

Internal Revenue Service

Department of the Treasury

District
Director

Baltimore District

▷

[REDACTED]

Person to contact:

Telephone Number:

Refer to:

CERTIFIED MAIL

FEB 08 1990

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under Section 501(c)(3) of the Internal Revenue Code and have determined that you do not qualify for exemption under that section. Our reasons for this conclusion and the facts on which it is based are explained below.

The evidence submitted indicates that you were incorporated [REDACTED] to advertise and promote the coordinated distribution and sale of authentic reproductions, adaptations, and interpretations of eighteenth century objects (Products) drawn from those items collected or approved by [REDACTED].

The Articles of Incorporation do not provide that the corporation is organized exclusively for 501(c)(3) purposes. In addition, the articles state that in the event of the dissolution of the corporation, all of its property not needed to provide for the payment of its debts and expenses shall be transferred to Colonial Williamsburg.

Further the Articles provide that [REDACTED] shall be a member of the corporation, and that other members of the corporation shall be parties licensed by [REDACTED] to manufacture the approved Products and have paid the amount assessed by the board of directors against them, respectively, for the next preceding fiscal year for the purpose of funding the operations of the corporation.

The articles provide that the corporation shall be managed by a board of directors, who shall have and exercise all the voting power of the corporation except the power to elect certain directors upon the expiration of their terms. The number of directors, until changed by the by-laws, shall be eight, two of whom shall be ex officio and six of whom shall be elected members. Two persons designated from

time to time by the president of [REDACTED] shall be ex officio directors with full voting power; any vacancy created by the incapacity, death or resignation of an ex officio director shall be filled promptly by the [REDACTED] president. The other six directors shall serve for terms of one year each and shall be elected annually by the members. A director (other than ex officio directors) may be removed from office, with or without cause, at any time at a meeting of the board of directors expressly called for that purpose.

In the additional information provided you list the corporation's current activities as:

1. Promoting the establishment of "[REDACTED]". A "[REDACTED]" is space within a retail establishment dedicated to the sale of Reproductions. You further state that the retailers are not associated with the Foundation other than through normal business transactions.
2. Distribution of printed educational materials which identify Reproductions with their antique counterparts.
3. Supporting existing "[REDACTED]" in the following manner:
 - a. Educating employees of "[REDACTED]" in the history of colonial [REDACTED] during an annual seminar.
 - b. Informing "[REDACTED]" about new Reproductions.
 - c. Ensuring that the operation of the "[REDACTED]" complies with standards established by the corporation.
4. Operating [REDACTED] showrooms where manufacturers may display Reproductions to potential retailers. The manufacturers may subsequently enter into purchase arrangements with the retailers.

You have stated that [REDACTED]% of the corporation's total time and effort is expended in accomplishing the above stated activities.

You have indicated that the activities are coordinated by employees of the Foundation ([REDACTED]) in conjunction with representatives of manufacturers licensed by the Foundation ([REDACTED]). You further indicate that the manufacturers and the Foundation ([REDACTED]) pay membership fees to the corporation to support the activities.

These fees are calculated as a percentage of net sales of Reproductions sold by the members in the preceding year. In order to participate in the benefits provided by this corporation, an organization must be licensed by the Foundation () to manufacture Reproductions to Foundation () standards and must have paid membership fees to the corporation.

You have indicated that the corporation's activities have promoted a wider understating and appreciation of the Foundation's () educational mission. Reproductions, and the accompanying educational materials, teach the history of early America by allowing individuals, some of whom may never visit historic (), to experience first-hand a re-creation of a portion of life in the eighteenth-century and encourage their visit to museums operated by the Foundation ().

You have indicated that the corporation does not have employees, it does however pay a consulting fee to the Foundation () for services rendered by three Foundation () employees on behalf of the corporation. Consulting fees were \$ () for the period () to () and \$ () for the fiscal year ended ().

You indicated that the consultants serve as representatives of (), that they do not act as salesman for Reproductions, that they devote substantially all of their time to the corporation and that the consulting fee is agreed upon by the Foundation () and the board of the corporation. You have also indicated that the consulting fee is reviewed and approved by the board annually during the budget process and that the corporation does not pay personal living expenses of any individuals.

