



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Number: **200914063**
Release Date: 4/3/2009

Date: January 6, 2009

UL: 501.03-00

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Dear :

This is our final determination that you do not qualify for exemption from Federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

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 and 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. Failure to file the returns timely may result in a penalty.

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, 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 & Agreements

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



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: June 25, 2008

UL: 501.03-00

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Applicant =

A =

B =

C =

Q =

R =

S =

T =

Year 1 =

Year 2 =

Year 3 =

Charity 1 =

Charity 2 =

Charity 3 =

X =

X1 =

X2 =

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

The Applicant indicated that its major purpose includes, but are not limited to: 1) building community awareness of important issues impacting the lives of families and children in the U.S., including safety, health and other community issues, particularly by mobilizing the auto dealership community resources and contacts, but also raising funds from the public at large; and, 2) directly educating the public as to health and safety issues, as well as to providing

funding for other charitable organizations with similar purposes and goals. Your mission statement indicated that you will join together the resources and influences of community minded dealers to improve safety and well being of your communities through innovative programs.

The Applicant indicated that its President, Q, and its Vice President, R, are also the President and the Vice President of A, a for-profit entity. Q and R are also husband and wife. A is a service coupon mailer company aimed at promoting customer traffic for local auto dealerships. A earned several X dollars in advertising revenue for the calendar years ending Year 1, Year 2, and Year 3. Q owns 100% of the stock in A, a S-corporation. The Applicant's five Board Members are also officers and/or Board Members of A. The Applicant further indicated that S and I are its secretary and treasurer, respectively, and that A also employs S and I and pays them annual salary with profit sharing. A's compensation for officers and/or employees for calendar years ending Year 2 and Year 3 totaled X1 and X2, respectively.

The Applicant's President, Q, and its Vice President, R, serve approximately 20 and 10 hours a week, respectively. S serves approximately 10 hours per week and is the Secretary of the Applicant. S is the creative mind, designing promotion give-aways and strengthening relationships between the Applicant and other non-profits participants. S creates much of the promotions material used to build awareness for the applicant's initiatives. I serves approximately 5 hours per week and is the Treasurer for the Applicant. I assists as the communication person as well as a financial adviser. I also serves as the communication secretary as well because of his knowledge of electronic communications.

The Applicant's response to Part V 7a of Form 1023 indicates that the Applicant may purchase services from S and I whom, as indicated above, are also officers of the Applicant. However, the Applicant indicated that so far, S and I have donated their services. The Board will set any compensation or price for any services or transactions with any board member or officer or related entity. The Board Member affected by a particular compensation issue will not be involved in that particular decision. The Applicant indicated that they would conduct research concerning the proper compensation for S's and I's time and services.

The Applicant also indicated that A transferred funds to the Applicant for assistance in covering invoices and bank charges. Neither Applicant nor A provided any documentation characterizing the transfer of funds, and neither has disclosed if this is a loan, partial loan and a partial gift, or an outright gift. The Applicant stated that A received a partial payment, for what may be a loan, with the balance to be paid when the Applicant is able, assuming financially able.

The Applicant represented that they will not enter into any advertising contracts with auto dealerships. The sample advertisement materials submitted with the application, according to Applicant, were prepared by A. The Applicant indicated that they are not preparing material for the auto dealerships but are placing the educational material on the already ordered auto dealership's advertisements, i.e. piggy-backing. The Applicant states that by this method they can persuade business they know, presumably through A, to fund the dissemination of these materials and save the cost of preparing and mailing separate flyers. The Applicant's representative asserted that the Applicant would piggy-back its safety awareness material onto

an auto dealership's routine business advertisements. The safety awareness material is not made available directly to the public at large but aimed at auto dealership's customer. The auto dealerships serves as dissemination point for the education material and have agreed to the piggy-backing arrangement. The Applicant stated that the auto dealerships do not anticipate additional business from this arrangement; "nobody is going to go to an auto dealership for service to get something with basically no monetary value."

The Applicant proposes to engage artists to create artwork for its children activity and coloring booklets and then sell and distribute these booklets to auto dealerships for a nominal fee. The activity and coloring booklets will carry the safety awareness material, featuring characters, and can be used to occupy the customer's children while customers are waiting for auto service repairs. The characters are creatures used in swimming safety awareness programs. The activity and coloring booklets are sold to the dealers at a price that covers the expenses that the Applicant incurs. The auto dealers then distribute the activity and coloring booklets to their customer base or potential customers.

