



**Department of the Treasury  
Internal Revenue Service  
Tax Exempt & Government Entities**

Date: November 21, 2014  
Employer ID number:

Person to contact/ID number:

Contact telephone number:

Form you must file:

Tax years:

Release Number: **201507023**

Release Date: 2/13/2015

UIL Code: 501.03-00

Dear \_\_\_\_\_ :

This is our final determination that you don't qualify for tax-exempt status under Section 501(c)(3) of the Internal Revenue Code (the Code).

We made this determination for the following reasons:

You failed to establish that your income does not inure to the benefit of private individuals and shareholders, which is prohibited by section 501(c)(3). In addition, you are operated for a substantial private purpose, including operating for the benefit of a for-profit business, which is prohibited by section 501(c)(3). Finally, you are not organized exclusively for charitable and educational purposes as required by section 501(c)(3).

Because you don't qualify as a tax-exempt organization under Section 501(c)(3) of the Code, donors can't deduct contributions they make to you under Section 170. You must file federal income tax returns for the tax years listed at the top of this letter using the required form (also listed above) within 30 days from the date of this letter unless you request an extension of time to file.

If you decide to contest this determination under the declaratory judgment provisions of Section 7428 of the Code, you must initiate a suit in the United States Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia before the 91st day after the date we mailed this letter to you. Contact the clerk of the appropriate court for rules on initiating suits for declaratory judgment. You still must file returns and pay taxes if you file a declaratory judgment suit under Section 7428.

We'll make this letter and our proposed adverse determination letter available for public inspection, as required under Section 6110 of the Code, after redacting identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the letters that show our proposed redactions. If you disagree with our proposed redactions, follow the instructions in Notice 437 on how to notify us. If you agree with our redactions, you don't need to take further action.

If you have questions about this letter, you can contact the person listed at the top of this letter. If you have questions about your federal income tax status and responsibilities, call customer service at 1-800-829-1040 (TTY 1-800-829-4933 for deaf or hard of hearing), or customer service for businesses at 1-800-829-4933.

Sincerely,

Tamera Ripperda  
Director, Exempt Organizations

Enclosures:

Notice 437

Redacted Letter 4036, *Proposed Adverse Determination under IRC Section 501(c)(3)*

Redacted Letter 5419, *Final Adverse Determination Organization is not Exempt under IRC Section 501(c)(3)-After Protest*



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

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

Date: February 10, 2014

Contact Person:

UIL: 501.03-00

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

LEGEND:

You =

Gym =

Dear :

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

FACTS

You were organized as a nonprofit corporation to: "foster the education and development of children's interest by participating in the activities of dance, gymnastics, Tae Kwon Do, child care, tumbling, cheer, and other children's social/athletic events." In your application, you described yourself as a "parent led booster club". Your articles contained the proper clauses concerning inurement, political activities, and dissolution. Your articles create a single class of members, consisting of those who pay the annual membership fee.

Your By-Laws further define "member" as the parent or legal guardian of a child who is currently enrolled in and actively participating in a program at a gymnastic complex with a name similar to yours ("Gym".) Members elect your directors, and the directors chose your officers. The By-Laws create four standing committees: Nominating, Competition, Fundraising, and Spirit, Travel, and Event. The duties of the "Spirit" Committee include advising the board on matters pertaining to publicity for Gym. One of your directors owns the Gym at which the children of your members take lessons and compete.

Your biggest category of expense is fundraising. You spent more than \$8500 to raise over \$16,000. Your other expenses totaled less than \$1000, most of which paid for assistance in applying for exempt status.

You do not directly provide athletic events or sporting activities or teach athletics. Rather you explain that you "help raise funds to help the athletes perform at... competitions." Parents sell

things such as steak, cookbooks, soup and coupon books to friends, family, neighbors and coworkers.

The money that each family raises by participating in your fundraising events is "earmarked for that family and goes towards their child's competition fees." Your "goal is to help alleviate some of the financial burden it costs to compete at these events." Families that do not participate in the fundraisers are "responsible to pay for the portion of their child's competition and coaches fees." As you explain:

We facilitate the fundraisers and the parents participate in these fundraisers we put on for them to help raise money for their children to compete, we keep track of their fundraising for them and the money goes towards their children's competition and coaching fees.

You do not currently provide any scholarships.

In the future, you would like to solicit sponsorships from local businesses with banners hanging in the Gym, advertising on parent t-shirts, and links from your website to the company website.

## LAW

I.R.C. § 501(c)(3) describes organizations organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or education purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment)...no part of the net earnings of which inures to the benefit of any private shareholder or individual....

Treas. Reg. § 1.501(c)(3)-1(a) states that in order to be described in § 501(c)(3), an organization must be both organized and operated for one or more of the purposes specified in that section.