Section 501(c)(3) of the Code provides for the exemption from federal income tax for organizations organized and operated exclusively for charitable, educational, religious, or scientific purposes, no part of the net earnings of which inures to the benefit of any private shareholders or individuals. A shareholder refers to anyone having a personal and private interest.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations provides that to be exempt 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 the operational test it is not exempt.

Section 1.501(c)(3)-1(b) of the Regulations provides that an organization is organized exclusively for exempt purposes only if its creating document limits its purposes and powers to those which are within the scope of Section 501(c)(3).

Section 1.501(c)(3)-1(c)(2) of the Regulations provides, in part, that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or part to the benefit of private shareholders or individuals.

Section 1.501(c)(3)-(d)(ii) of the Regulations provides that an organization is not organized and operated exclusively for one or more exempt purposes specified in Section 501(c)(3) unless it serves a public rather than a private interest. Thus, to meet the requirements of Section 501(c)(3), it is necessary for an organization to establish that it is not organized or operated for the benefit of private interest such as designated individuals.

Section 501(c)(3)-1(b)(4) of the Regulations further provides that an organization is not organized exclusively for 501(c)(3) purposes unless its assets are dedicated to an exempt 501(c)(3) purpose. To meet this requirement, an organization's creating document must provide that, in the event of dissolution, assets will be distributed for one or more 501(c)(3) purposes, or to the Federal government or a State or local government, for public purposes.

Revenue Ruling 73-104, CB 1977-1, 263 states that "The sale of greeting card reproductions of art works by an art museum exempt from tax under Section 501(c)(3) of the Code does not constitute unrelated trade or business." The organization sells the cards in the shop it operates in the museum.

Revenue Ruling 73-105, CB 1977-1, 264 states that "The sale of scientific books and city souvenirs by a museum of folk art exempt from tax under Section 501(c)(3) of the Code constitutes unrelated trade or business even though other items sold in the museum shop are related to its exempt function." The organization maintains and operates an art museum devoted to the exhibition of American folk art. It operates a shop in the museum...

Our review of your application indicates that your organization does not meet either the organizational or operational test's to be exempt under Section 501(c)(3). Your purposes are broader than those allowed by Section 501(c)(3) and your Articles of Incorporation do not contain a dissolution provision which satisfies Section 1.501(c)(3)-1(b)(4) of the Income Tax Regulations. Therefore you do not meet the organizational test of Section 501(c)(3).

You also fail to meet the operational test to be exempt because the "██████████" provide a sales outlet promoting sales for the manufacturer members, thus increasing their sales. This is an economic benefit to them and does not promote the purposes of this organization. This is an exploitation of the name and good will of ██████████. An economic benefit and unfair advantage occurs when sales are made by the licensed parties; those unlicensed lose sales. (We note that the items actually sold by "██████████" are only licensed items. However, similar items are sold by numerous retail outlets across the country.)

Further the "██████████" are not operated, in or for that fact near the museum, ██████████. The ██████████ "██████████" are located in ██████████. Both Revenue Rulings 73-104 and 73-105 provide for museum shops located in the museums, not hundreds of miles away.

Because of the incorporated structure ██████████ has full and final control over the operation by:

1. naming the two ex-officio members of the board,
2. by having final determination on the other members who may serve.
3. by the fact that ██████████ selects only those manufacturers who are licensed to produce Products for ██████████, thus an unfair advantage.

Because your organization does not meet the organizational test by having purposes broader than those contemplated by Section 501(c)(3) of the Code nor meet the operational test because the activities promote inurement of income and private benefit as contemplated by Section 501(c)(3) your application for exempt status is denied.

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

If you do not agree with our determination, you may request consideration of this matter by the Office of Regional Director of Appeals. To do this, you should file a written appeal as explained in the enclosed Publication 892. Your appeal should give the facts, law and any other information to support your position. If you want a hearing, please request it when you file your appeal and you will be contacted to arrange a date. The hearing may be held at the regional office, or, if you request, any mutually convenient district office. If you will be represented by someone who is not one of your principal officers, that person will need to file a power of attorney or tax information authorization with us.

If you do not appeal this determination within 30 days of the date of this letter, as explained in Publication 892, enclosed, this letter will become our final determination in the matter. Further, if you do not appeal this 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, "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."



District Director

Enclosure:
Publication 892
Envelope

cc: 