



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

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

Release Number: 200733027  
Release Date: 8/17/07  
Date: May 21, 2007

UIL Code:  
501.03-00

Employer Identification Number:

Person to Contact and ID Number:

Contact Telephone Number:

Form Required To Be Filed:  
1120

Tax Years:

Dear :

This is our final determination that you do not qualify for exemption from Federal income tax under Internal Revenue Code section 501(a) as an organization described in Code section 501(c)(3).

We made this determination for the following reason(s):

You have not established that you are organized and operated exclusively for charitable purposes under section 501(c)(3) of the Code and 1.501(c)(3)-1(a) of the Income Tax Regulations. In addition, you are operating a trade or business that primarily furthers a commercial rather than an exempt purpose specified in section 501(c)(3) of the Code. See section 1.501(c)(3)-1(e)(1) of the regulations.

Because you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file Federal income tax returns on the form for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office.

If you decide to contest this determination under the declaratory judgment provisions of Code section 7428, you must initiate a suit in the United States Tax Court, the United States Court of Federal Claims, or the District Court for the District of Columbia before the 91<sup>st</sup> day after we mailed this letter to you. Contact the clerk of the appropriate court for rules for initiating suits for declaratory judgment. Filing a declaratory judgment suit under Code section 7428 does not stay the requirement to file returns and pay taxes.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, Notice of Intention to Disclose, and review the two attached letters that

show our proposed deletions. If you disagree with our proposed deletions, you should follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

In accordance with Code section 6104(c), we will notify the appropriate State officials of our determination by sending them a copy of this final letter and the proposed adverse letter. You should contact your State officials if you have any questions about how this determination may affect your state responsibilities and requirements.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at 1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Robert Choi  
Director, Exempt Organizations  
Rulings and Agreements

Enclosures  
Notice 437  
Redacted Proposed Adverse Determination Letter  
Redacted Final Adverse Determination Letter



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

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

Date: October 17, 2006

Person to Contact:

Identification Number:

Contact Telephone Number:

FAX Number:

Employer Identification Number:

UIL Code:  
501.03-00

Legend:

L =

Date x =

Dear :

We have considered your application for recognition of exemption from Federal income tax under Internal Revenue Code section 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under Code section 501(c)(3). The basis for our conclusion is set forth below.

**FACTS**

You were incorporated on Date x under the laws of the State of L as a non-profit corporation. According to your organizational documents, you were formed for the purpose of "supplying used competition Ski Boats to non-profit youth camps" exempt from taxation under section 501(c)(3) of the Code. Your by-laws state that you will procure and place (by sale or gift) and transport good, used, competition ski boats to non-profit youth camps wanting to purchase them. Further, your by-laws state that you will receive these boats from the public as charitable donations. In order to receive donations, your contributors will require a tax deductible receipt.

You will operate by placing advertisements in newspapers asking the public to donate boats. Upon receiving the boats as a donation, you will fix and detail them, and subsequently market and sell them to the non-profit camp customer at their annual meetings. You will sell boats that are more than ten years old and closer to a ten thousand dollar price because the camps can afford that price more easily. You will use the proceeds from the sale of the donated boats to build your inventory of boats and pay your salary. You will seldom grant 100 percent of a boat to a non-profit camp. Your financial data shows that you will make no grants over the course of the next several years. You have not included any grant material with your application.

You will not offer any training to staff members about how to use the boats the camps have purchased. You will not offer formal training to the camps regarding the maintenance of the boats. You state that your formal responsibility with respect to the boat ends once the camp

has purchased it. You further state that the purpose of your organization is not to train the boat drivers.

Your board of directors consists of five members, a majority of whom are members of the same family. The board members are you, your daughter, your son-in-law, and two members of the community. Your compensation arrangements do not follow a conflict of interest policy nor have you adopted one into your by-laws. The chairman of the board sets his own compensation and it is voted on by the board.

### LAW

Section 501(c)(3) of the Code exempts from federal income tax corporations organized and operated exclusively for charitable, educational, and other exempt purposes, provided that no part of its net earnings inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations provides that the term "charitable" is used in section 501(c)(3) of the Code in its general accepted legal sense and includes the relief of the poor and distressed or of the underprivileged.

