

Internal Revenue Service
TEGE Appeals Division
300 N. Los Angeles Street
Los Angeles, CA 90012

CERTIFIED

Department of the Treasury

Release Number: **201019033**
Release Date: 5/14/10
Date: 2/14/10

Taxpayer Identification Number:

Person to Contact:

Refer Reply to:

AP:LA:EMW

In Re:

Tax Years:

UIL Index:

501.03-00

501.33-00

501.36-00

Last Day to File a Petition with the
United States Tax Court: **MAY 20 2010**

Dear

This is a final adverse determination as to your application for exempt status under section 501(a) as an organization described under section 501(c)(3) of the Internal Revenue Code. Our adverse determination was made for the following reason(s):

You did not establish that you were operated exclusively for educational, charitable or other exempt purposes as required by section 501(c)(3) of the Internal Revenue Code. You did not engage primarily in activities which accomplish one or more of the exempt purposes specified in section 501(c)(3). Treas. Reg. § 1.501(c)(3)-1(c)(1).

Contributions to your organization are not deductible under Code § 170. You are required to file federal Form 1120 for the year(s) shown above.

If you decide to contest this determination under the declaratory judgment provisions of Code section 7428, a petition to the United States Tax Court, the United States Court of Claims, or the district court of the United States for the District of Columbia must be filed before the 91st (ninety-first) day after the date this determination was mailed to you. Contact the clerk of the appropriate court for rules for filing petitions for declaratory judgment. To secure a petition form from the United States Tax Court, write to the United States Tax Court, 400 Second Street, N.W., Washington, D.C. 20217.

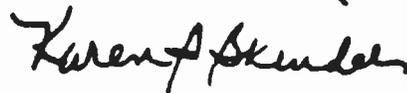
You also have the right to contact the Office of the Taxpayer Advocate. However, you should first contact the person whose name and telephone number are shown above since this person can access your tax information and can help you get answers. You can call 1-877-777-4778, and ask for Taxpayer Advocate assistance.

Taxpayer Advocate assistance cannot be used as a substitute for established IRS procedures, formal appeals procedures, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determinations, or extend the time fixed by law that you have to file a petition in the United States Tax Court. The Taxpayer Advocate, can however, see that a tax matter, that may not have been resolved through normal channels, gets prompt and proper handling.

We will notify the appropriate State officials of this final adverse determination of your exempt status, as required by Code section 6104(c).

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

Sincerely,



Karen A. Skinder
Appeals Team Manager

cc:



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Date: June 11, 2009

Contact Person:

Identification Number:

Contact Number:

Fax Number:

Employer Identification Number:

Legend

M =

N =

O =

P =

Q =

A =

B =

C =

D =

UIL Nos: 501.03-05
501.36-00
513.04-00
509.02-02
501.06-00

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) and further that you are not a supporting organizations as defined in section 509(a)(3) of the Code. The basis for our conclusion is set forth below. This letter supersedes our letter dated Jan. 23, 2009.

ISSUES

1. Does the applicant, which provides management and administrative services to exempt organizations, qualify for exemption under section 501(c)(3) of the Code?
2. If the applicant is exempt, is it a supporting organization, as described in IRC section 509(a)(3) of the Code?
3. Does the applicant, which provides management and administrative services to exempt organizations, qualify for exemption under section 501(c)(6) of the Code?

FACTS

You, M, (the applicant) are a corporation formed on A, and operate pursuant to the laws of the State of B. Article II A of your Articles of Incorporation specifies that you are organized to operate exclusively for charitable and educational purposes within the meaning of section 501(c)(3) of the Internal Revenue Code. It further states that you are a project of the citizens of C and D dedicated to "planning for an enhanced quality of life, economic health and growth for years and generations to come by providing a forum for discussion, consciousness raising and information/education by collecting, cataloging and publishing information on relevant and important issues affecting C and D by providing a list of actions opportunities, and by serving as a catalyst for action."

