

INTERNAL REVENUE SERVICE
NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM

September 18, 2015

[Third Party Communication:
Date of Communication: <Month> DD, YYYY]

Number: **201633032**
Release Date: 8/12/2016
Index (UIL) No.: 513.00-00
CASE-MIS No.: TAM-109518-15

Director
TEGE Exempt Organizations Examination

Taxpayer's Name:
Taxpayer's Address:

Taxpayer's Identification No
Year(s) Involved:
Date of Conference:

LEGEND:

Organization =

ISSUE(S):

Whether Organization's sale of through its online store, printed catalog, and at various unrelated retail outlets is an unrelated trade or business within the meaning of § 513 of the Internal Revenue Code.

CONCLUSION(S):

Organization's sale of through its online store, printed catalog, and at various unrelated retail outlets is an unrelated trade or business within the meaning of § 513.

FACTS:

Organization is a not-for-profit corporation organized under state law, and is recognized by the Internal Revenue Service as an organization described in § 501(c)(3).

Organization states that it is organized for the main purpose of preserving so that will not become extinct and can be used

for future . Organization's Articles of Incorporation provide that Organization is organized "for the literary, charitable and educational purposes of promoting research, acquiring and disseminating information and educational materials, promoting awareness and discussion of the problems of

, attempting solutions to these problems through the development of , and providing publications to serve as educational tools, guides and communications networks for individuals and organizations interested in the conservation of ."

Organization's Bylaws provide that Organization is "conserving and promoting America's diverse but endangered heritage for future generations by ." The Bylaws further provide that Organization "is formed for the literary, charitable, educational, and scientific purposes of ."

Organization's activities include providing publications regarding , providing research and education about conserving to keep from being extinct, and helping to develop , and networks for .

Organization collects and preserves from donors, such as families whose are . Organization's headquarters are where Organization

. The serves where . The are collected and stored.

Organization conducts workshops, seminars, conferences, and other events that are open to members and the general public. A visitor's center at has information displays regarding

. There are near the visitor's center which serve to explain Organization's mission and organizational purpose.

Organization maintains a public website. The website explains Organization's mission, activities, and membership opportunities. The educational portion of the website instructs about , how to donate to Organization for preservation, how to preserve , and how to participate in .

Members can share stories about the history and characteristics of

In addition, Organization sells to the public through its catalog (available both online and in print) and through unrelated retail outlets. The manager, in consultation with the preservation staff, determines which to offer for sale. The publication of the annual catalog is a . The sale of a

once are on hand. commences

About twenty percent of sold by Organization are produced at . These operations are conducted by employees of Organization. The remainder is produced by under contract with Organization. Organization provides these with the and inspects and monitors including performing quality control checks on

processing of orders and the packaging and distribution of . The occur

are sold in standard packages. The front of the package shows a picture of . The back of the package provides instructions typical of commercial packages, plus one or two sentences on . Organization's office and website addresses are also listed, in small print, on the back of the packages.

A prominent link on the home page of Organization's website connects visitors directly to the online store where books, and -related products are sold. A person can also link directly to the online store through online search engines. The is published . Recent catalogs comprise approximately pages. Aside from a few pages with information about Organization, its programs, and how to , the catalog is similar to the catalogs published by for-profit companies.

packages are also sold throughout the country from located in retail outlets. Retailers can request a from Organization.

LAW AND ANALYSIS:

Section 501(c)(3) describes as exempt from federal income tax organizations organized and operated exclusively for charitable, scientific, or educational purposes,

no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 511 imposes a tax on the unrelated business taxable income of an exempt organization that is otherwise exempt from federal income tax pursuant to § 501(c)(3).

Section 512(a)(1) defines the term “unrelated business taxable income” as gross income derived by any organization from any unrelated trade or business (as defined in § 513) regularly carried on by it, less the allowable deductions which are directly connected with the carrying on of such trade or business, both computed with the modifications provided in § 512(b).

Section 513(a) defines the term “unrelated trade or business” as any trade or business whose conduct is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under § 501.