The Applicant anticipates that the proceeds from distributions of the booklets will cover the cost of the materials. If there are any excess proceeds they will be donated to the Applicant's partner charities. The Applicant indicated that currently, all funds were expended in printing and preparing and distributing the public relations pieces, namely a musical CD and a coloring book. The Applicant is in the process of copywriting the activity booklet. B owns the rights to the musical CD. The rights to the characters are owned by C. The characters are also used by Charity 1 in promoting its message and activities. The Applicant received permission to use these characters and to distribute a musical CD. The Applicant does not have any business relationship with B and C other than receiving rights to use their intellectual property.

The Applicant submitted sample advertising mailers whereby the Applicant's logo and A's logo were prominently displayed within close proximity of each other, which suggests that there is an apparent business relationship between the Applicant and A. The Applicant places its logo onto advertising mailers prepared by A for distributions by the auto dealerships. The Applicant also places characters from Charity 1 onto materials prepared by A to further its presumed charitable purpose. The Applicant's musical CD and coloring book featuring safety information is made available at the auto dealerships. The Applicant encourages auto dealers to promote safety awareness campaigns for non-profit agencies to build good will in their communities. The Applicant represented a close working relationship with Charity 1 and Charity 2, both exempt organizations, with no commonality of ownership or control. The Applicant also works with the Charity 3 on a campaign where information is available on a website.

On one example of the A created advertising mailer for an auto dealership was submitted with the application. The front page of a four page 8½ x 11 inch mailer featured a swimming pool like background with the Charity 1's characters, along with an offer for a free Musical CD, activity booklet, an announcement to register for a free trip to an amusement park, and a chance to win free services. The inside of the material opens up to a 17 x 22 inch layout with essentially the same background layout as on the front with the Charity 1's characters features in the outer edges. However, on the inside of the material there is an overwhelming amount of space devoted to auto service specials. On the last page of the advertising material, ½ of the

space is devoted to service specials and the other ½ to consumer safety statistics. There is no mentioning of any charitable purpose or activity neither inside nor outside the advertising material.

The Applicant indicated that A permits access to its customers for solicitation purposes and A receives no benefit from this. The brochures enclosed with the application features prominently services available from different dealers. These materials do not mention any charity services available to the community but only service announcement for safety.

LAW

IRC 501(c)(3) provides exemption from federal income tax for organizations that are "organized and operated exclusively" for religious, educational, or charitable purposes. The exemption is further conditioned on the organization being one "no part of the net income of which inures to the benefit of any private shareholder or individual."

Regs. 1.501(a)-1(c) states that "[t]he words 'private shareholder or individual' in section 501 refer to persons having a personal and private interest in the activities of the organization."

Reg. 1.501(c)(3)-1(c)(1). 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). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Reg. 1.501(c)(3)-1(c)(2) An 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.

Reg. 1.501(c)(3)-1(d)(1)(ii) An organization is not organized or operated exclusively for one or more of the purposes specified in subdivision (i) of this subparagraph unless it serves a public rather than a private interest. 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.

Rev. Rul. 76-206, 1976-1 C.B. 154, considered an organization formed to promote broadcasting of classical music in a particular community. The organization carried on a variety of activities designed to stimulate public interest in the classical music programs of a for-profit radio station, and thereby enable the station to continue broadcasting such music. The activities included soliciting sponsors, soliciting subscriptions to the station's program guide, and distributing pamphlets and bumper stickers encouraging people to listen to the station. The organization's board of directors represented the community at large and did not include any representatives of the for-profit radio station. The revenue ruling concludes that the organization's activities enable the radio station to increase its total revenues and therefore benefit the for-profit radio station in more than an incidental way. Therefore, the organization is serving a private rather than a public interest and does not qualify for exemption.

Rev. Rul. 98-15, 1998-1 C.B. 718, 1998 WL 89783 (1998) ("If a private party is allowed to control or use the non-profit organization's activities or assets for the benefit of the private party, and the benefit is not incidental to the accomplishment of exempt purposes, the organization will fail to be organized and operated exclusively for exempt purposes.

St. David's Health Care System v. U.S., 349 F.3d 232, that court held "In order to ascertain whether an organization furthers non-charitable interests, we can examine the structure and management of the organization; in other words, we look to which individuals or entities controlling the organization.

Lowry Hosp. Ass'n v. Commissioner, 66 T.C. 850, 859-60, 1976 WL 3664 (1976) (concluding that a hospital could not be deemed to operate exclusively for charitable purposes, partly because of the "control and dominance" exercised by a single physician over the hospital's affairs). If private individuals or for-profit entities have either formal or effective control, we presume that the organization furthers the profit-seeking motivations of those private individuals or entities.

