



Department of the Treasury  
Internal Revenue Service  
P.O. Box 2508  
Cincinnati, OH 45201

Release Number: **201714031**  
Release Date: 4/7/2017

Date: January 9, 2017

Employer ID number:

Contact person/ID number:

Contact telephone number:

Form you must file:

Tax years:

UIL: 501.32-00, 501.33-00, 501.36-00

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

This letter 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). Recently, we sent you a proposed adverse determination in response to your application. The proposed adverse determination explained the facts, law, and basis for our conclusion, and it gave you 30 days to file a protest. Because we didn't receive a protest within the required 30 days, the proposed determination is now final.

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

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

We'll also notify the appropriate state officials of our determination by sending them a copy of this final letter and the proposed determination letter (under Section 6104(c) of the Code). You should contact your state officials if you have questions about how this determination will affect your state responsibilities and requirements.

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 our customer service number 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,

Jeffrey I. Cooper  
Director, Exempt Organizations  
Rulings and Agreements

Enclosures:

Notice 437

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

Redacted Letter 4038, *Final Adverse Determination Under IRC Section 501(c)(3) - No Protest*



**Department of the Treasury  
Internal Revenue Service**

P.O. Box 2508  
Cincinnati, OH 45201

**Date: November 15, 2016**

**Employer ID number:**

**Contact person/ID number:**

**Contact telephone number:**

**Contact fax number:**

**Legend:**

B = Date of formation

C = State

D = Program

F = LLC

G = Secretary

H = President/Director

j dollars = Amount

k dollars = Amount

**UIL:**

501.32-00

501.33-00

501-36-00

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

We considered your application for recognition of exemption from federal income tax under Section 501(a) of the Internal Revenue Code (the Code). Based on the information provided, we determined that you don't qualify for exemption under Section 501(c)(3) of the Code. This letter explains the basis for our conclusion. Please keep it for your records.

**Issues**

Do you qualify for exemption under Section 501(c)(3) of the Code? No, for the reasons stated below.

**Facts**

You were incorporated on B in the State of C. Your stated purposes, in part, are to act and operate as a charitable organization in lessening the burdens of government, providing relief to the poor and distressed or underprivileged, and promoting social welfare by health and wellness intervention to teach muscle management for a healthy back.

You teach muscle management with a program which detects muscle asymmetry and teaches therapeutic stretching exercises to heal chronically injured muscles and reduce back pain. You teach core muscle exercises to tone the back muscles so that they can then be strengthened and conditioned to make the back healthy and more strain resistant.

F is a for-profit organization that holds the intellectual property, a program called D, which you use for training purposes. The program name, D, is also included in your name and is also an integral part of the name of F.

F will train the D instructors, personal trainers and group exercise instructors which will work with your students in private. You will teach students, coaches and health teachers the D program. The program teaches

optimal therapeutic stretching techniques to rehabilitate core muscles of the back and neck and keeps muscle movement symmetrical.

G is your Secretary and a paid consultant. G is the individual that developed the D program. H is your President and a director. G and H are brothers. Your Treasurer is H's sister. One of your directors is a work associate of H. You have one governing body member, a director, unrelated to the others.

You provided what was purportedly your website address on your initial application. The website has copyright information in the name of F at the bottom of each page. It discusses the D program and indicates that it was designed to help people avoid needless reoccurring lower back pain, upper back pain, and shoulder and neck pain due to muscle strain. It further indicates that D was the first new scientific breakthrough for back pain in 100 years. The website gives locations and times for private consultations and classes. G wrote a book promoted by you and also for sale on the site. Later, when asked about your website, you said that it belongs to F. The website states that F has been operational for almost ten years.

The for-profit company F is owned by H. You said in your initial application that you will purchase books, e-books and phone apps from F. You later said that you own all rights to the intellectual property and therefore will have direct control over wholesale distribution. Per our request, you provided clarification regarding this discrepancy. You said that you will buy books, e-books and apps from F at wholesale prices. You further indicated that G owns the copyright and since his position on the board is Secretary/Consultant, he will be donating his royalties for intellectual properties to you. You said you have a contract with G, but you did not provide a copy.

You said that F has an exclusive license agreement with G. You said you are not planning to interact with for-profit entities, except F, to purchase material for classes and managing online sales. You further restated there will be no activities which benefit the for-profit entity. The only benefit for F is that it will realize the possible cost reduction in buying teaching materials in larger quantities. There will be no payments for services to F. F will not be compensating H when he teaches for you.

When asked how you are distinguishable from F from the public's perspective you indicated, "The non-profit customers will have a code to purchase materials at wholesale costs."