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) of the Code, 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)(1)(i) of the regulations provides that an organization is organized exclusively for one or more exempt purposes only if its articles of incorporation:

- a. Limit the purposes of such organization to one or more exempt purposes; and
- b. Do not expressly empower the organization to engage, otherwise than as an insubstantial part of its activities, in activities that in themselves are not in furtherance of one or more exempt purposes.

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 that 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 are not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(c)(2) of the regulations provides: "[a]n organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals."

Section 1.501(c)(3)-1(d)(1) of the regulations provides that an organization may be exempt as an organization described in section 501(c)(3) of the Code if it is operated exclusively for one or more of the following purposes: religious, charitable, scientific, testing for public safety, literary, educational, or prevention of cruelty to children or animals.

Section 1.501(c)(3)-1(d)(3) of the regulations provides, [t]he term "educational", as used in section 501(c)(3) of the Code relates to, the instruction or training of the individual for the purposes of improving or developing his capabilities or the instruction of the public on subjects useful to the individual and beneficial to the community.

Section 1.501(c)(3)-1(d)(3) of the regulations provides examples of educational organizations. Example 2 refers to an organization whose activities consist of presenting public discussion groups, forums, panels, lectures, or other similar programs.

Section 1.501(c)(3)-1(e)(1) 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 organization's exempt purpose or purposes and if the organization is not organized or operated for the primary purpose of carrying on an unrelated trade or business.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279 (1945), the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes.

In Rev. Rul. 72-369, 1972-2 C.B. 245, an organization was formed to provide managerial and consulting services for section 501(c)(3) organizations to improve the administration of their charitable programs. The organization enters into agreements with unrelated section 501(c)(3) organizations to furnish managerial and consulting services on a cost basis.

This revenue Ruling stated that:

An organization is not exempt merely because its operations are not conducted for the purpose of producing a profit. To satisfy the "operational test," the organization's resources must be devoted to purposes that qualify as exclusively charitable within the meaning of section 501(c)(3) of the Code and the applicable regulations.

Providing managerial and consulting services on a regular basis for a fee is a trade or business ordinarily carried on for profit. The fact that the services in this case are provided at cost and solely for exempt organizations is not sufficient to characterize this activity as charitable within the meaning of section 501(c)(3) of the Code. Furnishing the services at cost lacks the donative element necessary to establish this activity as charitable.

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), the Tax Court held that an organization did not qualify for exemption under section 501(c)(3) of the Code because it was primarily engaged in an activity that was characteristic of a trade or business and ordinarily carried on by for-profit commercial businesses. The Tax Court stated, "We must agree with the Commissioner that petitioner's activity constitutes the conduct of a consulting business of the sort which is ordinarily carried on by commercial ventures organized for profit..." 70 T.C. at 358.

In Easter House v. U.S., 12 Cl. Ct. 476 (1987), aff'd in an unpub. opinion, 846 F.2d 78 (Fed. Cir. 1988), cert. den., 488 U.S. 907 (1988), the organization, in exchange for a fee, provided adoption services to parents seeking to adopt a child, including services to pregnant women who intended to place their newborns for adoption. These fees were the organization's sole source of income. The Claims Court concluded that the organization's business purpose of operating an adoption service, not the advancement of educational and charitable activities, was its primary goal. It competed with other commercial organizations providing similar services. Thus, "[p]laintiff's competition provides its activities with a commercial hue." 12 Cl. Ct. at 486. Accordingly, the organization did not qualify for exemption under section 501(c)(3) of the Code.

In Airlie Foundation v. I.R.S., 283 F.Supp. 2d 58 (D.D.C. 2003), the District Court found that the organization was formed principally to organize, host, conduct, and sponsor educational and other charitable functions on its facilities. The organization's patrons were not limited to tax-exempt entities, but included patrons of a private and corporate nature. The organization paid advertising and promotional expenses and derived substantial income from weddings and special events held at its conference center. The court determined that the organization's activities competed with a number of commercial, as well as non-commercial entities, which strongly evidenced a commercial nature and purpose. The court concluded that although the organization carried out a number of charitable and educational activities, these were incidental to its primary activity of operating a for-profit conference center. The court stated, "While plaintiff's organizational purpose is exempt and the foundation operates, in important respects, in an exempt fashion, there is a distinctive "commercial hue" to the way Airlie carries out its business. 283 F.Supp.2d at 65.

