

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

Date: NOV 30 2001

Contact Person:

ID Number:

Telephone Number:

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)(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 are formed under the laws of the State of [REDACTED] as an irrevocable trust. Your trust document provides that you are organized and operated exclusively to support or benefit, as defined by section 1.509(a)-4(b)(1) of the Income Tax Regulations, one or more publicly supported organizations. Notwithstanding any other provision hereof, you shall not conduct or carry on any activities not permitted to be conducted or carried on by an organization which is tax exempt or by an organization donations to which are deductible from taxable income to the extent allowed by the provisions of the Code.

[REDACTED] and [REDACTED] are your donors and [REDACTED] is also your trustee. They are also disqualified persons since they are substantial contributors to you. As your trustee, [REDACTED] may receive donations from the donors, or from any other source in cash and may accept donations from the donors, or from any other source in property other than cash that is acceptable to him. Your principal financial support will be contributions by [REDACTED] and [REDACTED] and not fundraising activities.

Your trust document requires the trustee to distribute [REDACTED] percent of your net income to [REDACTED] to help [REDACTED] perform its functions and carry out its purposes. Each year your board shall meet with the board of [REDACTED] to determine the use of such distributions. Prior to making any donation or distribution, you shall obtain written confirmation that [REDACTED] is currently recognized as a tax exempt organization under section 501(c)(3) of the Code. You are also required to give periodic accountings (at least annually) to [REDACTED].

[REDACTED]

In addition to the distribution to be made to [REDACTED] each year, your trustee shall distribute a total of [REDACTED] percent of your net income to one or more of the 501(c)(3) tax exempt organizations listed on Schedule A or to [REDACTED] as is directed by your board in writing signed by at least three members. If at any time [REDACTED] is not an organization to which distributions can be made by an organization described in section 509(a)(3) of the Code, then your board shall select an organization from those listed on Schedule A and such organization shall be entitled to all of the rights and benefits as are herein designated for [REDACTED].

Your trustee may determine, in his sole and complete discretion, that the amount of funds in your trust is too small to economically administer, and distribute the funds outright and free of trust to such organization or organizations as described in section 170(c)(2) of the Code.

However, your dissolution clause provides that if you do not obtain tax exempt status under sections 501(c)(3) and 509(a)(3) of the Code, your assets shall go to the [REDACTED] family as a contingent remainder.

Your trustee shall have the power to retain any asset originally or later contributed to the trust estate whether or not such asset be of a character permissible for investment by fiduciaries; to retain and purchase assets notwithstanding the lack of diversification of the trust assets; to retain, purchase, sell or exchange any and all stocks, bonds, notes or other securities or any variety of real or personal property including stocks or interest in investments or mutual funds; to change the situs of the trust and of any property which is part of the trust to any place in the United States of America or any other country; and to make distributions of principal or income in kind. However, any of the powers, duties or authority given to the trustee may be exercised and is under the control of and by the board which shall be evidenced by a writing given to the trustee and signed by at least three members of the board. The board may remove your trustee as long as the trustee is given written notice of such removal signed by a member of the [REDACTED] family and one other board member.

Your board shall consist of five members. [REDACTED] or its designated agent has appointed [REDACTED] to your board. Two of your board members shall be from the class consisting of [REDACTED] and [REDACTED] and each of their descendants (the [REDACTED] Family). The other members of the board shall be appointed by a majority vote by the remaining members of your board. Your initial remaining board members are [REDACTED] and [REDACTED]. [REDACTED] and [REDACTED] are married to each other. Both [REDACTED] and [REDACTED] are vice presidents of [REDACTED]. [REDACTED] is the brother of [REDACTED], the attorney who is assisting you in applying for exempt status under section 501(c)(3) of the Code. The minutes from your first meeting state that the above named persons are board members for life.