Redlands Surgical Servs. v. Commissioner, 113 T.C. 47, 75, 1999 WL 513862 (1999) ("An organization's property may be impermissibly devoted to a private use where private interests have control, directly or indirectly, over its assets, and thereby secure non-incidental private benefits.") When the non-profit organization cedes control over the partnership to the for-profit entity, we assume that the partnership's activities substantially further the for-profit's interests. As a result, we conclude that the non-profit's activities via the partnership are not exclusively or primarily in furtherance of its charitable purposes. Thus, the non-profit is not entitled to a tax exemption.

Church of Ethereal Joy, 83 T.C. at 23 Although control by ... a small group may not necessarily disqualify [an organization] for exemption, it provides an obvious opportunity for abuse of the claimed tax-exempt status.

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. . If an organization is closely controlled, either by a board of directors comprised of related persons or a for-profit management company that operates with a great amount of autonomy, the application file must clearly show the organization meets the requirements of Reg. 1.501(c)(3)-1(d)(1)(ii) that it has established that it is not or will not be organized or operated for the benefit of private interests.

American Institute for Economic Research v. United States, 302 F.2d 934 (Ct. Cl. 1962), cert. denied, 372 U.S. 976 (1963), described an organization that had a stated aim of teaching and disseminating economic knowledge, published two semi-monthly periodicals available for subscription, and provided investment advice services for a fee. The court held that this organization did not qualify for exemption under section 501(c)(3) of the Code, because its commercial purpose was primary and not incidental to its educational purpose.

Bubbling Well Church of Universal Love, Inc. v. Commissioner, 74 T.C. 531 (1980) aff'd, 670 F.2d 104 (9th Cir. 1980), the Tax Court considered the qualification for exemption of an organization purporting to be a church. The Applicant was controlled by three family members. The court stated that, "While this domination of petitioner by the three Harberts, alone may not necessarily disqualify it for exemption, it provides an obvious opportunity for abuse of the claimed tax-exempt status. It calls for open and candid disclosure of all facts bearing upon petitioner's organization, operations, and finances so that the Court, should it uphold the claimed exemption, can be assured that it is not sanctioning an abuse of the revenue laws. If such disclosure is not made, the logical inference is that the facts, if disclosed, would show that petitioner fails to meet the requirements of section 501(c)(3). Thus, close control of an Applicant, because of the potential for abuse, requires a clear demonstration that private interests will not be served."

American Campaign Academy v. Commissioner, 92 TC 1053 (1989), "nonincidental benefits conferred on disinterested persons that serve private interests." Genuine public benefit often provides an incidental benefit to private individuals. But if private interests are served *other than incidentally*, exemption is precluded. *Qualitatively* incidental means that the private benefit is a mere byproduct of the public benefit. For private benefit to be *quantitatively* incidental, it must be insubstantial in amount. The private benefit must be compared to the public benefit of the specific activity in question, not the public benefit provided by all the organization's activities. The more exactly you can quantify the private benefit, the more likely it is to be non-incidental.

RATIONALE

The Applicant and A share the same president and vice president of their respective organizations, whom are also husband and wife. The five persons serving on the Applicant's Board also serve as officers and Board Members of A. A is a for profit entity while the Applicant is an entity applying for 501(c)(3) status. A is a marketing firm created to increase customer traffic to its advertisers, auto dealerships in particular. The Applicant in partnership with A, while simultaneously increasing customer traffic also strives to increase community safety awareness in the surrounding areas through the advertising material. But these advertisement mailers initially are not directed at the general public but at the auto dealers' customers and potential customers who might use the services of the dealers. Thus, the main focus of the advertising material is to increase customer traffic, and only secondarily to disseminate downstream the safety concerns.

In addition, the management between the two entities is indistinguishable. The Applicant described an inter-company transfer of funds from A to cover the Applicant's vendor invoices and bank charges. A received a partial payment from the Applicant with the balance to be paid when Applicant is able. The Applicant did not describe this matter as an arm-length transaction. The interrelated management determines and controls the resources and assets of both the Applicant and the for profit entity as if they were the same. This control clouds the issue of whether the Applicant is truly independent of A and increases the opportunity for abuse of the Applicant's exempt status. See Lowry Hosp. Ass'n v. Commissioner (If private individuals or for-profit entities have either formal or effective control, we presume that the organization furthers the profit-seeking motivations of those private individuals or entities); also see Church

of Ethereal Joy, 83 T.C. at 23. Although control by ... a small group may not necessarily disqualify [an organization] for exemption, it provides an obvious opportunity for abuse of the claimed tax-exempt status.