Section 513(c) explains that, for purposes of § 513, the term “trade or business” includes any activity which is carried on for the production of income from the sale of goods or the performance of services. For purposes of the preceding sentence, an activity does not lose identity as a trade or business merely because it is carried on within a larger aggregate of similar activities or within a larger complex of other endeavors which may, or may not, be related to the exempt purposes of the organization. Where an activity carried on for profit constitutes an unrelated trade or business, no part of such trade or business shall be excluded from such classification merely because it does not result in profit.

Section 1.501(c)(3)-1(d)(5) provides, in part, that the term “scientific,” as used in § 501(c)(3), includes the carrying on of scientific research in the public interest. For research to be scientific within the meaning of section 501(c)(3), it must be carried on in furtherance of a scientific purpose. Scientific research does not include activities of a type ordinarily carried on as an incident to commercial or industrial operations, as, for example, the ordinary testing or inspection of materials or products or the designing or construction of equipment, buildings, etc.

Section 1.513-1(a) provides that the gross income of an exempt organization subject to the tax imposed by § 511 is includible in the computation of unrelated business taxable income if: (1) it is income from trade or business; (2) such trade or business is regularly carried on by the organization; and (3) the conduct of such trade or business is not substantially related (other than through the production of funds) to the organization's performance of its exempt functions.

Section 1.513-1(b), provides that, for purposes of § 513, the term “trade or business” has the same meaning it has in § 162, and generally includes any activity carried on for the production of income from the sale of goods or performance of services. Thus, the term “trade or business” in § 513 is not limited to integrated aggregates of assets, activities, and good will which comprise businesses for the purposes of certain other provisions of the Internal Revenue Code. Activities of producing or distributing goods or performing services from which a particular amount of gross income is derived do not lose identity as trade or business merely because they are carried on within a larger aggregate of similar activities or within a larger complex of other endeavors which may, or may not, be related to the exempt purposes of the organization.

Section 1.513-1(d)(1) provides that gross income derives from unrelated trade or business, within the meaning of § 513(a), if the conduct of the trade or business which produces the income is not substantially related (other than through the production of funds) to the purposes for which exemption is granted. The presence of this requirement necessitates an examination of the relationship between the business activities which generate the particular income in question – the activities, that is, of producing or distributing the goods or performing the services involved – and the accomplishment of the organization’s exempt purposes.

Section 1.513-1(d)(2) provides, in part, that trade or business is “related” to exempt purposes only where the conduct of the business activities has a causal relationship to the achievement of exempt purposes (other than through the production of income), and is “substantially related” for purposes of § 513, only if the causal relationship is a substantial one. Thus, for the conduct of a trade or business from which a particular amount of gross income is derived to be substantially related to purposes for which exemption is granted, the production or distribution of the goods or the performance of the services from which the gross income is derived must contribute importantly to the accomplishment of those purposes. Where the production or distribution of the goods or the performance of the services does not contribute importantly to the accomplishment of the exempt purposes of an organization, the income from the sale of the goods or the performance of the services does not derive from the conduct of related trade or business. Whether activities productive of gross income contribute importantly to the accomplishment of any purpose for which an organization is granted exemption depends in each case upon the facts and circumstances involved.

Section 1.513-1(d)(3) provides that in determining whether activities contribute importantly to the accomplishment of an exempt purpose, the size and extent of the activities involved must be considered in relation to the nature and extent of the exempt function which they purport to serve. Thus, where income is realized by an exempt organization from activities which are in part related to the performance of its exempt functions, but which are conducted on a larger scale than is reasonably necessary for performance of such functions, the gross income attributable to that portion of the activities in excess of the needs of exempt functions constitutes gross income from the

conduct of unrelated trade or business. Such income is not derived from the production or distribution of goods or the performance of services which contribute importantly to the accomplishment of any exempt purpose of the organization.

Section 1.513-1(d)(4)(ii) provides that, ordinarily, gross income from the sale of products which result from the performance of exempt functions does not constitute gross income from the conduct of unrelated trade or business if the product is sold in substantially the same state it is in on completion of the exempt functions. Thus, in the case of an organization described in § 501(c)(3) and engaged in a program of rehabilitation of handicapped persons, income from the sale of articles made by such persons as a part of their rehabilitation training would not be gross income from conduct of unrelated trade or business. The income in such case would be from the sale of products, the production of which contributed importantly to the accomplishment of purposes for which exemption is granted the organization – namely, rehabilitation of the handicapped. On the other hand, if a product resulting from an exempt function is utilized or exploited in further business endeavor beyond that reasonably appropriate or necessary for disposition in the state it is in upon completion of exempt functions, the gross income derived therefrom would be from conduct of unrelated trade or business.