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The current board members of ██████████ are ██████████, ██████████, and ██████████. In ██████████, ██████████ had \$██████████ in income. You state that in ██████████ and ██████████ you had assets totaling \$██████████. Although you state that at least ██████████ percent of your net income will be given to ██████████, you have not submitted information stating how much net income you have earned. Aside from your initial meetings and the meeting regarding the application process, you have not conducted any activities or distributed any funds.

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for, among others, charitable 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(d)(2) of the Income Tax Regulations provides, in part, that the term "charitable" is used in its generally accepted legal sense.

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

Section 1.501(c)(3)-1(b)(4) provides that an organization is not organized exclusively for one or more exempt purposes unless its assets are dedicated to an exempt purpose. An organization's assets will not be considered to meet the organizational test if its articles or law of the State in which it was created provide that its assets would, upon dissolution, be distributed to its members or shareholders.

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 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 provides that an organization is not organized exclusively for any of the purposes specified in section 501(c)(3) unless it serves public rather than private interests. Thus, to meet the requirement 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(a)-1(c) of the regulations provides that private shareholders or individuals are defined as persons having a personal and private interest in the activities of an organization.

In Better Business Bureau v. United States, 326 U.S. 279 (1945), the Supreme Court

stated that the presence of a single nonexempt purpose, if substantial in nature, will preclude exemption under section 501(c)(3) of the Code, regardless of the number or importance of statutorily exempt purposes. Thus, the operational test standard prohibiting a substantial nonexempt purpose is broad enough to include inurement, private benefit, and operations which further nonprofit goals outside the scope of section 501(c)(3).

Rev. Rul. 64-182, 1964-1 (Part 1) C.B. 186, holds that a corporation is entitled to exemption from federal income tax as a corporation organized and operated exclusively for charitable purposes within the meaning of section 501(c)(3) of the Code where it is shown to be carrying on through contributions and grants to other charitable organizations a charitable program commensurate in scope with its financial resources.

In P.L.L. Scholarship v. Commissioner, 82 T.C. (1984), an organization operated bingo at a bar for the avowed purpose of raising money for scholarships. The board included the bar owners, the bar's accountant, also a director of the bar, as well as two players. The board was self-perpetuating. The Court reasoned that since the bar owners controlled the organization and appointed the organization's directors, the activities of the organization could be used to the advantage of the bar owners. The organization claimed that it was independent because there was separate accounting and no payments were going to the bar. The Court was not persuaded.

A realistic look at the operations of these two entities, however, shows that the activities of the taxpayer and the Pastime Lounge were so interrelated as to be functionally inseparable. Separate accountings of receipts and disbursements do not change that fact.

An organization is not organized exclusively for one or more exempt purposes unless its assets are dedicated to an exempt purpose. Your trust provides that if you do not qualify under sections 501(c)(3) and 509(a)(3) of the Code that your assets will revert to the Eastman family as a contingent remainder. Therefore, you do not satisfy the organizational test and are not exempt under section 501(c)(3).

In addition, you are operated in a manner similar to the organization in P.L.L. Scholarship, supra. Your donors appointed two members to your board with whom they have a business relationship. Your donors also have an indirect relationship with the director appointed by [REDACTED] because [REDACTED] is the brother of the lawyer selected by the [REDACTED] to assist in the exemption application process. According to your minutes, all of your directors serve for life. Since your donors control you and appoint your directors, your activities could be used to the advantage of your donors. Therefore, you are not operated exclusively for charitable purposes under section 501(c)(3) of the Code because you serve private, rather than public interests.

Furthermore, even if you were exempt under section 501(c)(3), you would be a private

foundation under section 509(a). Section 509(a)(3)(A), in effect, describes as a public charity, an organization which is organized and at all times thereafter is operated, exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more specified organizations described in paragraph (1) and (2).

Section 509(a)(3) of the Code provides that the term "private foundation" does not include an organization which

(A) is organized, and at all times thereafter is operated, exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more specified organizations described in section 509(a)(1) or (2),

(B) is operated, supervised, or controlled by or in connection with one or more organizations described in section 509(a)(1) or (2), and

(C) is not controlled directly or indirectly by one or more disqualified persons (as defined in section 4946) other than foundation managers and other than one or more organizations described in section 509(a)(1) or (2).