The website, which you state belongs to F, indicates that the classes are j dollars per class, which includes the D program Book/DVD. When asked about how much you will charge for classes, you said class fees are k dollars, which is more than the class offered by F (according to their website). You said the fee includes a book or e-book and a phone app. The fee pays the instructor and includes the wholesale prices for the class material. You said you are not collecting fees at this time.

H has been teaching classes through F and promoting the book that was written by G. When asked for a list of duties for each compensated individual, including the number of hours each individual works for both you and any other entity, you said that H will be managing both F and you. G is a consultant for both organizations. There are no other individuals working for both you and F. The details we requested regarding the hours worked and duties performed were not provided.

Additionally, when asked what portion of F's overall revenue would be received through your activities you said that the percentage of the for-profit's overall sales are going to be determined by how many schools and other non-profit organizations purchase classes and materials.

When asked if you share a physical space, address or employees with any for-profit organizations you said, "I work out of my home at the present time. In the future there will need to be employees and instructors working for both the LLC and non-profit." No other information was provided.

You said the wholesale prices of the materials are about half of the regular general public price. The wholesale price is the amount you will pay to obtain the materials for resale. When asked for the price that you will pay for materials that will be purchased from F, you did not submit this information.

In your initial application you stated that you plan on seeking funds through email, personal, and website solicitations as well as foundation and government grants. You provided projected financial data with your initial application which included compensation for G and H. For the first two years of your operations, you project that 70% of your total revenue will be used to compensate G and H. You anticipate that your revenue will double in your third year of operations and that 45% of that revenue will be used to compensate G and H with another 25% being allocated for an additional instructor.

We requested a specific breakdown of each type and amount of revenue you have received since your formation and that you plan to receive. To this request you replied, "The non-profit will be soliciting grant money to teach firefighters, police officers, school personnel and school athletic teams." No additional information was provided.

#### **Law**

Section 501(c)(3) of the Code provides, in part, for the exemption from federal income tax organizations organized and operated exclusively for charitable, religious or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Treasury Regulation Section 1.501(c)(3)-1(a)(1) states that, in order to be exempt as an organization described in Section 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Treas. Reg. Section 1.501(c)(3)-1(c)(1) provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more such exempt purposes specified in Section 501(c)(3) of the Code. 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. Section 1.501(c)(3)-1(c)(2) provides that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals.

Treas. Reg. Section 1.501(c)(3)-1(d)(1)(ii) provides an applicant must show that it serves a public rather than a private interest and specifically that it is not organized or operated for the benefit of private interests, such as

designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Rev. Rul. 80-287, 1980-2 C.B. 185, involved a nonprofit lawyer referral service that arranged, at the request of any member of the public, an initial half-hour appointment for a nominal charge with a lawyer whose name was on an approved list maintained by the organization. As a general rule, providing services of an ordinary commercial nature in a community, even though the undertaking is conducted on a nonprofit basis, is not regarded as conferring a charitable benefit on the community unless the service directly accomplishes one of the established categories of charitable purposes. The organization's activities were directed toward assisting individuals in obtaining preventive or remedial legal services and, as such, were not specifically designed to confer a charitable benefit on the community. Although the lawyer referral service provided some public benefit, a substantial purpose of the program was promotion of the legal profession.

Rev. Proc. 2016-5 provides that a favorable determination letter or ruling will be issued to an organization only if its application and supporting documents establish that it meets the particular requirements of the section under which exemption from federal income tax is claimed. The organization must fully describe all of the activities in which it expects to engage, including the standards, criteria, procedures, or other means adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures. Where the organization cannot demonstrate to the satisfaction of the Service that it qualifies for exemption pursuant to the section of the Code under which exemption is claimed, the Service will generally issue a proposed adverse determination letter.

In Better Business Bureau of Washington, D.C. v. U.S., 326 U.S. 279, 283, 66 S. Ct. 112, 90 L. Ed. 67 (1945), the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes.”

In Old Dominion Box Co. v. United States, 477 F. 2d 340 (4th Cir. 1973), cert. denied 413 U.S. 910 (1973), the Fourth Circuit held that operating for the benefit of private parties constitutes a substantial nonexempt purpose.

In est of Hawaii v. Commissioner, 71 T.C. 1067 (1979), several for-profit est organizations exerted significant indirect control over est of Hawaii, a nonprofit entity, through contractual arrangements. The Tax Court concluded that the for-profits were able to use the nonprofit as an “instrument” to further their for-profit purposes. Neither the fact that the for-profits lacked structural control over the organization nor the fact that amounts paid to the for-profit organizations under the contracts were reasonable affected the court's conclusion that the organization did not qualify as an organization described in Section 501(c)(3) of the Code.