Section 1.513-1(d)(4)(iii) provides that, in certain cases, an asset or facility necessary to the conduct of exempt functions may also be employed in a commercial endeavor. In such cases, the mere fact of the use of the asset or facility in exempt functions does not, by itself, make the income from the commercial endeavor gross income from related trade or business. The test, instead, is whether the activities productive of the income in question contribute importantly to the accomplishment of exempt purposes.

Rev. Rul. 65-1, 1965-1 C.B. 226, concerns an organization, the primary purpose of which is to foster the development and design of labor saving agricultural machinery, including the development of new labor saving ideas and methods, and to conduct pertinent research. In carrying out its purposes, the organization undertakes to determine the need for the development of agricultural machinery which can plant, cultivate, or harvest crops of the type which are normally planted, cultivated, or harvested manually by agricultural laborers. Upon selecting a project to be developed, the organization consults with various public institutions, agricultural colleges, and engineers to ascertain if any similar projects are in process. If not, a grant is made by the organization to an appropriate public agency or firm to develop the necessary machinery. A committee then follows up the development under actual field conditions during the agricultural season. If a machine proves successful, a patent is sought in the organization's name and a manufacturer is licensed to build and sell the machine or device on an exclusive or non-exclusive basis. The successful development of such machinery is expected to ultimately result in reducing the cost of the particular crops to the public. The ruling concludes that the development or designing of machinery under these circumstances is incident to commercial or industrial operations and does not constitute "scientific research" within the meaning of § 1.501(c)(3)-1(d)(5). Furthermore,

the development of a new machine, the patents of which may be licensed on a restrictive basis to selected manufacturers, is directed toward benefiting those particular manufacturers. Under these circumstances the organization cannot be considered as operating for a public purpose. Accordingly, it is held that the organization is not organized and operated for scientific or any other purpose described in § 501(c)(3).

Rev. Rul. 66-179, 1966-1 C.B. 139, concerns a nonprofit organization organized for the purposes of instructing the public on horticultural subjects and stimulating interest in the beautification of the geographic areas. In furtherance of these purposes, the organization (1) maintains and operates a free library of materials on horticulture and allied subjects; (2) instructs the public on correct gardening procedures and conservation of trees and plants by means of radio, television, and lecture programs; (3) holds public flower shows of a noncommercial nature at which new varieties of plants are exhibited; (4) makes awards to children for achievements in gardening; (5) encourages roadside beautification and civic planting; and (6) makes awards for civic achievement in conservation and horticulture. It is concluded that the organization is organized and, in carrying out its purposes in the manner described above, is operated exclusively for charitable and educational purposes. Accordingly, the organization qualifies for exemption under § 501(c)(3).

Rev. Rul. 73-104, 1973-1 C.B. 263, concerns an organization, exempt from federal income tax under § 501(c)(3), that maintains and operates an art museum devoted to the exhibition of modern art. The museum offers for sale to the general public greeting cards that display printed reproductions of selected works from the museum's collection. Each card is imprinted with the name of the artist, the title or subject matter of the work, the date or period of its creation, and the museum's name. The organization sells the cards in the shop it operates in the museum. It also publishes a catalog in which it solicits mail orders for the greeting cards. In addition, the shop sells the cards at quantity discounts to retail stores. It is concluded that the sale of the greeting cards displaying printed reproductions of art works contributes importantly to the achievement of the museum's exempt educational purposes by stimulating and enhancing public awareness, interest, and appreciation of art. Moreover, a broader segment of the public may be encouraged to visit the museum itself to share in its educational functions and programs as a result of seeing the cards. The fact that the cards are promoted and sold in a clearly commercial manner at a profit does not alter the fact of the activity's relatedness to the museum's exempt purpose. Accordingly, it is held that these sales activities do not constitute unrelated trade or business under § 513.