Section 509(a)(3)(B) of the Code provides that, in order to qualify under section 509(a)(3), an organization must be "operated, supervised, or controlled by," "supervised or controlled in connection with," or "operated in connection with" one or more publicly supported organizations.

Section 1.509(a)-4(g)(1) of the Income Tax Regulations provides that an "operated, supervised, or controlled by" relationship is established by the fact that a majority of the officers, directors, or trustees of the supporting organization are appointed or elected by the governing body, members of the governing body, officers acting in their official capacity, or the membership of one or more publicly supported organizations.

Section 1.509(a)-4(h)(1) of the regulations provides that a "supervised or controlled in connection with" relationship involves control or management of the supporting organization in the same persons that control or manage the publicly supported organizations.

Section 1.509(a)-4(i)(1) of the regulations provides that to have an "operated in connection with" relationship, an organization must meet a "responsiveness test" and an "integral part test."

Section 1.509(a)-4(i)(3)(i) of the regulations provides generally that a supporting organization will be considered to meet the "integral part test" if it maintains a significant involvement in the operations of one or more publicly supported organizations and such publicly supported organizations are in turn dependent upon the supporting organization for the type of

support which it provides. In order to meet this test, either section 1.509(a)-4(i)(3)(ii) or (iii) must be satisfied.

Section 1.509(a)-4(i)(3)(ii) of the regulations provides one "integral part" test: the activities engaged in for or on behalf of the publicly supported organizations are activities to perform the functions of, or to carry out the purposes of, such organizations, and, but for the involvement of the supporting organization, would normally be engaged in by the publicly supported organizations themselves.

Section 1.509(a)-4(i)(3)(iii)(a) of the regulations provides an alternative "integral part" test: the supporting organization makes payments of substantially all of its income to or for the use of one or more publicly supported organizations, and the amount of support received by one or more of such publicly supported organizations is sufficient to insure the attentiveness of such organizations to the operations of the supporting organization. In addition, a substantial amount of the total support of the supporting organization must go to those publicly supported organizations which meet the attentiveness requirement of section 1.509(a)-4(i)(3)(iii) with respect to such supporting organization. Except as provided in section 1.509(a)-4(i)(3)(iii)(b), the amount of support received by a publicly supported organization must represent a sufficient part of the organization's total support so as to insure such attentiveness. In applying the preceding sentence, if such supporting organization makes payments to, or for the use of, a particular department or school of a university, hospital or church, the total support of the department or school shall be substituted for the total support of the beneficiary organization.

Section 1.509(a)-4(i)(3)(iii)(b) of the regulations provides that even where the amount of support received by a publicly supported beneficiary organization does not represent a sufficient part of the beneficiary organization's total support, the amount of support received from a supporting organization may be sufficient to meet the requirements of this subdivision if it can be demonstrated that in order to avoid the interruption of the carrying on of a particular function or activity, the beneficiary organization will be sufficiently attentive to the operations of the supporting organization. This may be the case where either the supporting organization or the beneficiary organization earmarks the support received from the supporting organization for a particular program or activity, even if such program or activity is not the beneficiary organization's primary program or activity so long as such program or activity is a substantial one.

Section 1.509(a)-4(i)(3)(iii)(d) of the regulations provides that all pertinent factors, including the number of beneficiaries, the length and nature of the relationship between the beneficiary and supporting organization and the purpose to which the funds are put (as illustrated by sections 1.509(a)-4(i)(3)(iii)(b) and (c)), will be considered in determining whether the amount of support received by a publicly supported beneficiary organization is sufficient to insure the attentiveness of such organization to the operations of the supporting organization. Normally the attentiveness of a beneficiary organization is motivated by reason of the amounts received from the supporting organization. Thus, the more substantial the amount involved, in