You have nine board members; one each from the Members, N, O, P, Q (four), one from the City C, one from the County D, one from a local college, and two from the community. Six out of the nine board members are from the Members since the City and County Officials also serve on most of the four supported organizations' boards.

Article IV, Section 4 of your Bylaws specify that one director shall be named by each of the member organizations, one named by C and one named by D. The remaining directors "shall be representative of the community in which the corporation's principal office is located." It does not require that a majority of your Board members must serve on the boards of your supported organizations.

You wish to be recognized as a publicly supported organization under section 509(a)(3) of the Code and have requested a definitive ruling. Your activities are limited to providing administrative support to the specifically named organizations identified in your application. Two of your supported organizations, N and O, are exempt under 501(c)(3) of the Code and publicly supported under sections 509(a)(1) or (2). The other two supported organizations, P and Q, are exempt from federal income tax under section 501(c)(6). You were created by these four organizations (the Members) to centralize their administrative functions.

In your application, you state that you were created to avoid duplication of work by the Members. Your application details that you provide personnel, fringe benefits, payroll service, and office administration, including telephone service and accounting functions for the Members. The cost of your services is reimbursed by the Members monthly. You further state that "you approve an annual budget listing the charges allocated for each organization."

Your letter of March 26, 2007 affirmed this fact and further detailed your services to the Member. It states:

M provides administrative support, accounting and support staff to the supported organizations so that the organizations can concentrate on their core functions with better efficiency. The support staff not only provides administrative support but also assists with various events and fundraisers for the supported organizations.

It further explains your activities as following:

M not only provides administrative service and H/R management, but we also provide support staff that assists with various fund raising functions and community events hosted by the supported organizations. This includes helping raise money for community improvements and donated to various charitable organizations, as well as money used to improve the community's image. More than that, M was formed to created a partnership between all of these organizations so that they could work together on projects for the community in a more efficient and effective manner.

In your letter of September 15, 2008, you provided a percentage breakdown of your activities:

	2002	2003	2004	2005	2006	2007
Administrative Services						
Exempt Activities						
Fundraising						

The exempt activities listed included opportunities for showcasing products, social networking, joint advertising and civic festivals.

This letter also allocated the time spent by your three-person workforce. By administrative services totaled % or more for each person. Exempt activities decreased to % for each person by ; member activities ranged from % to %.

Almost all of your revenues come from membership contributions. Your members are assessed fees based on how much of your work is attributed to work benefiting their individual operations. Between 2002 and 2006, % of your expenses and fees were allocated to the two members that are exempt under IRC 501(c)(6). In the most recent year reported (2006), % of your expenses and fees were allocated to these 501(c)(6) members.

	FY 6/02	FY 6/03	FY 6/04	FY 6/05	FY 6/06	Total
Expenses and Fees From (c)(6) Members Percentage						

You have four member organizations in essence since the City and the County support you financially but they do not receive any services or direct benefits from you. In the letter of April 3, 2009, you provided the member organizations' activities. The following roughly summarizes their activities with respect to common business interest:

- P: Promoting commerce and business in general (%), community improvement (%) charitable activities (%), other activities (%)
- Q: Providing information about financial resources, government advocacy, building and land inventories, economic and demographic data; promoting startup, relocation, expansion and retention of business; and assisting with labor training resources (100%)

O: Re-vitalizing downtown area and improving communities (100%)

N: Promoting area events and tourism (100%)

ISSUE 1 - 501(c)(3)

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 or educational purposes, provided that no part of the net earnings inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(a)(1) of the Regulations provides that in order for an organization to be exempt under section 501(c)(3) of the Code it 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 or operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the Regulations provides that an organization operates exclusively for exempt purposes only if it engages primarily in activities that accomplish exempt purposes specified in section 501(c)(3) of the Code. An organization must not engage in substantial activities that fail to further an exempt purpose.

Section 502 of the Code clarify that an organization operated for the primary purpose of carrying on a trade or business for profit shall not be exempt under IRC 501 on the ground that all of its profits are payable to one or more organizations exempt under IRC 501.