It is presumed that if private individuals or for-profit entities have either formal or effective control, that the organization furthers the profit-seeking motivations of those private individuals or entities. That is true, even when the organization is a partnership between a non-profit and a for-profit entity. See *Redlands Surgical Servs. v. Commissioner*, 113 T.C. 47, 75, 1999 WL 513862 (1999) ("An organization's property may be impermissibly devoted to a private use where private interests have control, directly or indirectly, over its assets, and thereby secure nonincidental private benefits."). As a result, the non-profit's activities via the partnership are not exclusively or primarily in furtherance of its charitable purposes. Thus, the non-profit is not entitled to a tax exemption. See Rev. Rul. 98-15, 1998-1 C.B. 718, 1998 WL 89783 (1998).

Private benefit does not necessarily involve the flow of funds from an exempt organization to a private party. *Rev. Rul. 76-206*, 1976-1 C.B. 154, considered an organization formed to promote broadcasting of classical music in a particular community. The organization carried on a variety of activities designed to stimulate public interest in the classical music programs of a for-profit radio station, and thereby enable the station to continue broadcasting such music. The activities included soliciting sponsors, soliciting subscriptions to the station's program guide, and distributing pamphlets and bumper stickers encouraging people to listen to the station. The organization's board of directors represented the community at large and did not include any representatives of the for-profit radio station. The revenue ruling concludes that the organization's activities enable the radio station to increase its total revenues and therefore benefit the for-profit radio station in more than an incidental way. Therefore, the organization is serving a private rather than a public interest and does not qualify for exemption.

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. The Court found that a trade association had an "underlying commercial motive" that distinguished its educational program from that carried out by a university, and therefore, the association did not qualify for exemption.

Similar to the holding in *Better Business Bureau*, the benefits of the Applicant are substantially private in nature and favor the advertisers and the advertisers' customers and not the public at large. Two quotes in the brochure generated by joint efforts of the Applicant and A substantiates this claim that the safety concerns are but incidental to the profit motives of the auto dealerships. First, "Ask yourself: 'Is there anything wrong with doing something that benefits the community and brings my auto dealership increased profits by strengthening my relationship with my customers. Second, 'While it is true that not all you customers have children, it is safe to say they recognize the value of your auto dealership promoting children issues. The organization's activities focus more on promoting individual auto dealerships than children safety issues. Further, it should be remembered that the auto dealership are customers of A. By helping to promote the business of the auto dealerships, A is also promoting its own business interests.

The Applicant indicated that it may purchases services from S and T whom are also officers of the Applicant. The Applicant indicated that after research in the market price they would pay a fair value for S's and T's time and services. As previously stated, Reg. 1.501(c)(3)-1(c)(2) clarifies that an organization is not operated exclusively for exempt purposes if its net earnings inure to the benefit of private individuals. Where an exempt organization engages in a transaction with an insider and there is a purpose to benefit the insider(s) rather than the organization, inurement occurs even though the transaction ultimately proves profitable for the exempt organization.

It appears the Applicant is carrying on the same business as A, except that the Applicant also promotes safety awareness. The Applicant's primary vehicle for carrying its message for safety issues is to "piggy-back" onto the advertising materials placed by area auto dealers to increase its customer base. Advertising and marketing are an activities carried on by for-profit entities not organized for a public charity or for other exempt purposes. The principles set forth in Rev. Rul. 76-206, applies in this instant application, benefit to a private interest in more than an incidental way precludes exemption. In conclusion, you fail to qualify for exemption because the facts show that you are serving more of a private rather than a public interest not exclusively or primarily in furtherance of a charitable purpose.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination.

Your protest statement should be accompanied by the following declaration:

Under penalties of perjury, I declare that I have examined this protest statement, including accompanying documents, and, to the best of my knowledge and belief, the statement contains all the relevant facts, and such facts are true, correct, and complete.

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to protest as a failure to exhaust available administrative remedies. Code section 7428(b)(2) 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 all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to this address:

Internal Revenue Service
TE/GE SE: T: EO: RA: T: 3
Exempt Organizations Technical Group 3

1111 Constitution Avenue, NW:
Washington DC 20224

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

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

Sincerely,

Robert Choi
Director, Exempt Organizations
Rulings & Agreements