### RATIONALE

Your organizational documents fail to limit your purposes to one or more exempt purposes as required by section 501(c)(3) of the Code. See Section 1-501(c)(3)-1(b)(1)(i) of the regulations. Soliciting boat donations, then procuring and fixing those boats, and then selling them to a non-profit camp does not further one of the exempt purposes included by section 501(c)(3) of the Code. Furthermore, your organizational documents empower your organization to engage in the activity of selling boats, which is not an activity that furthers any of the exempt purposes described in section 1.501(c)(3)-1(d)(1) of the regulations. See section 1.501(c)(3)-1(b)(1)(i).

By selling these boats to camps at a discounted price after they have been donated to you, you are engaged in a commercial activity. You will receive donated boats at no cost. You will fix up the boats and sell them to camps. All of these activities constitute common commercial activities, rather than activities that further an exempt purpose. See B.S.W. Group, Inc. v Commissioner, supra; Easter House v. U.S., supra; and Airlie Foundation v. I.R.S., supra.

Selling boats to non-profit camps is similar to providing adoption services for a fee and managerial services for a fee, in the sense that they are all commercial activities usually carried on by for-profit businesses. See Easter House v. U.S., supra; Rev. Rul. 72-369, supra. You will compete with other commercial boat dealers for the camps' business and; therefore, there is a

distinctive "commercial hue" to the way you propose to carry out your business. See Airlie Foundation v. I.R.S., supra

The fact that you are performing your services exclusively for section 501(c)(3) camps is insufficient to render your activities charitable. See Rev. Rul. 72-369, supra. By procuring, fixing, servicing, and then selling the boats to the camps after they have been donated to you at no cost, you lack the donative intent element necessary to establish this activity as charitable. See Rev. Rul. 72-369, supra.

Additionally, you will not provide any formal training to the camps to maintain the boats. Furthermore, you state your purpose is not to train the camps to operate the boats. Once you have sold the boat to a camp, your responsibility with respect to that boat ends. Therefore, you lack an educational purpose required by section 501(c)(3) of the Code because you do not provide any formal training designed to increase the capabilities of the individuals that purchase the boats. See Section 1.501(c)(3)-1(d)(3) of the regulations.

The composition of your board of directors, taken with the fact that you have not adopted a conflicts of interest policy, indicates that the board will be voting on their own compensation. You will also use the proceeds from the sale of boats to camps to increase your inventory of used boats to sell, bolstering your commercial activity. You do not use the proceeds to further any exempt purpose. Thus, absent a conflicts of interest policy, the fact that a majority of your board of directors are members of the same family may result in prohibited inurement under section 1.501(c)(3)-1(c)(2) of the regulations.

Lastly, since all of your activities constitute the operation of a commercial activity, you are organized and operated for the primary purpose of carrying on a commercial business rather than a charitable activity. As a result, under section 1.501(c)(3)-1(e)(1) of the regulations, you do not meet the requirement of section 501(c)(3) of the Code. You do not operate exclusively for charitable purposes, as required by section 501(c)(3).

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(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 a 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 Practice 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 administrative remedies. Section 7428(b)(2) of the

Code provides, in part, that a declaratory judgment or decree 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 of it will be forwarded to the Ohio Tax Exempt and Governmental 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 (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).

In the event this ruling becomes final, it will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, Notice of Intent to Disclose. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, and do not intend to protest our denial of exempt status, you should follow the instructions in Notice 437.

If you decide to protest this ruling, your protest statement should be sent to the address shown below. If you also disagree with our proposed deletions, you should send your comments on the deletions with your protest statement, and not to the address shown in Notice 437.

Internal Revenue Service

1111 Constitution Ave.  
Washington, D.C. 20224

If you do not intend to protest this ruling, and if you agree with our proposed deletions as shown in the letter attached to Notice 437, you do not need to take further action.

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

Sincerely,

Lois G. Lerner  
Director, Exempt Organizations  
Rulings and Agreements