

no protest received  
3/5/93

Internal Revenue Service

Department of the Treasury

District  
Director

P.O. Box 2508  
Cincinnati, OH 45201

Date: FEB 03 1993

Person to Contact:

Telephone Number:

Refer Reply to:

EP/EO

Employer Identification Number:

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under the provisions of section 501(c)(3) of the Internal Revenue Code of 1986 and its applicable Income Tax Regulations. Based on the available information, we have determined that you do not qualify for the reasons set forth on Enclosure I.

Consideration was given to whether you qualify for exemption under other subsections of section 501(c) of the Code and we have concluded that you do not.

As your organization has not established exemption from Federal income tax, it will be necessary for you to file an annual income tax return on Form 1041 if you are a trust or Form 1120 if you are a corporation or an unincorporated association. Contributions to you are not deductible under section 170 of the Code.

If you are in agreement with our proposed denial, please sign and return one copy of the enclosed Form 6018, Consent to Proposed Adverse Action.

You have the right to protest this proposed determination if you believe that it is incorrect. To protest, you should submit a written appeal giving the facts, law and other information to support your position as explained in the enclosed Publication 892, "Exempt Organizations Appeal Procedures for Unagreed Issues". The appeal must be submitted within 30 days from the date of this letter and must be signed by one of your principal officers. You may request a hearing with a member of the office of the Regional Director of Appeals when you file your appeal. If a hearing is requested, you will be contacted to arrange a date for it. The hearing may be held at the Regional Office, or, if you request, at any mutually convenient District Office. If you are to be represented by someone who is not one of your principal officers, he or she must file a proper power of attorney and otherwise qualify under our Conference and Practice Requirements as set forth in Section 601.502 of the Statement of Procedural Rules. See Treasury Department Circular No. 230.

11/17/92

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[REDACTED]

If 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. Section 7428(b)(2) of the Internal Revenue Code provides in part that:

A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, 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 the time specified, this will become our final determination. In that event, appropriate State officials will be notified of this action in accordance with the provisions of section 6104(c) of the Code.

Sincerely yours,

[REDACTED]

District Director

Enclosures: 3

cc: [REDACTED]

ENCLOSURE I

[REDACTED]

A review of your application and subsequent correspondence states that you were incorporated in the State of [REDACTED] on [REDACTED]. Your Articles of Incorporation state that your purposes, in part, are:

To operate and maintain, as a non-profit corporation, a nursery school for children of the ages from nine (9) months to eleven (11) years (more or less), providing educational opportunities, extending said services to boys and girls, regardless of prior conditions of servitude or of their color or sex, in an attempt to instill within these children an educational awareness and in addition to this step in childhood development, to provide early childhood training; and in any other lawful and legal manner to instill educational aspirations within the children coming to said corporation for educational guidance; to provide a center of educational guidance for said children, to instruct them in a lawful manner and to educate said children by all lawful means and manner in such a way as to make them constructive citizens and useful children; to enhance their learning abilities, and to do all things incident thereto.

You amended your Articles of Incorporation on [REDACTED] to add the provisions of section 501(c)(3) of the Internal Revenue Code. You do not have a separate set of Bylaws.

You have been operating on a stock basis. There were [REDACTED] shares of common stock issued to [REDACTED] shareholders. [REDACTED] owns [REDACTED] shares, and [REDACTED], [REDACTED] and [REDACTED] each own [REDACTED] shares. These shareholders are also your officers. [REDACTED], president, [REDACTED], vice-president, [REDACTED], treasurer, and [REDACTED], secretary, are family members. [REDACTED] is the mother of [REDACTED] and [REDACTED] and a sister of [REDACTED]. [REDACTED] receives an annual salary of \$[REDACTED]. The remaining officers do not receive compensation.

[REDACTED] and her family still own these [REDACTED] shares of common stock. Your stock can only be sold back to the corporation or to your shareholder(s) at the current book value.

You have been operating as a for profit corporation for [REDACTED] years. You had filed Form 1120 from [REDACTED] through [REDACTED]. You have never operated as a nonprofit corporation since your incorporation.

Your response to our letter dated [REDACTED] stated that you decided to apply for exemption after [REDACTED] years in operation in order to take advantage of the various programs offered by the local government. For example, a nonprofit organization will be eligible to receive funds to help purchase food for low income groups of children enrolled in your school. A nonprofit organization is eligible to

receive funds to do any kind of repairs to the building. Also, some parents will give you funds, equipment or other assets if you are a nonprofit organization.

Your service fees are the same as those charged by a for profit corporation.

Section 501(c)(3) of the Code provides, in part, for the exemption from Federal income tax of organizations organized and operated exclusively for charitable, religious 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 states that in order to qualify under section 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more exempt purposes. If an organization fails to meet either the organizational or operational test, it is not exempt.

Section 1.501(c)(3)-1(a)(2) of the Regulations states that the term "exempt purpose or purposes", means any purpose or purposes specified in section 501(c)(3) of the Code.

Section 1.501(c)(3)-1(b)(4) of the Regulations requires assets of the organization must dedicate to an exempt purpose.

Section 1.501(c)(3)-1(c)(1) of the Regulations states 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) of the Code. 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 operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. It must not be operated for the benefit of designated individuals or the persons who created it.

Section 502(a) of the Internal Revenue Code states that an organization which operates 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 organizations exempt from taxation under section 501 of the Internal Revenue Code.

Revenue Ruling 67-5, C.B. 1967-1, 123, states a foundation controlled by the creator's family and operated to serve the private interests of the creator and his family is not entitled to exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code.

Revenue Ruling 66-225, - C.B. 1966-2, 227 states that an organization formed by the owner of a regular, for profit business is not entitled to exemption when the organization is used as a part of the private business.

Your stock redemption policy contravenes section 1.501(c)(3)-1(b)(4) of the Regulations which requires the organization's assets to be permanently dedicated to exempt purposes.

Although you were incorporated as a nonprofit corporation, you have operated as a for profit corporation. You operate a trade or business for profit or benefit of the shareholders. [REDACTED] and her family members have been your officers and stockholders since your creation.

After [REDACTED] years in operation, you decided to apply for exemption so you could take advantage of the exempt status. There is no indication of change in your operation. Your method of operation is still the same. You are in competition with a for profit corporation. Accordingly, your operation furthers the private benefit of the shareholders and lacks a significant charitable accomplishment.

Furthermore, section 502 of the Internal Revenue Code states that an organization shall not qualify for exemption under section 501 on the ground that it uses all of its net income for charitable purposes if its primary purpose is conduct a trade or business for profit. You have been operating a family business. Section 502 of the Internal Revenue Code prohibits exemption to such organization.

Based on information submitted, you do not meet the operational test under section 501(c)(3) of the Internal Revenue Code. Therefore, we conclude that you do not meet the requirements to qualify for exemption under section 501(c)(3) or any other section of the Internal Revenue Code.

This is a denial letter.