Rev. Rul. 76-204, 1976-1 C.B. 152, concerns an organization formed for the purpose of preserving the natural environment. The organization accomplishes this purpose by acquiring and maintaining ecologically significant and undeveloped land such as swamps, marshes, forests, wilderness tracts, and other natural areas. The organization works closely with Federal, state, and local government agencies, and private organizations that are also concerned with environmental conservation. Through

preserving "ecologically significant undeveloped land, the organization is enhancing the accomplishment of express national policy of conserving the nation's unique natural resources." Thus, it is concluded that the "organization is advancing education and science and is benefiting the public in a manner that the law regards as charitable."

Rev. Rul. 78-145, 1978-1 C.B. 169, concerns a blood bank, exempt from income tax under § 501(c)(3), that collects and maintains inventories of human blood and blood products which are furnished to hospitals for immediate patient use. The whole blood collected by the blood bank is separated into components to meet demands for red blood cell transfusion. The blood bank is left with a large supply of plasma after removal of the red blood cells. Since only a small part of this supply of plasma is needed by the hospitals served by the blood bank, most of it is sold to commercial laboratories. The blood bank also obtains plasma from donors through a procedure called plasmapheresis, in which whole blood is drawn from a donor (typically a donor with rare antigens, reagents, and antibodies in his or her plasma), the red cells are separated and replaced in the donor, and plasma is collected. The plasma obtained through plasmapheresis is sold to commercial laboratories for processing into its various components. The blood bank also sells plasma to commercial laboratories that is salvaged from unused whole blood in the blood bank's inventory that is near the end of its shelf life. Finally, the blood bank purchases some plasma from other blood banks that it sells to commercial laboratories. The ruling states that although the sale of plasma to commercial laboratories does not bear a causal relationship to the blood bank's exempt functions, where the blood bank is merely disposing of products which result from the performance of its exempt functions, it will not be considered to be engaging in unrelated trade or business under § 1.513-1(d)(4)(ii). Since providing blood and blood products to hospitals is one of the organization's exempt functions, its sale of by-product plasma after the red blood cells are removed for use by the hospitals is not unrelated trade or business. Similarly, since the maintenance of an inventory of whole blood is one of the organization's exempt functions, its sale of plasma salvaged from blood in its inventory that is nearing the end of its shelf life is not unrelated trade or business, assuming that the amount of whole blood maintained in inventory is not excessive in view of the expected needs of the hospitals that the organization serves. On the other hand, plasma derived from donors through the process of plasmapheresis is not a product resulting from the performance of exempt functions, but is obtained for resale. Similarly, the plasma purchase from other blood banks and resold to commercial laboratories is not a result of the performance of an exempt function. In both of these cases, the sale of the plasma constitutes unrelated trade or business.

Rev. Rul. 78-384, 1978-2 C.B. 174, concerns an organization that owns farm land. It restricts the use of its farm land to farming or such other uses as the organization deems ecologically suitable for the land. Although the organization claims to benefit the public by restricting its land to uses compatible with the ecology of the area, it is not preserving land that has any distinctive ecological significance with the meaning of Rev. Rul. 76-204. In addition, any benefit to the public from this organization's self-imposed

restriction on its own land is too indirect and insignificant to establish that the organization serves a charitable purpose within the meaning of § 1.501(c)(3)-1(d)(2). Accordingly, because the organization does not preserve ecologically significant land and has not otherwise established that it serves a charitable purpose, it is not operated exclusively for charitable purposes and does not qualify for exemption from federal income tax under § 501(c)(3).