terms of a percentage of the publicly supported organization's total support the greater the likelihood that the required degree of attentiveness will be present. However, in determining whether the amount received from the supporting organization is sufficient to insure the attentiveness of the beneficiary organization to the operations of the supporting organization (including attentiveness to the nature and yield of such supporting organization's investments), evidence of actual attentiveness by the beneficiary organization is of almost equal importance. An example of acceptable evidence of actual attentiveness is the imposition of a requirement that

the supporting organization furnish reports at least annually to the beneficiary organization to assist such beneficiary organization in insuring that the supporting organization has invested its endowment in assets productive of a reasonable rate of return (taking appreciation into account) and has not engaged in any activity which would give rise to liability for a tax imposed under sections 4941, 4943, 4944, and 4945 of the Code if such organization were a private foundation. The imposition of such requirement is, however, merely one of the factors in determining whether a supporting organization is complying with section 1.509(a)-4(i)(3)(iii) of the regulations and the absence of such requirement will not preclude an organization from classification as a supporting organization based on other factors.

Section 1.509(a)-4(i)(3)(iii)(e) of the regulations provides that however, where none of the beneficiary organizations is dependent upon the supporting organization for a sufficient amount of the beneficiary organization's support within the meaning of section 1.509(a)-4(i)(3)(iii), the requirements of section 1.509(a)-4(i)(3) will not be satisfied, even though such beneficiary organizations have enforceable rights against such organization under State law.

You have failed to establish that you meet the relationship test of section 509(a)(3)(B) of the Code. You are not "operated, supervised, or controlled by" the Foundation, as a majority of your trustees are not appointed or elected by the Foundation. You are not "supervised or controlled in connection with" the Foundation, as your trustees do not also control or manage the Foundation. You are not "operated in connection with" the Foundation because you do not meet the integral part test under section 1.509(a)-4(i)(3) of the regulations.

Section 1.509(a)-4(i)(3) of the regulations provides that the integral part test will be satisfied if the supporting organization maintains a significant involvement in the operations of one or more publicly supported organizations and such publicly supported organizations are in turn dependent upon the supporting organization for the type of support which it provides.

Section 1.509(a)-4(i)(3)(iii) of the regulations has three basic requirements: (1) the supporting organization must pay substantially all of its income to or for the use of one or more publicly supported organizations; (2) the amount of support received by one or more of such publicly supported organizations must be sufficient to ensure the attentiveness of such organizations to the operations of the supporting organization; and (3) a substantial amount of the total support of the supporting organization must go to those publicly supported

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organizations which meet the attentiveness requirement.

The facts in your case show that you satisfy the first requirement because you are required to pay all of your net income to publicly supported organizations. However, you have failed to satisfy the second requirement, the showing of the requisite attentiveness on the part of one or more of the supported organizations.

Section 1.509(a)-4(i)(3)(iii) of the regulations sets forth in subdivisions (a), (b), and (d) three ways of meeting the attentiveness requirement. The first of these concerns the situation where the amount of support provided to a supported organization represents a sufficient amount of its total support so as to insure its attentiveness. Although we requested the amount of your net income, you failed to respond with the information. Since you have provided insufficient information for us to make this determination, you do not satisfy this requirement for meeting the attentiveness test.

Another way of determining whether the amount of support received by a publicly supported beneficiary organization is sufficient to ensure the attentiveness of such organization to the operations of the supporting organization is to consider all the pertinent factors, including the number of beneficiaries, the length and nature of the relationship between the beneficiary and supporting organization and the purpose to which the funds are put. In this case, there is no evidence or history demonstrating that ██████████ has shown attentiveness.

Based on the above, you have not established that you maintain a significant involvement in the operations of ██████████ and that it is dependent upon you for the type of support that you provide.

Section 1.509(a)(4)(j) of the regulations provides that a supporting organization cannot be controlled (50% voting power or veto power) directly or indirectly by disqualified persons except for foundation managers and publicly-supported organizations. An organization will be considered controlled if the disqualified persons can by aggregating their votes or positions of authority cause the organization to act or prevent the organization from acting.