Treas. Reg. § 1.501(c)(3)-1(b) describes the organizational requirements for an exempt entity, including the required provisions for its articles of incorporation.

Treas. Reg. § 1.501(c)(3)-1(c)(1) states that 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 the exempt purposes specified in § 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.

Treas. Reg. § 1.501(c)(3)-1(d)(1)(i) describes various exempt purposes, including "charitable."

Treas. Reg. § 1.501(c)(3)-1(d)(1)(ii) provides that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. To meet the requirement of this subsection, the burden of proof is on the organization to show 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.

Treas. Reg. § 1.501(c)(3)-1(d)(2)(i) defines "charitable" in its generally accepted legal sense, and as including advancement of education and science.

Treas. Reg. § 1.501(c)(3)-1(d)(3)(i) provides that the term educational relates 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.

Rev. Rul. 69-175, 1969-1 C.B. 149, describes an organization created to provide bus transportation for school children to a tax-exempt private school. The organization was formed by the parents of pupils attending the school. The organization provided transportation to and from the school for those children whose parents belonged to the organization. Parents were required to pay an initial family fee and an additional annual charge for each child. The IRS determined that "when a group of individuals associate to provide a cooperative service for themselves, they are serving a private interest."

Rev. Rul. 71-395, 1971-2 C.B. 228, holds that a cooperative art gallery formed and operated by a group of artists for the purpose of exhibiting and selling their works does not qualify for exemption under § 501(c)(3). The IRS concluded that the cooperative gallery served the private purposes of its members, even though the exhibition and sales of paintings were also educational in some respects.

In Ginsberg v. Commissioner, 46 T.C. 47 (1966), the court considered a collective organization created to dredge waterways. The majority of the funds for this activity came from owners of property adjacent to the waterways. The court found that the primary beneficiaries were the adjacent property owners. Any benefit to the general public because these dredged waterways would be a safe harbor for boats during a storm was secondary. Therefore, the organization was not exempt because of the significant private benefit provided.

In Aid to Artisans, Inc. v. Commissioner, 71 T.C. 202 (1978), the court held an organization that marketed handicrafts made by disadvantaged artisans through museums and other non-profit organizations and shops was operated for exclusively charitable purposes within the meaning of § 501(c)(3). The organization, in cooperation with national craft agencies, selected the handicrafts it would market from craft cooperatives in disadvantaged communities. The organization marketed only handicrafts it purchased in bulk from a community of craftsmen. The court concluded that the overall purpose of the activity was to benefit disadvantaged communities. The method it used to achieve its purpose did not cause it to serve primarily private interests because the disadvantaged artisans constituted a charitable class and the organization showed no selectivity with regard to benefiting specific artisans.

In Retired Teachers Legal Def. Fund. v. Comm, 78 T.C. 280 (1982), the Tax Court referred to Black's Law Dictionary to define "benefit" and conclude that the private benefits referred to in the Treasury Regulations for exempt organizations were not unconstitutionally vague.

In P.L.L. Scholarship v. Commissioner, 82 T.C. (1984), an organization operated bingo games at a bar for the avowed purpose of raising money for scholarships. The board included the bar owners, the bar's accountant, also a director of the bar, as well as two others. The court reasoned that, because the bar owners controlled the organization and appointed the organization's directors, the activities of the organization could be used to the advantage of the

bar owners. The organization claimed that it was independent because there was separate accounting and no payments were going to the bar. The court was not persuaded:

A realistic look at the operations of these two entities, however, shows that the activities of the taxpayer and the Pastime Lounge were so interrelated as to be functionally inseparable. Separate accountings of receipts and disbursements do not change that fact.

The court went on to conclude that because the record indicates that it substantially benefited private interests, exemption was properly denied.

In Church By Mail, Inc. v. Commissioner, T.C. Memo 1984-349, *aff'd* 765 F. 2d 1387 (9<sup>th</sup> Cir. 1985), the Tax Court found that a church was operated with a substantial purpose of providing a market for an advertising and mailing company owned by the same people who controlled the church. The church argued that the contracts between the two were reasonable, but the Court of Appeals pointed out that "the critical inquiry is not whether particular contractual payments to a related for-profit organization are reasonable or excessive, but instead whether the entire enterprise is carried on in such a manner that the for-profit organization benefits substantially from the operation of the Church."

Wendy Parker Rehab. Found. Inc. v. Comm., T.C. Memo. 1986-348, concerned an organization created by a family to aid an open-ended class of "victims of coma." However, the organization stated that it anticipated spending 30 percent of its income for the benefit of Wendy Parker, significant contributions were made to the organization by the Parker family, and the Parker family controlled the organization. Wendy's selection as a substantial recipient of funds substantially benefited the Parker family by assisting with the economic burden of caring for her. The benefit did not flow primarily to the general public as required under § 1.501(c)(3)-1(d)(1)(ii). Therefore, the Foundation was not exempt under § 501(c)(3).