California Thoroughbred Breeders Assoc. v. Comm’r, T.C. Memo 1989-342, concerns a nonprofit corporation (“CTBA”, or “the petitioner”) organized “to encourage, assist, regulate, and protect the raising and breeding of Thoroughbred horses; to disseminate information to members of the corporation and to others who are breeders of Thoroughbred horses within the State of California, and to give support, financially or otherwise, to the development and general welfare of the breeding of Thoroughbred horses by breeders within the State of California....” CTBA’s bylaws limit membership to owners of one or more thoroughbred brood mares maintained for breeding in California. The Service recognizes CTBA as tax exempt as an organization described under the predecessor statute to § 501(c)(5). CTBA entered into a joint venture with a for-profit auction company, and later formed wholly owned corporation, to conduct thoroughbred horse auction sales in California. The Service sought to tax CTBA’s distributive share of the profits of the joint venture as unrelated business taxable income under § 511, relying on § 1.513-1(d)(2) to assert that the auction sales bear no causal relationship to the advancement of CTBA’s exempt purpose. The Tax Court looked to § 1.501(c)(5)-1(a)(2) to define the exempt purposes of a § 501(c)(5) organization as “the betterment of the conditions of those engaged in [labor, agricultural, or horticultural] pursuits, as well as the improvement of their products.” The court concluded that CTBA’s objectives of encouraging, assisting, regulating and protecting the breeding of thoroughbreds in California is an exempt purpose under § 501(c)(5), and that the auction sales were substantially related to those purposes, saying that “the size of the state, the scattering of breeders throughout the state, the history of unreliable auction sales conducted by private commercial operations, the inherent importance of petitioner’s auctions to the operation of the industry, and the benefits achieved by the industry because of the auctions, all establish that the auction sales are indeed substantially related to CTBA’s objectives.” The court noted that “petitioner itself is not buying and selling the product, but providing an outlet for its members to do so. Of particular interest is that the industry had no comparable commercial outlet available for such services. Had petitioner not organized such sales, the industry as a whole would undoubtedly have floundered [sic], with the result that the California horses would have remained undermarketed and underpriced.”

As an organization described in § 501(c)(3), Organization is subject to the tax imposed by § 511 on its unrelated business taxable income (as defined in § 512). Generally, gross income of an exempt organization is includible in the computation of unrelated business taxable income if: (1) is it income from trade or business; (2) such trade or business is regularly carried on; and (3) the conduct of such trade or business is not

substantially related (other than through the production of funds) to the organization's performance of its exempt functions. See § 1.513-1(a).

Organization derives gross income from the sale of

to the public (the " sales"). These sales are conducted continuously through print and web-based catalogs and from located at

and other retail locations in a manner, and with regularity, similar to that of non-exempt suppliers. Organization does not dispute that its sales are a trade or business or that they are regularly carried on. Therefore, the gross income from Organization's sales will not be excluded from unrelated business taxable income unless such sales are substantially related to Organization's exempt purpose within the meaning of § 1.513-1(d). Also see § 1.513-1(b).

Organization is organized for the purpose of

. To find that the sales are substantially related to Organization's exempt purpose within the meaning of § 513, the sales activities must contribute importantly to the accomplishment of that purpose. See § 1.513-1(d)(2). Organization maintains that its sales contribute importantly to its exempt purposes by serving educational, charitable, and scientific functions.

Even though Organization's research and educational activities are substantially related to Organization's exempt purposes, the fact that the sales are conducted in conjunction with, or (in the case of its online catalog) through the same vehicles (e.g., the website) as, Organization's exempt activities does not compel a conclusion that the sales, too, are substantially related. The sales do not lose their separate identity as a trade or business merely because they are carried on within the larger context of as part of Organization's functions. See § 1.513-1(b). Therefore, to determine whether the sales are substantially related (other than through the production of funds) to the purposes for which exemption was granted to Organization, it is necessary to examine the relationship between those sales, as a separate trade or business, and the accomplishment of Organization's exempt purposes. See § 1.513-1(d)(1).

Organization posits that the sales contribute importantly to its educational function in that they may encourage buyers to visit its visitor center or the educational pages of its website. Organization points specifically to a reference, printed of each package, to its website and, furthermore, notes that customers who order online and provide their email addresses during checkout will subsequently receive periodic educational newsletters via email. In Rev. Rul. 73-104, an art museum sold greeting cards that display reproductions of art work and that are imprinted with the name of the artist, the title or subject matter of the work, the date and period of its

creation, and the name of the museum. The Service concluded that the sales of greeting cards contribute importantly to the achievement of the museum's educational purposes by stimulating and enhancing public awareness, interest, and appreciation of art, and by encouraging a broader segment of the public to visit the museum. The mere reference on a package to another, separate activity or function of the Organization, in this case, the educational portion of its website does not render the package itself "educational" or cause the sales, as a separate trade or business, to "contribute importantly" to the accomplishment of Organization's educational purpose within the meaning of § 1.513-1(d)(2). Likewise, the fact that a piece of information, such as a customer's e-mail address, is acquired in the course of a commercial endeavor and used in the conduct of exempt educational functions such as to include in the e-newsletter mailing list does not, by itself, make the commercial endeavor of sales substantially related to exempt functions; this is because visitors to Organization's website can sign up online to receive Organization's e-newsletters without purchasing . The test, instead, is whether the activity of selling , in and of itself, contributes importantly to the accomplishment of Organization's educational purposes. See § 1.513-1(d)(4)(iii).

