



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Release Number: **201016088**
Release Date: 4/23/10

Date: January 29, 2010

UIL: 501.03-05, 501.05-01, 501.33-00, 504.50-00

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

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.

Since 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.

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.

Letter 4038 (CG) (11-2005)
Catalog Number 47632S

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,

Rob Choi
Director, Exempt Organizations
Rulings & Agreements

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



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INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Date: January 29, 2010

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend:

M =

B =

C =

D =

E =

F =

G =

H =

x =

y =

z =

UIL Nos:

501.03-05

501.05-01

501.33-00

504.50-00

Dear _____ :

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.

ISSUE

Whether you, M, qualify for exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code of 1986.

FACTS

The Form 1023, Application requesting Recognition of Exemption under Section 501(c)(3) of the Internal Revenue Code, requesting private foundation status, was filed on w. M incorporated on x in y and operates in z. The registered agent listed on the Articles of Incorporation is G. M's three

officers are B, C, and D and are all family. E is an additional employee of M who is related to B, C, and D. B owns E, a for-profit business in z. B, C, and D are officers of E.

H approached the owner of E and proposed E to pursue grants. E paid H for research, letters writing, and requests for proposal for E. Later H advised E to apply for non-profit because most grants are awarded to non-profit organizations. At H's suggestion E proceeded with filing as a non-profit entity to create M.

M stated, how B plans to expand its operations, by purchasing property joining E's existing ranch, and improve conditions through the following processes.

- Raising commercial cattle for the beef industry
- Rangeland management for cattle and wildlife
- Proper techniques in raising and harvesting mature whitetail deer
- Wildlife protection
- Land and water conservation

B stated the benefits of expanding its property are large and will improve the quality of life for many.

There are several different processes that H will be performing that are crucial in attaining any grants for B, & E. All information regarding the grant process including funding is kept strictly confidential. M stated the following will be provided with all the necessary steps.

1st Step – Research

Matching individuals with for-profit business and non-profit 501(c)(3) organizations or private foundations that are dispersing funds for your type of project and current location.

2nd Step – Letter Writing Letter of Intent (L.O.I.)

H will draft a L.O.I. on behalf of E & B for the foundations they match. The purpose of H's letters is to explain situations and what will be done with any grant money received.

3rd Step – Request for Proposal (R.F.P.)

Should any foundation or organization request a formal grant application (grant), H will send a R.F.P. E & B will be assigned to a grant writer who will write the actual grant to be received for the foundation or organization.

Finally, H stated if a foundation or other section 501(c)(3) organization is willing to fund M's project, the grant money will be dispersed to E or M.

M intends to buy property that is currently owned by private individuals. M plans to purchase the property in about 2 years. The agreement to buy the land in the future is verbal between B's family and owners of the property. M intend to build a building on the property and rent it out to help pay for the building.

M intends to raise commercial cattle for the beef industry. M stated the land purchased is now owned by a neighbor who is retiring, and who has raised commercial cattle for generations. B's family has been in this area since _____ and B and C have the expertise and experience to be able to use the land to continue raising healthy cattle, and to be sold to the beef industry.

M intends to conduct rangeland management for cattle and wildlife. M stated they plan to develop programs to increase the health of the livestock that is present on the land, and to raise the quality of the animals. M will work with the scientific community to provide data and research on M's programs, resulting in an economic benefit to the beef industry.

M intends to implement proper techniques in raising and harvesting mature whitetail deer. M stated that using the experience that has been in B's family for generations, M will develop programs that will raise the quality of life for the deer.

When asked about the commercial operation M stated because of the expertise and experience of M's officers in F, M believes that it can run the new company and develop the programs M has outlined for the benefit of economic growth for the local community in providing jobs and training; educational research and development for animals and wildlife habitats for the advancement of education and science; and providing a charitable organization to foster these programs. B stated that combined as a family and group of business people, B's family has the skills to run the new operations, and believe that they can do so with the dedication and focus required.

M indicated they will conducted wildlife protection as well as land and water conservation on the property that they plan to purchase.

M stated B will determine the compensation for each position along with officers and directors.

M stated that wages and salaries will not be set at this time. Once land is purchased, wages will be set. The administration and management will be mostly family except for laborers in the field who will be working along side family members.

M stated that the education section of the program will emphasize the importance toward establishing proper homemaking values through farming, ranching, and range management for both cattle and wildlife.

M stated that sections of the program will consist of donations towards county livestock shows.