Rev. Rul. 80-207, 1980-2 C.B. 113, provides an example of indirect control. In Rev. Rul. 80-207, two of the four supporting organization directors were also employees of a corporation in which the substantial contributor to the organization owned more than 35 percent of the voting power of the corporation. This individual was also a director of the supporting organization. Because of the employment relationship of the two employee board members, Rev. Rul. 80-207 concluded that the supporting organization was controlled indirectly by the disqualified person.

Rev. Rul. 80-207 provides the following analysis:

Because only one of the organization's directors is a disqualified person and neither the

disqualified person nor any other director has a veto power over the organization's actions, the organization is not directly controlled by a disqualified person under section 1.509(a)-4(j) of the regulations. However, in determining whether an organization is indirectly controlled by one or more disqualified persons, one circumstance to be considered is whether a disqualified person is in a position to influence the decisions of members of the organization's governing body who are not themselves disqualified persons. Thus, employees of a disqualified person will be considered in determining whether one or more disqualified persons control 50 percent or more of the voting power of an organization's governing body.

Rev. Rul. 80-207 clarifies that all pertinent facts and circumstances will be considered in determining whether a disqualified person does in fact indirectly control a supporting organization such as through a position of influence.

In Rev. Rul. 80-305, 1980-2 C.B. 71, an organization was created to receive donations, to pool them in a common fund, and to distribute all of its income to organizations that are publicly supported organizations under section 509(a)(1). Each donor has the right to designate annually the recipient of such portion, subject to the requirement that the recipient be a publicly supported organization under section 509(a)(1), and to direct the payment, to an organization described in section 509(a)(1), of the corpus in the common fund attributable to his or her contribution. The trust is subject to the control of the distribution committee of a community trust that is a publicly supported organization described in sections 170(b)(1)(A)(vi) and 509(a)(1) of the Code. If a donor does not exercise his right to designate a recipient, the funds are disbursed as the distribution committee may direct. The distribution committee also has the power to replace the trustee for breach of fiduciary duty or failure to earn a reasonable rate of return on the trust principal. The Service held that the donor's right to designate recipients constitutes "control" by substantial contributors for purposes of section 509(a)(3)(C) of the Code. Accordingly, the organization failed to meet the requirements to be a 509(a)(3) supporting organization of the community trust.

Based on the above facts, disqualified persons control your board selection process and with it your activities. Since two of your directors are disqualified persons, two are business partners in the same firm as the disqualified persons and the fifth is the brother of the legal consultant who is assisting you in the application process for 501(c)(3) exemption, disqualified persons indirectly control you in a manner similar to the situation in Rev. Rul. 80-207, including indirectly controlling the timing, manner, amount or other terms of donations/assets and distributions. In addition, your trust instrument gives the donors and the trustees selected by them the power to designate charitable recipients similar to the situation in Rev. Rul. 80-305. Therefore, you are indirectly controlled by one or more disqualified persons within the meaning of section 509(a)(3)(c) of the Code and are not excluded from private foundation status under section 509(a)(3). Therefore, you are a private foundation within the meaning of section 509(a) of the Code.

[REDACTED]

In addition and separately, operation of the donor advised fund may be a further indication of the control by disqualified persons. Section 1.509(a)-4(j)(1) of the regulations provides that the authority of the disqualified persons to designate among a group of specified supported organizations those organizations to be supported for the year may constitute control of the supported organization within the meaning of section 509(a)(3) of the Code.

Accordingly, you do not qualify as an organization described in sections 501(c)(3) and 509(a)(3) of the Code and you must file federal income tax returns.

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 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. 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

[REDACTED]
1111 Constitution Ave, N.W.
Washington, D.C. 20224

[REDACTED]

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

Sincerely,

/s/

[REDACTED]
Manager, Exempt Organizations
Technical Group 4