The greeting cards described in Rev. Rul. 73-104 are different from the offered for sale by Organization. In the case of Rev. Rul. 73-104, the thing sold – i.e., the greeting card – bears a reproduction of an original work of art. A person looking at the greeting card sees an image of the work itself, and is thus exposed to all of the "information" conveyed by the original. In addition, since the greeting card reproduces a unique work in the possession of one museum, a person looking at the card is more likely to be encouraged to visit that museum to see the original and other work in the museum's collection.

In the case of the sales, on the other hand, the thing sold – i.e., the – do not impart any information at all, while the package, with its instructions on how to as well as a sentence or two concerning , imparts little that could not also be found on packages offered by commercial . Significantly, there are no instructions or other information on the package about how to or how to . Therefore, we conclude that Organization's sales do not contribute importantly to the educational purpose of preserving and conserving

Organization states that the sales further its charitable purpose of preserving and protecting the environment for the benefit of the public, similar to Rev. Rul. 76-204 (holding that an organization that acquires and preserves ecologically significant undeveloped land is operated exclusively for charitable purposes). However, the facts here are more similar to those described in Rev. Rul. 78-384 (holding that an organization that operates a farm and merely restricts the land to uses that do not

change the environment is not preserving land that has any distinctive ecological significance within the meaning of Rev. Rul. 76-204). Organization does not claim that its _____ occupies ecologically significant land, nor, more importantly, that the _____ and selling the _____ serve in any way to preserve land that has ecological significance.

We recognize that Organization's purpose to conserve _____

_____ is charitable and educational. See, e.g., Rev. Rul. 66-179, supra. We also recognize that many of Organization's conservation "strategies" — developing _____

_____, teaching _____, and inspiring _____, and facilitating the sharing of _____ — are in furtherance of that exempt purpose. However, Organization has not shown that selling large quantities of _____ is necessary to preserve _____

Organization states that another of its conservation strategies of encouraging companies to sell _____ is also in furtherance of the same exempt purposes, and that its _____ sales are necessary to effectuating that strategy. Specifically, Organization maintains that the establishment of a successful _____ catalog _____

_____ is an example of a market-driven conservation model, which anticipates that the for-profit _____ industry will supply more _____, thus making _____ less scarce, if another institution can demonstrate a demand for the resource. Organization reasons that its _____ sales contribute importantly to its scientific and charitable purpose of conserving _____ by establishing market demand and thus incentivizing other _____ companies to carry _____

However, there are already commercial _____ companies selling _____

Further, the development of a product in connection with a commercial operation does not necessarily further scientific purposes under § 501(c)(3). See, e.g., Rev. Rul. 65-1 (holding that an organization which promotes and fosters the development and design of machinery incident to commercial operations does not qualify for exemption under § 501(c)(3)). Organization compares its _____ sales to the horse auctions conducted by the petitioner ("CTBA") in California Thoroughbred Breeders Ass'n v. Comm'r, T.C. Memo 1989-342. Organization maintains that both it and CTBA are "_____

