local Soroptimist organization, and organizing the annual barbecue. The Show is held at [REDACTED] in [REDACTED].

Artwork, which ranges from stationary to sculptures is selected by a panel of judges consisting of board members and local volunteers. They perform a "subjective review of the artists work and select those artists whose work is of high quality and marketable." The artwork is primarily of a western theme. There are no awards associated with this selection (the selection process is not juried).

[REDACTED]

Your organization retains a [REDACTED] % commission from the sale of the artwork which is "based on the marketplace."

Admission to the Show is \$ [REDACTED] per person. The barbecue is \$ [REDACTED] per adult and \$ [REDACTED] per child. The artwork ranges in price from \$ [REDACTED] to \$ [REDACTED] the average sale being \$ [REDACTED] to \$ [REDACTED]. A raffle is also conducted during the show for \$ [REDACTED] per ticket. Artists are not charged for their entry in the show or for the space they occupy. Program advertising is also solicited.

In [REDACTED], gross receipts for your organization consisted of:

[REDACTED]	Sales of art
[REDACTED]	Admissions and donations
[REDACTED]	Investment income
[REDACTED]	Total
[REDACTED]	Less artists commissions
[REDACTED]	Net receipts

The profits of the show are entered into a scholarship fund. [REDACTED] is responsible for distributing funds to local high school students.

In order for an organization to qualify for exemption from Federal income tax as an organization described in section 501(c)(3) of the Internal Revenue Code of 1986, it must be both organized and operated exclusively for any one or more of the purposes as set forth in that [REDACTED] section of the law.

Section 1.501(c)(3)-1(b) of the Regulations states that an organization is organized exclusively for the required purposes only when its charter or other creating documents authorizes it to carry on only activities that are in furtherance of those purposes. This "organizational test" must be met even though actual operations and other circumstances tend to reflect the required purposes.

Section 1.501(c)(3)-1(c)(1) of the Regulations provides that an organization is operated exclusively for the purposes set out in section 501(c)(3) of the Code only if substantially all of its activities are in furtherance of those purposes.

Section 1.501(c)(3)-1(e) of the Regulations provides 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 organizations' exempt purposes and if the organization is not operated for the primary purpose of carrying on an unrelated trade or business, as defined in section 513 of the Code.

In Revenue Ruling 66-178, 1966-1 C.B.138, an organization was recognized as exempt under section 501(c)(3) of the Code. It

[REDACTED]

[REDACTED]

sponsored an annual public art exhibit that gratuitously displayed the works of unknown but promising artists. Although the organization charged a nominal admission fee to the exhibit and sold a catalogue describing the exhibit at a nominal fee, the organization did not sell or offer the displayed works for sale.

Revenue Ruling 76-152, 1976-1 C.B. 151, held that an organization whose sole purpose is to select, exhibit, and sell works of its local artists on a consignment fee basis retaining a ten percent commission on sales does not qualify for tax-exemption under section 501(c)(3) of the Code. In this case the artists were being directly benefited by the exhibition and sale of their works, with the result that a major activity of the organization was serving the private interest of those artists whose works were displayed. This was the case even when commercial charges [REDACTED] were not sufficient to recover the costs of operating the gallery. Furthermore, the artists had no control over the organization or its selection process.

Your organization's Articles of Association does not limit your purposes to those specified in section 501(c)(3) of the Code. Your purposes are therefore broader than those specified in section 501(c)(3). Therefore, you do not meet the "organizational test" as you are not organized exclusively for the purposes set forth in section 501(c)(3).

As noted in the Revenue Rulings, aiding the arts is a charitable activity. Nevertheless, as section 1.501(c)(3)-1(d)(1)(ii) of the Regulations states, an organization is not organized or operated exclusively for one or more exempt purposes unless it serves public rather than a private purpose. Thus, even if an organization's purposes are truly charitable, it would still not qualify for exemption if its activities result in private benefit.

Based on the facts, the sale of artwork provides the individual artists with a prohibited direct economic benefit as stated in Revenue Ruling 76-152. The sales activity provides the artist with a direct monetary benefit and serves to enhance his/her artistic career by means of funds being collected and forwarded to them.

This benefit is not incidental as your sole activity is the Show and all of your efforts are expended to organize the Show and to sell artwork with the motive of raising funds. The artwork is not juried but rather, is chosen for its sales ability. Unlike Revenue Ruling 66-178, there is no emphasis on selecting artwork produced by unknown artists.

Furthermore, your organization retains a [REDACTED] % commission based on the marketplace. Thus the sales of artwork are done in a similar manner to a for-profit art gallery and the sales of artwork would then be considered an unrelated trade or business. The commissioned

sales of artwork does not contribute importantly to the promotion of arts in general.

Accordingly, as you are neither organized nor operated for one or more exempt purposes, you are not entitled to exemption from Federal income tax as an organization described in section 501(c)(3) of the Code. Since your purposes are "not exclusively" limited to those purposes contemplated by section 501(c)(3) of the Code, you fail to meet the organizational test. Moreover, the sales of artwork is your primary activity. Not only is this activity considered an unrelated trade or business, the primary conduct of which is prohibited by Regulations section 1.501(c)(3)-1(4), but it also results in direct private benefit to individual persons (the artists) which is prohibited by Regulations section 501(c)(3)-1(d)(1)(ii). Therefore, you do not meet the operational test.

You are required to file Federal income tax returns annually, with you District Director.

Contributions to you are not deductible under section 170.

As provided by section 6104(c) of the Internal Revenue Code of 1986 and the applicable regulations, the appropriate State officials are being notified of our determination.

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 on the reverse side of this 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 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 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 we do not hear from you within 30 days from the date of this letter, and you do not protest this proposed determination in a timely manner, 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

[REDACTED]

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 or the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service."

Sincerely yours,

District Director

Enclosures:  
Publication 892  
Form 6018