Section 1.502-1(b) of the Regulations provides an example which describes an organization that is owned by several exempt organizations. However, these organizations are not related to each other. The organization in this example provides electric power to each of the unrelated "owner". If any one of the tax-exempt "owners" were to carry on this activity of providing electric power to the other unrelated "owners", it would be considered an unrelated business. Therefore, the organization described in this example is not exempt.

In Better Business Bureau v. United States, 326 U.S. 279 (1945), the Supreme Court stated that the presence of a single nonexempt purpose, if substantial in nature, will preclude exemption under section 501(c)(3) of the Code, regardless of the number or importance of statutorily exempt purposes. Thus, the operational test standard prohibiting a substantial nonexempt purpose is broad enough to include inurement, private benefit, and operations that further nonprofit goals outside the scope of section 501(c)(3).

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), the Tax Court considered an organization that provides consulting services to groups that were mostly 501(c)(3) organization. The organization charged fees for its services set at or close to its own cost. The court concluded that there was nothing to distinguish these activities from those of an ordinary commercial consulting enterprise, and affirmed the Service's denial of exemption under IRC

501(c)(3).

Rev. Rul. 71-529 held that a nonprofit organization that provided assistance in the management of participating colleges' and universities' endowment or investment funds for a fee substantially below the cost of providing such service, qualified for exemption under IRC 501(c)(3). Membership was restricted to colleges and universities exempt under section 501(c)(3) of the Code, and its board of directors was composed of representatives of the member organizations.

Application of Law

Your primary activity consists of providing accounting, administrative, and payroll related services to your members. This activity is not inherently educational or charitable by itself under 501(c)(3) of the Code. An organization cannot be recognized as exempt under section 501(c)(3) unless it shows that it is both organized and operated for exclusively for charitable, educational, or other exempt purpose. You failed to meet the operational test of section 1.501(c)(3)-1(a)(1) and section 1.501(c)(3)-1(c)(1) of the regulation because you are organized for substantial commercial purposes, and operate in a manner that a private commercial entity operates.

Like the organization in B.S.W. Group Inc. v Commission, *supra.*, you charge fees for your services at cost. This does not distinguish your organization from an ordinary commercial business that provides back-office services to exempt organizations.

You are similar to the organization in Section 1.502-1(b) of the Regulations because the Members are not related to each other and are not controlled by a parent organization like the organization in the example; therefore, you are not exempt.

Unlike the organization described in Rev. Rul. 71-529, *supra.*, you do not offer services at substantially below cost. In addition, the breakdown of your expenses and fees indicates that you primarily serve organizations that are exempt under IRC 501(c)(6). Offering fee-based services to business leagues does not serve the purposes specified in IRC 501(c)(3). Granting you exemption under 501(c)(3) would allow the usual members/contributors to your 501(c)(6) supported organizations to take a charitable deduction when they could not do so by contributing directly to your 501(c)(6) members.

Offering fee-based services in this manner is a substantial nonexempt purpose. This is similar to the situation described in Better Business Bureau v. United States, *supra.*, and is sufficient to preclude exemption.

DETERMINATION - ISSUE 1:

In summary, your primary purpose is to provide accounting, administrative, and payroll related services to your Members, which are exempt under both 501(c)(3) and 501(c)(6). This activity by itself is not educational or charitable under 501(c)(3) of the Code; rather, it is a trade or business as defined in Section 502 of the Code. Providing services to exempt business leagues

is also not a charitable activity as described in IRC 501(c)(3). Therefore, you do not qualify for exemption under IRC 501(c)(3).

ISSUE 2 - 509(a)(3)

Introduction:

Even if we determined that you were described in Section 501(c)(3) of the Code, you would not qualify as a supporting organization as described in Section 509(a)(3).