_____, and that both seek "to provide a superior product to the public." However, California Thoroughbred Breeders Ass'n involved an organization exempt under § 501(c)(5), not one exempt under § 501(c)(3). Section 1.501(c)(5)-1(a)(2)

provides that an organization described in § 501(c)(5) has as its object the betterment of the conditions of those engaged in labor, agricultural, and horticultural pursuits, the improvement of the grade of their products, and the development of a higher degree of efficiency in their respective occupations. In finding that “had petitioner not organized such sales, the industry as a whole would undoubtedly have floundered [sic], with the result that the California horses would have remained under-marketed and underpriced,” the Tax Court concluded that the auction sales bettered the conditions of thoroughbred breeders and improved the grade of their products, and heightened the efficiency of their occupations consistent with § 501(c)(5). Furthermore, the Tax Court discerned a difference between selling a product directly and conducting an auction. In explaining its reasons for concluding that CTBA’s activities “better the conditions of those engaged in [thoroughbred breeding] pursuits” the court noted that “[CTBA] itself was not buying and selling the product but providing an outlet for its members to do so.” Conversely, Organization’s sales go beyond “providing an outlet” for its members to share , but entail direct sales to the public. In determining whether Organization’s sales are substantially related to § 501(c)(3) purposes, the question is not whether the sales better conditions in, or improve the grade of products of a particular industry; It is whether they contribute importantly to Organization’s charitable and scientific purpose of . Organization has failed to demonstrate that they do.

The sales are not aimed at interested in working to preserve, multiply, and spread unique and threatened , nor to people wishing to start or participate in . Rather the are marketed and sold to the public in a manner similar to that of other purveyors of , and, thus, are likely to be used for the same purpose as sold by other purveyors – i.e., to , not preservation. Therefore, we conclude that there is no substantial causal relationship between the sales and Organization’s exempt purposes of conserving and preserving .

Finally, the sold to the public through the catalog and are not “products which result from the performance of exempt functions” as described in § 1.513-1(d)(4)(ii).

Rev. Rul. 78-145 holds that blood bank sales of by-product plasma (which is what remains of whole blood after the red cells have been extracted to meet the demands of hospitals for red blood cell transfusion) and salvage plasma (which is plasma extracted from units of whole blood which are no longer fresh enough for transfusions because their shelf-life has expired) to commercial laboratories does not give rise to unrelated trade or business income, assuming that the amount of whole blood maintained in inventory is not excessive in view of the expected needs of the hospitals served by the blood bank. On the other hand, gross income derived from the sale to commercial

laboratories of plasma obtained from other blood banks or drawn from individual donors does give rise to unrelated business taxable income.

By analogy, if the _____ sold through the _____ catalog are merely the “by-products” or the “remains” of _____ in the course of the performance of Organization’s preservation functions in furtherance of exempt purposes (assuming that the amount of _____ is not excessive in view of the expected requirements of such functions), gross income from the sale of such by-product or _____ would not be gross income from the conduct of unrelated trade or business. On the other hand, if the _____ sold are not products that result from the performance of Organization’s preservation functions, as would be the case if the _____ were _____ specifically for sale, the _____ sales would constitute unrelated trade or business.

Organization needs to _____ to effectuate its preservation strategies in furtherance of its exempt function of preserving _____. Specifically, Organization needs to _____ to maintain its _____, stock its _____, and provision its members, volunteers and other persons who are interested in preserving _____ through Organization’s preservation and conservation projects, _____. Where the quantity of _____

_____, is reasonable in relation to the requirements of Organization’s conservation strategies, income from the disposition of the _____ does not constitute unrelated trade or business. However, where the _____ is conducted on a larger scale than is reasonably necessary to effectuate such strategies, the gross income attributable to the _____ in excess of the needs of exempt functions constitutes gross income from the conduct of unrelated trade or business. See § 1.501(c)(3)-1(d)(3).

The facts show that the _____ offered for sale through the catalog and _____ are not the mere “by-products” or “remains” of _____ in the course of the performance of Organization’s conservation functions, but, instead, are the product of _____ produced in a business venture which sees Organization _____ the quantity of _____ necessary to have sufficient stock on hand to sustain a commercially viable and profitable _____ business. This quantity of _____ is in excess of the quantity of _____ necessary to effectuate the Organization’s preservation strategies in furtherance of its exempt function of preserving _____. Therefore, because the _____ is _____ conducted on a larger scale than is reasonably necessary for performance of Organization’s exempt functions, the _____ for sale are not considered

products which result from the performance of exempt functions under § 1.513-1(d)(4)(ii). Consequently, the gross income attributable to the sales constitutes gross income from the conduct of unrelated trade or business.

CAVEAT(S):

A copy of this technical advice memorandum is to be given to the taxpayer(s). Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.