M stated that the laborers will be the backbone of the program as it takes a lot of work to see a program like this work. Laborers will work alongside family members making sure the ranch is running to its full potential. Such activities will include driving tractors, dozers, building roads, right a ways, planning for both cattle and wildlife, observing cattle and wildlife year round for difficulties, and all other activities it takes to run a successful ranch.

LAW

Section 501(c)(3) of the Internal Revenue Code provides for the exemption from Federal income tax of corporations organized and operated exclusively for charitable, educational, and other purposes, provided that no part of the net earnings inure to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(a)(1) of the Income Tax 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(c)(1) of the Income Tax 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). 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(c)(2) of the Income Tax Regulations provides that 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. Section 1.501(a)-1(c) defines the words "private shareholder or individual" in section 501 to refer to persons having a personal and private interest in the activities of the organization.

Section 1.501(c)(3)-1(d)(1)(ii) of the Income Tax Regulations assigns the burden of proof to an applicant organization to show that it serves a public rather than a private interest and specifically 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(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 generally accepted legal sense and includes the relief of the poor and distressed or of the under privileged as well as the advancement of education.

Section 1.501(c)(3)-1(d)(3) of the Income Tax Regulations provides that the term "educational" refers to:

- (a) The instruction or training of the individual for the purpose of improving or developing his capabilities; or
- (b) The instruction of the public on subjects useful to the individual and beneficial to the community.

Section 1.501(c)(3)-1(e)(1) of the Income Tax Regulations provides that an organization may meet the requirements of section 501(c)(3) 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 Easter House v. U.S., 12 Cl. Ct. 476 (1987), aff'd 846 F. 2d 78 (Fed. Cir 1988), the court found that adoption services were the primary activity of the organization. In deciding that the organization conducted adoption services for a business purpose rather than for a charitable purpose, the court considered the manner in which the organization operated. The record established a number of factors that characterize a commercial activity and which were evident in the operations of Easter House also. The court determined that the organization competed with other commercial organizations providing similar services; fees were the only source of revenue; it accumulated very substantial profits, because it set its fees in order to generate a profit; it accumulated capital that was substantially greater than the amounts spent on charitable and educational activity; and the organization did not solicit and did not plan to solicit contributions. The court also found a corporate-type structure in the classes of memberships (including a single life member having inherent power that the holder could transfer like stock), and dependence on paid employees.

In American Institute for Economic Research v. United States, 302 F. 2d 934 (Ct. Cl. 1962), the Court considered an organization that provided analyses of securities and industries and of the economic climate in general. It sold subscriptions to various periodicals and services providing advice for purchases of individual securities. The court noted that education is a broad concept, and assumed *arguendo* that the organization had an educational purpose. However, the totality of the organization's activities, which included the sale of many publications as well as the sale of advice for a fee to individuals, was indicative of a business. Therefore, the court held that the organization had a significant non-exempt commercial purpose that was not incidental to the educational purpose, and was not entitled to be regarded as exempt.

In KJ's Fund Raisers, Inc. v. Commissioner, T.C. Memo 1997-424 (1997), affirmed 82 AFTR 2d 7092 (1998), the Tax Court found that another gaming organization was not exempt. While the organization raised money for charitable purposes, it also operated for the substantial benefit of private interests. The organization's founders were the sole owners of a bar, KJ's Place. The organization, through the owners and employees of KJ's Place, sold lottery tickets exclusively at KJ's Place during regular business hours. While in KJ's Place, the lottery ticket purchasers were sold beverages. The initial directors were the two founders and a related individual. The initial board was replaced several times until the two founders were no longer on the board. At all times these two individuals were the organization's officers. Salaries had been paid to them and rent had been paid to KJ's Place. The organization maintained that the fact that salaries and rent were no longer paid in this fashion indicated the independence of the board. The Court took another view: "Although those practices ceased and are not in issue here, the current board of directors is composed of at least the majority of the same members who allowed those amounts to be paid."

In Church by Mail, Inc. v. Commissioner, (1985) the Court affirmed a Tax Court decision. Church by Mail sent out sermons in numerous mailings. This required a great deal of printing services. A for-profit company, controlled by the same ministers, provided the printing and the mailing. This company also employed family members. The services were provided under two contracts. The contracts were signed by the two ministers for both the organization and the for-profit company. The organization's business comprised two-thirds of the overall business done by the for-profit

company. The court determined that there was ample evidence in the record to support the finding that the organization was operated for the substantial non-exempt purpose of providing a market for the services of the for-profit company. The employees of the company spend two-thirds of their time working on the services provided to the church. The majority of the Church's income is paid to the for-profit company to cover repayments on loan principal, interest, and commissions. Finally, the potential for abuse created by the ministers' control of the Church requires open and candid disclosure of facts bearing upon the exemption application. Moreover, the ministers' dual control of both the Church and the for-profit company enables them to profit from the affiliation of the two entities through increased compensation.