Bubbling Well Church of Universal Love, Inc. v. Commissioner, 74 T.C. 531 (1980), provides that an application for tax-exempt status “calls for open and candid disclosure of all facts bearing upon [an Applicant's] organization, operations, and finances to assure [that there is not] abuse of the revenue laws.” Further, in the absence of such disclosure, “the logical inference is that the facts, if disclosed, would show that the [Applicant] fails to meet the requirements of [Section] 501(c)(3).”

In Church by Mail, Inc. v. Commissioner, T.C. Memo 1984-349, affd 765 F. 2d 1387 (9th Cir. 1985) the court upheld that an organization operated for the substantial non-exempt purpose of providing a market for a for-profit corporation was not exempt under Section 501(c)(3) of the Code. In this case, a non-profit organization was formed to promote religion through the distribution of printed religious messages. The non-profit

organization was related to a for-profit corporation that provided the printing and mailing services for the non-profit organization. The for-profit corporation also provided similar services to others as part of its normal commercial operations. The court determined that the non-profit organization was operated for the non-exempt purpose of providing a market for the for-profit corporation's services and that this non-exempt purpose would preclude exemption under Section 501(c)(3) of the Code.

In International Postgraduate Medical Foundation v. Commissioner, TCM 1989-36 (1989), the Tax Court considered the qualification for exemption under section 501(c)(3) of the Code of a nonprofit corporation that conducted continuing medical education tours. The petitioner had three trustees: Mr. Helin, who was a shareholder and the president of H & C Tours, a for profit travel agency, Mr. Regan, an attorney, and a third director, who was ill and did not participate. The petitioner used H & C Tours exclusively for all travel arrangements. There is no evidence that the petitioner ever sought a competitive bid. The Court found that a substantial purpose of the petitioner was benefiting the for-profit travel agency. It concluded that: "When a for-profit organization benefits substantially from the manner in which the activities of a related organization are carried on, the latter organization is not operated exclusively within the meaning of section 501(c)(3), even if it furthers other exempt purposes." The court found that a substantial purpose of the applicant's operations was to increase the income of H&C Tours. H&C Tours benefits from the distribution and production of brochures which solicit customers for tours arranged by H&C Tours.

In New Dynamics Foundation v. United States, 70 Fed. Cl. 782, 798 (Fed. Cl. 2006), the U.S. Court of Federal Claims held that the Service properly denied tax exempt status under Section 501(c)(3) to a nonprofit corporation that was organized to promote and contribute to charitable causes. In reaching this conclusion, the court stated, "It is well-accepted that, in initial qualification cases [any] gaps in the administrative record are resolved against the applicant," adding that courts "can draw inferences adverse to a taxpayer seeking exempt status where the taxpayer fails to provide evidence concerning its operations, or where the evidence is vague or inconclusive."

#### **Application of law**

You are not described in Section 501(c)(3) of the Code or Treas. Reg. Section 1.501(c)(3)-1(a)(1) because you fail the operational test. Specifically, the facts show you are not operated exclusively for Section 501(c)(3) purposes, but for the substantial non-exempt purpose of facilitating sales for the benefit of your governing body members, G and H.

You are not operated exclusively for an exempt purpose as described in Treas. Reg. Section 1.501(c)(3)-1(c)(1). Operating for the benefit of private parties, such as G and H, constitutes a substantial non-exempt purpose as illustrated in Old Dominion. The presence of a single non-exempt purpose, if substantial in nature, will destroy a claim for exemption regardless of the number or importance of truly exempt purposes. Treas. Reg. Section 1.501(c)(3)-1(d)(1)(ii).

You are similar to the organization described in International Postgraduate Medical Foundation. The majority of your board is related. H owns the related for-profit entity, F, and G is the author of the materials promoted by you. H and G benefit substantially from the manner in which your activities are conducted. Like the organization described in this case, you are not operated exclusively for exempt purposes within the meaning of Section 501(c)(3). Your activities inure to the benefit of G and H as described in Treas. Reg. Section 1.501(c)(3)-1(c)(2). G and H are both compensated and their salaries consume a large portion of your revenue. Prior to your formation, F would sell the books, e-books and apps to the general public for a certain price. You

were formed to purchase those materials from F and resell them to those interested in your programs. G is the author of the book, holds the copyright and is the one that designed the D program. Your promotion of the D program, which benefits G and H directly, creates inurement, which causes you be precluded from exemption under Section 501(c)(3) of the Code.

Like the organization described in Rev. Rul. 80-287, your activities directly promote and facilitate the sale of products by a for-profit organization. You are similar to the organization in est of Hawaii because you are dependent on one for-profit entity, F, for your operations. Without the materials you purchase from F, you would have no program. You are similar to Church by Mail, because you provide a market for the for-profit business and you are promoting the for-profit business.