The court in Capital Gymnastics Booster Club v. Comm., T.C. Memo 2013-193, analyzed the fundraising activity of a gymnastic booster club. Parent-members sold items and were awarded points in proportion to the profit that the family generated. Each point was valued at \$10, and used to offset the family's assessed costs of competition for their children. Parents who did not fundraise did not receive a benefit from the activity, they were responsible for writing a check to the organization for the full assessment for their children. The court held that the fundraising structure allowed assets of the organization to inure to the members who control the organization.

## RATIONALE

Congress specifically identified fostering amateur sports as an exempt purpose that would entitle an organization to exempt status if it meets the other requirements of § 501(c)(3). You are properly organized for exempt status, but because your manner of operation provides inurement to your members and private benefit to a business owned by one of your directors, we cannot recognize you as exempt under § 501(c)(3).

An exempt organization must operate exclusively for public good. If an entity operates for the benefit of specific individuals, it is not operating exclusively for exempt purposes. Section 1.501(c)(3)-1(d)(1)(ii). The regulations clarify that an organization may not operate for the benefit of its creators or other designated persons. Those with control over the organization,

such as members, directors, or officers may not direct income, assets or any "advantage; profit; fruit; privilege; gain; [or] interest." Retired Teachers Legal Def. Fund.v. Comm, 78 T.C. 280.

Membership organizations that primarily benefit their own members have long been denied exempt status. Rev. Rul. 69-175, 1969-1 C.B. 149 (parent-organized bus transportation to their children's private school); Rev. Rul. 71-395, 1971-2 C.B. 228 (cooperative art gallery to sell members' art); Ginsburg v. Commissioner, 46 T.C. 47 (dredging primarily benefited adjacent landowner-members). An organization may not operate to benefit specific, designated persons, even if they are members of a charitable class. For example, because a foundation established to raise money for people in comas expended a significant portion of organizational funds on the daughter of the founders, it was held not exempt. Wendy Parker, T.C. Memo. 1986-348.

Your purpose is to assist your members fulfill a financial obligation for their children. Fundraising is your primary activity. You "facilitate" and "put on fundraisers" and the majority of your budget is spent on fundraising. Evidently you are using your funds, your time, and your exempt status to provide fundraising opportunities for your parents. However, the money that they make in your name does not go into your general budget. Rather, you keep an accounting of how much revenue each member brings in and permit each member to apply that revenue to the cost of athletic competitions for their children. Members who do not fundraise pay the cost of competitions from their own funds. You do not provide scholarships to any family. You do not jointly fundraise for the organization and then allocate to all equally or based on need or merit. The benefit from the fundraising activity is allocated in direct proportion to the participation of the family.

An athletic booster club similar to yours was the subject of a recent opinion from the Tax Court. Capital Gymnastics Booster Club v. Comm, T.C. Memo 2013-193. The judge described the system by which the club kept track of how much each family raised so that it could allocate a proportionate amount of the club's funds to pay for that family's competition expenses. He concluded that even though the club did not distribute cash to the member parents, the arrangement resulted in inurement to them. Although the club conducted some activities that benefited all members and generally fostered amateur athletics, a primary activity was raising money to relieve the financial obligations of its fundraising members. Therefore, he affirmed the decision of the IRS denying exempt status to the booster club.

You also devote a significant amount of time and resources to assisting your members raise money for their own children's competition expenses. Therefore the same legal conclusion applies to your application for exempt status. Although the Capital Gymnastics Booster Club opinion was issued last year, it builds upon and validates the longstanding legal position of the Service regarding operation for the benefit of members and other insiders. This position was explained and approved in the revenue rulings and cases referred to above, among others.

In addition to the benefit to all your fundraising members, you provide a special benefit to the director who owns the gymnasium where all of the children of your members take lessons and compete. An exempt organization may not operate to direct funds, business, or other benefits to a commercial entity. P.L.L. Scholarship v. Commissioner, (events to raise funds for scholarships benefit affiliated bar), 82 T.C. Church by Mail (owners of printing and mailing service benefited from business directed to it from church they also controlled) The fact that all of the money that you raise enables athletes to compete on teams sponsored by the gym is a substantial private benefit. You also referred to using 25% of the membership fee to "be used towards upkeep of equipment they use for competing each year." It is not clear whether you were referring to

equipment owned by the Gym. If so, it would be additional inurement to a director and benefit to a commercial entity.

Because you significantly benefit your members rather than operating exclusively for exempt purposes, we cannot recognize you as exempt under §501(c)(3).

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](http://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:

1111 Constitution Ave, N.W.  
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,

Karen Schiller  
Acting Director, Exempt Organizations  
Rulings and Agreements