New Dynamics Foundation v. United States, 70 Fed.Cl. 782 (2006), was an action for declaratory judgment that the petitioner brought to challenge the denial of its application for exempt status. The court found that the administrative record supported the Service's denial on the basis that the organization operated for the private benefit of its founder, who had a history of promoting dubious schemes. The organization's petition claimed that the founder had resigned and it had changed. However, there was little evidence of change other than replacement of the founder with an acquaintance who had no apparent qualifications. The court resolved these questions against the petitioner, who had the burden of establishing it was qualified for exemption. If the petitioner had evidence that contradicted these findings, it should have submitted it as part of the administrative process. "It is well-accepted that, in initial qualification cases such as this, gaps in the administrative record are resolved against the applicant".

In National Association of American Churches v. Commissioner, 82 T.C. 18 (1984), the court denied a petition for declaratory judgment that the organization qualified for exempt status as a church. In addition to evidence of a pattern of tax-avoidance in its operations, the court noted that the organization had failed to respond completely and candidly to IRS during administrative processing of its application for exemption. An organization may not declare what information or questions are relevant in a determination process. It cited a number of declaratory relief actions that upheld adverse rulings by the Service because of the failure of the applicants to provide full and complete information on which the Service could make an informed decision.

In Rev. Rul. 61-170, 1961-1 C.B. 112, an association composed of professional private duty nurses and practical nurses that supported and operated a nurses' registry primarily to afford greater opportunities for its members was not entitled to exemption under section 501(c)(3) of the Code. Although the public received some benefit from the organization's activities, the primary benefit of these activities was to the organization's members.

Application of Law:

The requirement for organizations desiring to be recognized as exempt from federal income tax under section 501(c)(3) is to be operated exclusively for charitable, educational, and other purposes. Section 1.501(c)(3)-1(a)(1) of the regulations, *supra.*, must be both organized and operated exclusively for one or more of the purposes. M's services are raising commercial cattle for the beef industry, rangeland management for cattle and wildlife, raising and harvesting mature whitetail deer, and running a ranch. Therefore, M's activities are not that of operating exclusively for an exempt purpose but that of a commercial operation.

Section 1.501(c)(3)-1(d)(1)(ii) of the Income Tax Regulations states that an organization is not organized exclusively for any of the purposes specified in section 501(c)(3) of the Code unless it serves public, rather than private interests. For purposes of section 501(c)(3) of the Code, the term "private interests" has a specific meaning. Private interests include: the creator of an organization or members of his family, shareholders of an organization, or persons controlled, directly or indirectly, by such private interests. B, C, & D are all family and officers of M.

M operates for substantial non-exempt commercial purposes in contravention of section 501(c)(3). (See, Better Business Bureau of Washington D.C., Inc. v. United States, 326 U.S. 279 (1945), and American Institute for Economic Research v. United States, 302 F. 2d 934 (Ct. Cl. 1962), in which 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.) M's activities will be devoted mostly to raising commercial cattle for the beef industry, rangeland management for cattle and wildlife, raising and harvesting mature whitetail deer, and running a ranch. Therefore, the activities are those of a commercial operation and when asked how the activities are different from those of a commercial operation, M stated "not Much".

To be exempt under Section 501(c)(3), an organization must be both organized and operated for one or more exempt purposes specified in the Section. Although "exclusively" does not mean "solely" or "without exception," the presence of a single nonexempt purpose, if substantial, will preclude exemption regardless of the number or importance of exempt purposes, as stated in Better Business Bureau, Easter House, and Rev. Rul. 61-170, 1961-1 C.B. 112 supra. 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 purposes specified in Section 501(c)(3). Neither is an organization operated exclusively for one or more exempt purposes if its net earnings inure to the benefit of private shareholders or individuals, or its activities further private rather than public interests. Therefore, since B and B's family are the board and there are no other board members to M, B and B's family hold complete control. In addition, M stated that B's family members will be compensated; however, only after M receives the grants that H has promised. Then compensation will be determined by B. As stated B and B's family exercise complete control.