According to Better Business Bureau, a single non-exempt purpose will destroy exemption. You have a substantial non-exempt purpose of promoting the D program through the purchase of books, e-books and apps from the related for-profit entity, precluding you from exemption. You are marketing the same program, D, as the for-profit, F. You serve the same purpose as F, provide the same educational services, have a very similar name and share a website with F. You and F are virtually indistinguishable. In fact, you indicated the only difference between you and F, from the public's perspective, is that the individuals buying materials through you get a discount code to use at checkout.

We asked for specific details regarding your activities and financial data to which you provided vague generalities, some contradictory information, and to some of our specific requests your response was silent. An organization has the burden of proof to describe its activities to sufficient detail to permit the Service to determine whether it meets the definition of the Code section under which exemption is sought. As explained in Bubbling Well, when details regarding financial data and activities are sought and the organization does not provide that information, the logical inference is that if the requested information was provided, the organization would not qualify for exemption.

In addition, New Dynamics explains that in initial application cases, any gaps in the administrative record are resolved against the applicant, especially in cases where the applicant fails to provide evidence concerning its operations, or where the evidence is vague or inconclusive. You have failed to fully describe all of your activities in which you expect to engage, including the standards, criteria, procedures, or other means planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures as required by Rev. Proc. 2016-5. Therefore, you are not entitled to exemption under Section 501(c)(3) of the Code.

### **Your position**

You feel you qualify for exemption since none of the directors or officers will receive financial benefits outside of a salary for services rendered. You will buy self-published teaching materials and resources wholesale directly from the publisher. You also state that the phone apps and e-books will have a code that allows students and teachers to download the products at wholesale costs.

You also stated that back pain is the number one cause of disability in the world. H personally instructs the D program at schools in health classes and the physical education department and teaches patients at a medical clinic. This educational program has the potential to help many individuals develop a healthy back for life and prevent needless suffering and economic loss.



### **Our response to your position**

You were formed to promote the business of F and to promote a book written by G. H owns F and you will be purchasing books, e-books and apps from F. Both G and H are benefiting substantially from the promotion and sale of the books, e-books and apps that will be purchased F.

### **Conclusion**

You do not qualify for exemption under Section 501(c)(3) of the Code because you fail the operational test. You conduct activities which are indistinguishable from the for-profit's activities. Your activities further substantial non-exempt purposes and cause inurement to G and H. Additionally, you failed to provide the details we requested regarding your activities. Therefore, you are not exempt under Section 501(c)(3).

### **If you don't agree**

You have a right to file a protest if you don't agree with our proposed adverse determination. To do so, you must send a statement to us within 30 days of the date of this letter. The statement must include:

- Your name, address, employer identification number (EIN), and a daytime phone number
- A copy of this letter highlighting the findings you disagree with
- An explanation of why you disagree, including any supporting documents
- The law or authority, if any, you are relying on
- The signature of an officer, director, trustee, or other official who is authorized to sign for the organization, or your authorized representative
- One of the following declarations:

**For an officer, director, trustee, or other official who is authorized to sign for the organization:**

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

**For authorized representatives:**

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

Your representative (attorney, certified public accountant, or other individual enrolled to practice before the IRS) must file a Form 2848, *Power of Attorney and Declaration of Representative*, with us if he or she hasn't already done so. You can find more information about representation in Publication 947, *Practice Before the IRS and Power of Attorney*.

We'll review your protest statement and decide if you provided a basis for us to reconsider our determination. If so, we'll continue to process your case considering the information you provided. If you haven't provided a

basis for reconsideration, we'll forward your case to the Office of Appeals and notify you. You can find more information about the role of the Appeals Office in Publication 892, *How to Appeal an IRS Decision on Tax-Exempt Status*.

If you don't file a protest within 30 days, you can't seek a declaratory judgment in court at a later date because the law requires that you use the IRS administrative process first (Section 7428(b)(2) of the Code).

**Where to send your protest**

Please send your protest statement, Form 2848, if needed, and any supporting documents to the applicable address:

U.S. mail:

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

Street address for delivery service:

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

You can also fax your statement and supporting documents to the fax number listed at the top of this letter. If you fax your statement, please contact the person listed at the top of this letter to confirm that he or she received it.

**If you agree**

If you agree with our proposed adverse determination, you don't need to do anything. If we don't hear from you within 30 days, we'll issue a final adverse determination letter. That letter will provide information on your income tax filing requirements.

You can find all forms and publications mentioned in this letter on our website at [www.irs.gov/formspubs](http://www.irs.gov/formspubs). If you have questions, you can contact the person listed at the top of this letter.

Sincerely,

Jeffrey I. Cooper  
Director, Exempt Organizations  
Rulings and Agreements

Enclosure:  
Publication 892