Law - Organizational and Operation Test:

Section 509(a)(3) of the Code provides that the term "private foundation" does not include an organization which:

(A) is organized, and at all times thereafter is operated, exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more specified organizations described in section 509(a)(1) or (2),

(B) is operated, supervised, or controlled by or in connection with one or more organizations described in section 509(a)(1) or (2), and

(C) is not controlled directly or indirectly by one or more disqualified persons (as defined in section 4946) other than foundation managers and other than one or more organizations described in section 509(a)(1) or (2).

IRC 509(a)(4) also provides that a supporting organization can be qualified as a 509(a)(3) entity when it carries on a charitable function of organizations described in sections 501(c)(4), 501(c)(5), or 501(c)(6). The supported organization sources of support must qualify as 509(a)(2) and the majority of the supporting organization's board must be elected by the supported organizations.

Regs. 1.509(a)-4(b)(1) provides that a supporting organization must be organized and operated exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more specified supported organization(s). If an organization fails to meet either the organizational or the operational test, it cannot qualify as a supporting organization. The operational test is concerned with permissible beneficiaries and permissible activities.

Reg. 1.509(a)-4(e)(1) provides that a supported organization will be regarded as "operated exclusively" to support one or more specified public supported organization only if it engages solely in activities which support or benefit the specified publicly supported organizations.

Application of Law

A majority of your activities benefits two supported organizations that are exempt under IRC 501(c)(6). Their income by source would qualify as 509(a)(2) and the majority of the supporting organization's board come from the supported organizations. Thus, you satisfy Regs. 1.509(a)-4(b)(1). However, you do not carry out any of their charitable or exempt functions. Rather, you primarily provide routine office management tasks that are not in themselves charitable activities. Therefore, you failed to meet the requirement of Reg. 1.509(a)-4(e)(1).

DETERMINATION - ISSUE 2:

You do not qualify for exclusion from private foundation status under section 509(a)(3) of the Code. You did not pass the operational test.

ISSUE 3 - 501(c)(6)

Law

Section 501(a) of the Code provides for the exemption from Federal income tax of organizations described in section 501(c).

Section 501(c)(6) of the Code provides exemption from Federal income tax for "Business leagues, chambers of commerce, real-estate boards, boards of trade, or professional football leagues (whether or not administering a pension fund for football players), not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual."

Section 1.501(c)(6)-1 of the Income Tax Regulations states, "A business league is an association of persons having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of the kind ordinarily carried on for profit. It is an organization of the same general class as a chamber of commerce or board of trade. Thus, its activities should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons. An organization whose purpose is to engage in a regular business of a kind ordinarily carried on for profit, even though the business is conducted on a cooperative basis or produces only sufficient income to be self-sustaining, is not a business league."

In Revenue Ruling 67-176, 1967-1, CB140 (Jan. 01, 1967) the organization was formed to advance a given profession, contribute to the welfare and education of students preparing for that profession, to furnish financial aid to that profession in the form of grants and loans and to do other things for the benefit, welfare and security of its members. An emergency loan fund is provided which allows members to borrow small amounts of money interest free for short periods. The Ruling mentions Income Tax Regulation 1.501(c)(6)-1 which indicates that a business league is an association of persons having some common business interest, the

purpose of which is to promote said common interest and not to engage in a regular business of a kind ordinarily carried on for profit. Its activities should be directed at the improvement of business conditions of one or more lines of business as opposed to performance of particular services for individual persons. The Ruling found that the emergency loan plan, among other activities served primarily as a convenience and for the economy of the members in providing financial aid, which is found to be the performance of particular services to members as opposed to improving a line of business. Thus, exemption under section 501(c)(6) was not afforded to the organization.

In Revenue Ruling 76-38, 1976-1 CB 157, (Jan. 01, 1976), the organization in question was formed to maintain the goodwill and reputation of the credit unions in a particular state. To achieve this goal, they maintained a fund for assistance to credit unions having financial difficulty to keep them solvent so that their members would not lose deposits upon liquidation. They allowed member credit unions to take interest free loans from the fund. The loans were to be repaid only if the borrowers were financially able to do so. The Ruling found that the loan activities were not solely calculated to accomplish the objective of improving the industry's image by protecting depositors. Further, the favorable terms of the loans to members was done in a manner that would provide little or no additional security to depositors and is clearly for the convenience (and economy) of the members in their business and does not constitute an exempt activity under section 501(c)(6).