Based on the above, M failed to establish that they are not operating in a manner that would confer substantial benefits, and that M is not serving private interests in a manner precluded by section 1.501(c)(3)-1(d)(1)(ii) of the regulations.

Therefore, M failed to establish that they will be operated exclusively for charitable purposes and not of a private interest. Like the organizations in International KJ's Fund Raisers, Inc. v. Commissioner, supra, and Church by Mail, supra, M is controlled by B who along with C, D, and E will receive substantial benefit. M did not provide any evidence for reasonable due diligence of M's board regarding the decisions related to salaries.

Secondly, as stated in New Dynamics, supra, exemption from Federal income taxation is not a right; it is a matter of legislative grace that is strictly construed. M bears the burden of establishing that it qualifies for exempt status. M must prove that it is organized and operated exclusively for exempt purposes and not for the private benefit of its creators, designated individuals or organizations controlled by such private interests, as in Section 1.501(c)(3)-1(d)(1)(ii) of the Regulations. Again, exclusively does not mean "solely," but no more than an insubstantial part of

M's activities may further a non-exempt purpose.

An applicant for exempt status must provide sufficient information for the IRS to make an informed decision as indicated in National Association of American Churches, supra. It must respond to questions completely and candidly. When asked twice about M's activities being different from a commercial operation, M stated first "Not Much", the second request M stayed silent.

Applicant's Position:

M stated that the programs wanting to pursue did fall into the charitable, educational, and prevention of cruelty to animals sections of the IRS regulations.

Service response to Applicant's Position:

As the regulations indicate, raising commercial cattle for the beef industry, rangeland management for cattle and wildlife and proper techniques in raising and harvesting mature whitetail deer are not activities that qualify under charitable, educational and prevention of cruelty to animals as described in section IRC 501(c)(3). M's activities are those of a commercial operation and not as described under Treas. Reg. section 1.501(c)(3)-1(a)(1). Any wildlife protection, land and water conservation or educational activities that M may have are insignificant to the overall activities and that the commercial aspects of the operation are M's primary functions.

Conclusion:

In summary, M does not meet the requirements under section 501(c)(3) because M fails the operational test. Because M's primary purpose is raising commercial cattle for the beef industry, rangeland management for cattle and wildlife, raising and harvesting mature whitetail deer, and running a ranch, we find that M operates for non-exempt commercial purposes. In addition, we have determined that M has failed to establish activities further a tax-exempt purpose within the meaning of section 501(c)(3). Accordingly, M does not qualify for exemption as an organization described in section 501(c)(3) of the Code.

Consideration was given to whether the application organization qualifies for exemption under other subsections of section 501(c) of the Code. However, based on the information that you have submitted, we cannot find that you are entitled to exempt status under section 501(c) of the Code because you are operated for a significant non-exempt commercial purpose, rather than exclusively for exempt purposes.

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. If your statement does not provide a basis to reconsider our determination, we will forward your case to our Appeals Office. You can find more information about the role of the Appeals Office in Publication 892; *Exempt Organization Appeal Procedures for Unagreed Issues*.

Types of information that should be included in your appeal can be found on page 2 of Publication 892, under the heading "Regional Office Appeal". These items include:

1. The organization's name, address, and employer identification number;
2. A statement that the organization wants to appeal the determination;
3. The date and symbols on the determination letter;
4. A statement of facts supporting the organization's position in any contested factual issue;
5. A statement outlining the law or other authority the organization is relying on; and
6. A statement as to whether a hearing is desired.

The statement of facts (item 4) must be declared true under penalties of perjury. This may be done by adding to the appeal the following signed declaration:

"Under penalties of perjury, I declare that I have examined the statement of facts presented in this appeal and in any accompanying schedules and statements and, to the best of my knowledge and belief, they are true, correct, and complete."

Your appeal will be considered incomplete without this statement.

If an organization's representative submits the appeal, a substitute declaration must be included stating that the representative prepared the appeal and accompanying documents; and whether the representative knows personally that the statements of facts contained in the appeal and accompanying documents are true and correct.

An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you during the appeal process. If you want representation during the appeal process, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. You can find more information about representation in 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 appeal 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 the applicable address:

Mail to:

Internal Revenue Service
EO Determinations Quality Assurance
Room 7-008
P.O. Box 2508
Cincinnati, OH 45201

Deliver to:

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Room 7-008
Cincinnati, OH 45202

You may 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

Enclosures
Publication 892