In MIB, Inc. v. Commissioner of Internal Revenue, 734 F.2d 71 (1986), an organization whose membership consisted of insurance companies was denied exemption as a business league under section 501(c)(6) of the Internal Revenue Code. The principal activity carried on by MIB was the maintenance and operation of a computerized system for compiling, storing and distributing information about applicants for life insurance. MIB argued that its activities created a deterrent to fraud which created benefits to the industry through reduced investigation expenses and reduced losses due to misclassification of applicants. The Court held MIB's activities by their nature consisted of rendering particular services for individual member companies and served to benefit the individual members' businesses. The Court also stated that even though the services produced various indirect and intangible benefits for the industry as a whole, the fact remained that the rendered services were in form and substance particular services for individual member companies.

Application of Law

The purpose of section 501(c)(6) of the Code is to give income tax exemption for business leagues, chambers of commerce, real-estate boards, boards of trade, or professional football leagues (whether or not administering a pension fund for football players). However, you do not belong to any of such categories since your primary activity consists of providing accounting, administrative, and payroll related services to your members.

Section 1.501(c)(6)-1 of the Income Tax Regulations specifically states, "Activities of a business league should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons." In contrast, you do not improve the conditions of one or more lines of business of the member

organizations. Your coordinated services to the members may reduce the costs of operation and improve the efficiency of supporting function, but it does not improve the conditions of one or more lines of the business themselves.

According to the activities of your member organizations, the common interest of your member organizations consist of economic and community development; thus, your main activities should consist of improving the business conditions of economic and community development to be qualified as a 501(c)(6) organization. The organizations in Revenue Ruling 67-176, *supra*, and Revenue Ruling 76-38, *supra*, run a fund for the members. The rulings concluded that it is the performance of particular services to members as opposed to improving a line of business since it is for the convenience and economy of the members. Your accounting and administrative work for the member organizations are very similar to the fund service of these organizations because the purpose of your work is also for the convenience and economy of the members.

You are also analogous to the organizations in MIB, Inc. v. Commissioner of Internal Revenue, *supra*, because your activities by their nature consisted of rendering particular services for individual member companies and served to benefit the individual members' businesses just like the organization in the case. In fact, the situation of MIB is almost identical with yours except that MIB provides computer related services instead of accounting and administrative services.

The fact that you conduct some activities that improve the conditions of one or more lines of business of the member organizations is insufficient to overcome your non-exempt purpose because such activities are insubstantial. See Better Business Bureau v. United States.

DETERMINATION - ISSUE 3:

In summary, your primary purpose is to provide accounting, administrative, and payroll related services to your Members, which are exempt under both 501(c)(3) and 501(c)(6). The activities are not directed to the improvement of business conditions of one or more lines of business, but to engagement in a regular business of the kind ordinarily carried on in for-profit business. Providing such services to exempt business leagues is not an exempt activity under IRC 501(c)(6). Therefore, you do not qualify for exemption under IRC 501(c)(6).

SUMMARY:

In summary, you do not meet the requirements under both sections of 501(c)(3) and 501(c)(6) because you fail both the organizational and operational tests. Your primary purpose is to minimize the operating cost of the Members which is a commercial, not charitable, activity. Therefore, we have determined that you have failed to establish that your activities further tax-exempt purposes within the meaning of sections 501(c)(3) and 501(c)(6). Accordingly, you do not qualify for exemption as an organization described in sections 501(c)(3) and 501(c)(6) of the Codes and you must file federal income tax returns. Further, you are not a supporting organization as described in IRC 509(a)(3).

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

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
Room 7-008
550 Main Street
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